TAX REFORM IN LATVIA IN 2018

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Introduction

The Tax Reform in Latvia has entered into force as of January 1, 2018.

The Ministry of Finance has been working on proposals on reforming the tax system of Latvia for more than a year in close collaboration with the governmental and non-governmental sectors, as well as the World Bank and the OECD. After reviewing more than 300 proposals, the government has approved in total 12 laws associated with the tax reform.

The tax policy reform makes workforce expenses similar to those in the other Baltic States, promotes the competitiveness on a regional level and the motivation to start business, invest in a company development, attract investors, pay taxes.
New corporate tax regime

As from this year, a new corporate tax regime – the reinvested profit model – is introduced, meaning that the tax is suspended until profits are distributed or used for purposes other than ensuring the company’s further development. Reinvested profits are not taxed, but the rate on distributed profits is 20%. Until now the corporate income tax rate was 15%. Dividends are henceforth taxed at corporate level at a 20% rate, therefore natural persons no longer have to pay personal income tax on the dividends they receive.
As regards a tax relief for donations to social organisations, companies have a choice of three options:

1) reduce taxable profits by the donated amount, but not more than 5% of total profit in the previous year;

2) reduce the taxable profit by an amount not exceeding 2% of the total gross salaries paid to employees in the previous year from which the social tax has been paid;

3) reduce the tax on dividends by 75% of profits, but not more than by 20% of the calculated tax.

Furthermore, the new tax regime provides that, as of 1 July 2018, corporate income tax will no longer have to be paid in advance. A two years transition period has been set for distributing previously accumulated profits, to which a 10% personal income tax applies.

Amendments to the microenterprise tax regime provide that companies operating within the regime will further pay a uniform rate of 15% of turnover, whereas the maximum turnover is reduced from the current EUR 100 000 to EUR 40 000 per year. In accordance with the amendments, as of 1 January 2019, employees of microenterprises will only be allowed to work in one microenterprise.

The turnover threshold at which economic operators must register with the State Revenue Service as value added taxpayers is now reduced from EUR 50 000 per year to EUR 40 000. The threshold for indicating a breakdown of VAT transactions is reduced to EUR 150 from the current EUR 1430.

As of 2018, the reverse charge VAT applies to a broader range of industries and further includes the delivery of gaming consoles and home appliances, the delivery of construction materials and metal products and related services.

A special law has been adopted to allow natural and legal persons to repay outstanding tax debts, stipulating that as of 1 January 2018 the State Revenue Service may dismiss accumulated late fees and fines.

**Labour taxes from 2018**

As to the labour taxes starting from this year, the minimum monthly salary raises from the current EUR 380 to EUR 430. The maximum differentiated tax allowance for the personal income also increases – from EUR 115 to EUR 200, further raising to EUR 230 in 2019 and EUR 250 in 2020. The untaxable minimum will gradually reduce depending on total income and will not apply to the income exceeding EUR 1000 per month in 2018, EUR 1100 per month in 2019, and EUR 1200 per month in 2020. This year the untaxable minimum for pensions raises from the current EUR 235 per month to EUR 250, reaching EUR 270 in 2019 and EUR 300 in 2020. The untaxable minimum applies directly without submission of the annual income declaration.
Changes in personal taxes

As of 1 January 2018, the application of personal income tax is differentiated with a progressive rate of 31.4% being applied to the portion of income exceeding EUR 55,000 per year. In turn, the annual income up to EUR 20,000 per year will be subject to 20% tax rate, and the income between EUR 20,000 and EUR 55,000 per year will be subject to 23% rate. A higher tax rate – 20% instead of the current 10% or 15% - applies to the income from the capital and capital gains.

A tax relief for dependent increases from the current EUR 175 to EUR 200 per month, reaching EUR 230 in 2019 and EUR 250 in 2020.

For natural persons the total amount of eligible expenses for health care, education and donations as from this year is EUR 600 per year per family member, but not exceeding 50% of total taxable annual income. Until now, the maximum amount of eligible expenses per year was set at EUR 215 for education and medical services, whereas there was no limit set for dentistry and planned surgeries. As regards private pension funds and life insurance premiums, the redeemable amount is now limited to 10% of taxable annual income, but not exceeding EUR 4000 per year.

As from this year, the rate for patent fees also changes to EUR 50 or EUR 100 per month instead of the current EUR 43 to EUR 100. As of 1 January, persons with Group I and II disabilities are allowed to pay a reduced patent fee.

The social contribution rate for both employers and employees raises by 0.5% this year. Furthermore, 1% of the state social insurance mandatory contributions are earmarked for the health care. The use of funds allocated for health care services is regulated by a law on health care financing.

As of 2018, mandatory social insurance contributions have to be paid also from royalties. The payer of a royalty has to pay a 5% social contribution for the recipient, and these contributions are paid into the person’s pension insurance.

Mandatory contributions of at least 5% also have to be paid by economic operators if their monthly income does not exceed EUR 430. For higher monthly income, social contributions of 32.13% have to be made from a freely chosen portion of income (but no less than the national minimum salary, i.e. EUR 430), and at least 5% of the difference between the chosen amount and actual income has to be paid into pension insurance. In turn, the operators whose total annual income does not exceed EUR 50 are exempt from social contributions.

Combatting the shadow economy

In order to compensate the loss in the state and municipal budgets due to the tax reform, the gambling tax and excise duties increase from this year. The established compensation mechanisms pertain to combatting the shadow economy and improving the tax administration. On top of it the new regulations stipulate an annual obligation
for credit institutions and payment service providers to submit to the State Revenue Service information about natural persons, whose account turnover has exceeded EUR 15 000 in the previous year.

Campaign about tax reform

In the end of 2017, the State Revenue Service organized 76 free of charge seminars for taxpayers about the tax reform of 2018 which were attended by more than 4842 visitors including 22 co-operation industry associations. In the beginning of 2018 two round-table discussions with journalists have taken place. For a better perceptibility of information 3 animated video materials and infographics have been created and published on SRS website, Facebook, Twitter and Instagram.

Also this year SRS organizes an informative campaign about tax amendments in order to cover a possibly wide extension of audience.