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COUNTRY

Doing Business in
Latvia

Preface

This guide has been prepared by Baker Tilly Baltics SIA, an independent member of Baker Tilly International. It is designed to provide information on a number of subjects important to those considering investing or doing business in Latvia.

Baker Tilly International is the world's 8th largest accountancy and business advisory network by combined fee income, and is represented by 138 firms in 104 countries and over 24,000 personnel worldwide. Its members are high quality, independent accountancy and business advisory firms, all of whom are committed to providing the best possible service to their clients, both in their own marketplace and across the world.

This guide is one of a series of country profiles compiled for use by Baker Tilly International member firms' clients and professional staff. Copies may be obtained from Baker Tilly Baltics SIA or any of our independent member firms.

Doing Business in Latvia has been designed for the information of readers. Whilst every effort has been made to ensure accuracy, information contained in this guide may not be comprehensive and recipients should not act upon it without seeking professional advice. Facts and figures as presented are correct at the time of writing.

Up-to-date advice and general assistance on Latvian matters can be obtained from Baker Tilly Baltics SIA; contact details can be found at the end of this guide.

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Contents

1 Fact Sheet

Geography

Location	At the crossroads of Northern and Eastern Europe, on the east cost of the Baltic Sea
Area	64,589km^2
Land boundaries	Estonia (north), Lithuania (south), Russia and Belarus (east)
Coastline	494km
Climate	Temperate climate zone
Terrain	Flat
Time zone	GMT +2

People

Population	2.27 million
Ethnic groups	Latvians, Russians, Byelorussians, Ukrainians and others
Religion	Lutheran, Catholic and Orthodox
Language	Latvian

Government

Country name	Republic of Latvia
Government type	Parliamentary
Capital	Riga
Administrative divisions	Vidzeme, Zemgale, Kurzeme and Latgale
Political situation	Democratic

Economy

GDP – per capita	LVL6134
GDP – real growth rate	110.3%
Labour force	1.1 million
Unemployment	6%
Currency (code)	Lat (LVL)

2 Business Entities and Accounting

2.1 Corporate Entities

The permissible forms of business entities are stated in the Commerce Law and, with exception of self-employed traders, must be registered at the Commerce Registry.

2.1.1 Limited liability companies (SIA)

A SIA must be established by at least one member with a minimum share capital of LVL2000 contributed in cash or in-kind. When contribution in-kind exceeds LVL4000 or amounts to 50% or more of the share capital, it must be valued by a certified expert.

The board must consist of at least one member elected by the general meeting of shareholders (GMS) for up to three years (council is optional).

2.1.2 Stock corporations (AS)

An AS is a type of limited liability company formed to conduct certain businesses (banking, insurance) or for public trading of shares.

It may be established by one shareholder. Except for large-scale businesses, minimum initial share capital is LVL25,000.

A two-level management system exists within an AS:

- A council consisting of at least three members (five if shares are publicly traded) elected by the GMS for up to three years
- The council elects a board, consisting of at least one member, for up to three years.

2.1.3 Partnerships

There are two types of partnerships – general and limited – distinguished by the partners' liability.

A partnership *(līgumsabiedrība)* may be registered for VAT (not income tax) and acquires most legal rights and obligations, including property ownership. A partnership agreement is optional. A partnership may exist unregistered, but once it becomes a VAT payer, requires a commercial licence, or distributes gross profits to its partners, registration becomes mandatory.

2.1.4 Branches

A foreign branch *(filiāle)* or permanent establishment is a separate part of the head office undertaking. It is not a legal entity, but must be registered and obtain a domestic tax code.

Special rules apply to the taxation of a branch's profits and its allocation of expenses.

2.1.5 Representative offices

A representative office *(pārstāvniecība)* cannot trade, but must be registered and pay payroll taxes on behalf of the contracted employees.

2.1.6 Europe Economic Interest Groupings (EEIG)

An EEIG may be established by two persons performing principal activities within different member states.

2.1.7 Sole merchants

A sole merchant *(individuālais komersants)* is a private individual with annual sales over LVL200,000 or with five or more employees.

2.1.8 Agents, brokers and self-employed persons

Commercial agents, brokers and liberal professions (artists and providers of professional services) are often registered as self-employed *(pašnodarbinātais)* to reduce their tax burden.

2.2 Accounting

Accounting principles are provided by the Companies' Annual Reports Act and the recently introduced Latvian Accounting Standards which are largely based on International Financial Reporting Standards (IFRS). Bookkeeping is governed by the Accounting Act and a set of cabinet regulations.

All accounting transactions must be reflected in lats (LVL) as per the Bank of Latvia exchange rate on the day of transaction. At the year-end, all monetary assets and liabilities nominated in a foreign currency must be revalued using the exchange rate as at the last day of the fiscal year. Profits less losses arising from differences in exchange rates are taxable. Domestic transaction documents should be in Latvian.

2.3 Financial Reporting

The Companies' Annual Reports Act is based on the 4th and 7th EU Directives. The fiscal year covers a 12 month period and, unless specifically reported, coincides with the calendar year. Newly established businesses may opt for a longer fiscal year (of up to 18 months), while those changing their fiscal year start date or those in liquidation may adopt a shorter fiscal year.

Annual reports consist of financial statements (balance sheet, profit and loss statement, cash-flow statement and statement of changes in equity with explanatory notes) and a management report. The GMS approves the financial statements four months after the fiscal year-end (or seven months for companies subject to consolidation). Within one month of approval of the annual accounts and no later than four (or seven) months after the fiscal year-end, the annual report should be presented together with the auditor's report and consolidated statements (if required) to the tax authorities.

If two or more of the below criteria are exceeded, financial statements must be audited by sworn auditors or an auditing firm:

- Total assets – LVL250,000
- Net sales – LVL500,000
- Average number of employees – 25.

Consolidated accounts are required when the parent and subsidiaries exceed two or more of the following criteria over two successive years:

- Total assets – LVL1m
- Net sales – LVL2.4m
- Average number of employees – 250.

When a concern agreement is not publicly registered, a dependant company must prepare a dependency statement reflecting inter-company transactions and their financial impact.

3 Finance and Investment

3.1 Exchange Control

The lat is fixed to the euro at LVL0.702804 per euro.

Plans to introduce the euro in 2008 have been delayed.

3.2 Banking and Sources of Finance

The country's banking sector is supervised by the Financial and Capital Market Commission. Latvia's central bank, the Bank of Latvia, is charged with regulating currency in circulation by implementing monetary policy to maintain price stability.

There are 25 licensed commercial banks; foreign affiliates are mainly controlled by Scandinavian bankers.

3.3 Foreign Investment Incentives

- EU funding may be available for innovation and new product development.
- Various tax allowances are available on new technological equipment and also on the replacement and upgrade of obsolete machinery and technological equipment. In addition, in certain circumstances, the tax loss carry-forward period may be extended or even doubled, while training of newly recruited staff and the interest on borrowings may be compensated for by the State.
- Certain tax grants are available for non-EU traders at Riga and Ventspils free ports (80% rebates from standard 15% corporation tax) and at Liepaja and Rezekne special economic zones.
- Real estate tax rebate (25%-90%) may be provided by local municipalities.

3.4 Foreign Investment Restrictions

3.4.1 Acquisition of real estate

With the exception of protected zones and forests, foreigners may purchase Latvian real estate. Procedures may vary depending on the foreigner's residency and the status of the land.

There are no restrictions on the acquisition of city land by EU residents, but the purchase of rural land requires municipal approval until 2011. The simplest way to acquire land is through an EU-registered limited liability company.

3.4.2 Limitations for capital movement

Persons crossing an EU border to/from a non-EU country are required to declare cash in excess of €10,000.

Cash transactions between legal entities are subject to monthly restrictions and it may be necessary to report to the tax authorities. For cross-border transactions the amounts received/paid and the purpose of payment must be declared to the Bank of Latvia.

The domestic transfer of goods between domestic legal entities or between two locations of one entity is permitted only by common dispatch note invoice, which simultaneously serves as a VAT invoice. Special delivery notes are required for the transportation of timber products and alcoholic beverages.

4 Employment Regulation and Social Security

4.1 Entry Visa and Work Permit Requirements

4.1.1 Entry visas

Visas are mainly issued by consular missions of Latvia abroad. Documents for extending the duration of a stay may be arranged through any regional office of the Citizenship and Migration Affairs Bureau.

Citizens of the EU, EEA and Swiss Confederation do not require a visa. A visa-free regime is also available to visitors from certain other countries (see Appendix 1). Foreigners not requiring a visa can stay in Latvia for 90 days during a six-month period. Temporary or permanent residence permits are required beyond this term.

Latvia is a member of the Schengen zone.

4.1.2 Work permit requirement

To be a board or council member of a Latvian-registered company, or to receive remuneration for work performed in Latvia (including work on behalf of a foreign company for longer than six months), a work permit is required. The permit should be issued for a period of employment or a term of duties up to five years, and can be extended.

Work permits are not required for EU citizens.

4.2 Hiring Local Employees

The Latvian Labour Act complies with EU policies and is rigid.

The standard working week is eight hours per day and 40 hours per week. Vacations are four calendar weeks (excluding 15 days of state holiday) available after the first six months of employment. The maximum probation period allowed is three months.

Labour agreements must be produced in a prescribed format and are usually for an indefinite period of time. Employers have limited rights to terminate labour agreements.

The minimum age of workers is 18 years (in certain circumstances it is 15 years). The average annual gross salary in the private sector is LVL4,680. However, this does not reflect actual remunerations paid “off record” in many businesses due to the high burden of payroll taxes.

4.3 Trade Unions

Although trade unions have not been popular since the Soviet era, an increasing number of professions are now turning to unions to negotiate pay rises.

4.4 Social Security System

The social benefit system provides insurance for sickness, maternity, paternity, parent support, pension, disability, unemployment and accidents at work, although the majority of benefits are low. Insured persons are domestic and foreign individuals and sole traders.

Companies are liable for calculating and paying social security contributions of 33.09%, including that payable by employees (9%).

Companies are liable to an additional commerce risk levy (LVL0.25 per employee monthly) to ensure compensation is payable in the event of bankruptcy.

5 Taxation

5.1 Corporation Tax

A 15% corporation tax rate is imposed on the worldwide income of residents, with a few exceptions on dividends. The list of applicable tax treaties is provided in Appendix 2.

For tax purposes, assets (except intangible assets) are depreciated under the reducing balance method at the following rates:

Buildings and constructions	10%
Railway, marine and power equipment	20%
Electronic equipment	70%
Other (furniture, cars, equipment)	40%
Oil research and extraction equipment	15%

Luxury cars over LVL25,424 (net of VAT) and related expenses are not deductible for tax purposes. Related third-party transactions are interpreted according to OECD.

Tax losses can be carried forward in an historical order (oldest first) during five years (special rules apply to securities and the loss carry-forward period from 2010). Neither revaluation of assets nor income (losses) from publicly traded securities have any tax impact. The transfer of losses within a group is allowed.

5.2 Individual Tax

The worldwide income of residents and non-residents is taxed at 25%, with the exception of self-employed persons and liberal professions who are taxed at the rate of 15%.

Tax residents are:

- Citizens and permanent residents of Latvia
- Individuals present in Latvia for 183 days or more in any 12-month period starting or ending in the calendar year.

The following are deductible from income in arriving at the taxable amount:

- National social insurance paid by the employee
- Tax exempt minimum – LVL960 per annum
- Statutory allowances for each dependant – LVL672
- Medical costs and education expenses (up to LVL150 per annum); personal and dependant allowances, medical costs and education, applicable only for tax residents
- Dentist services (unlimited)
- Accumulative life insurance premiums, payments to private pension funds and investment fund certificates owned for more than 60 months (limited to 20% of taxable income per annum)
- Expenses related to art, music, literary, science, educational and similar works
- Donations to organisations approved by the government/cabinet (up to 20% of taxable income).

With the exception of sole traders and expatriates working for non-residents, employers are liable for tax compliance and payments.

5.3 Value Added Tax (VAT)

The delivery of goods, the supply of services, community acquisitions, import and self-consumption are chargeable to VAT. Local persons should be registered for VAT once their domestic taxable supplies reach LVL10,000 in a 12-month period or have EU purchases of LVL7,000 or more. It is possible to register prior to reaching these thresholds.

VAT rates are:

Most domestic sales and services, including intra-community acquisitions and third country imports (unless they are exempt or subject to reduced VAT)	18%
Hotel services, utilities for private individuals, medicals, baby food, books, magazines and newspapers	5%
Export and transit of goods, intra-community shipments to EU VAT-registered persons and most services provided to overseas taxpayers	0%

VAT payers may only recover VAT which is paid to generate VAT-taxable supplies. VAT related to exempt supplies is irrevocable. Input VAT should be adjusted in proportion to taxable and exempt supplies.

The taxable period is a calendar month; the VAT balance should be reported and paid monthly before the 15th of the following month. Invoices must be issued within 15 days from the delivery of goods/supply of services. Continuous services should be invoiced at least every six months. Output VAT is accounted upon receiving advance payments or delivery of goods/services.

The sales list of goods sold to the EU are submitted on a quarterly basis and are due by the 15th of the month following the quarter end. The requirement to submit intrastat declarations commences as soon as annual EU shipments exceed €98,000 or EU purchases exceed €65,000.

5.3.1 VAT compliance of foreigners

Reverse charge VAT is permitted on most services and deliveries to Latvian VAT payers. When an EU VAT payer conducts one of the following transactions with a VAT exempt person in Latvia, it should register for VAT:

- Distance sales exceeding €34,000 per annum
- Provision of services related to education, sport, culture, science and arts
- Provision of services related to real estate located in Latvia
- Delivery of excise goods
- Assembly and installation of goods
- Provision of services related to transportation, handling and storage of goods or any local sales.

Specific cases exist when local VAT registration may still be required upon domestic sales or the sale of inland goods to overseas, or the transfer of inter-company assets within the EU. In addition, third country residents (non-EU VAT payers) whose commerce involves telecommunications or movable assets in Latvia must register for VAT.

VAT refunds to EU traders without local fiscal presence are provided on a quarterly basis. The application should be supported with accounting vouchers verifying the VAT paid in Latvia and the home country VAT identity number.

5.4 Withholding Taxes

Profit repatriation is possible after withholdings taxes charged on various pre-tax payments to overseas:

Dividends, except dividends to EU tax residents taxed at 0%	Up to 10%
Management and consultancy fees	Up to 10%
Interest paid to related overseas parties (reduced rates of 5% and 0% will be applicable for EU companies during 2009 to 2013)	Up to 10%
Royalties related to art, literature, sound recording and movies (tax relief for EU-related companies is expected until 2013)	15%
Other royalties not listed above (0% will be applicable to EU-related companies from 2013)	5%
Rent for estate located in Latvia	5%
Gross proceeds from sale of real estate or shares in companies holding real estate situated in Latvia comprising more than 50% of assets	2%
Majority of payments to off-shores (Appendix 3)	15%

5.5 Other Taxes

5.5.1 Natural resource (packaging) tax

Natural resource tax is payable on the packaging of goods entering Latvia, packaging materials and environmentally hazardous goods upon their first sale. The extraction of natural resources and pollution are subject to licensing and taxation.

5.5.2 Customs and excise goods

Certain excise goods, such as tobacco and spirits, are subject to licensing.

5.5.3 Real estate tax

Real estate tax is charged on land and buildings owned or possessed by domestic or foreign persons. The tax base is the registered value of the real estate taxed at 1%. Residential houses used by individuals and certain other real estate are tax exempt.

5.5.4 Capital gains tax

A capital gains tax of between 15% and 25% applies to the sale of real estate located in Latvia, including the disposal of shares in Latvian-registered companies if more than 50% of the assets consist of real estate located in Latvia. When the seller is a non-resident and the buyer is a Latvian resident corporation, a 2% withholding tax is deducted from the gross price and considered as advance payment until the non-resident submits their annual tax return declaring taxable income and applying a 25% (or 15%) tax rate depending on their tax position.

5.5.5 Other fiscal charges

Other fiscal charges, such as gambling and lottery taxes or state and municipal duties, are imposed on different services, permissions and trading activities.

Appendix 1

Visa-free Regime Countries

Citizens of the following countries do not require a visa to enter Latvia in accordance with bilateral agreements on visa-free entry:

- Andorra
- Argentina
- Costa Rica
- Croatia
- Israel
- Japan
- Korea (South)
- Monaco
- Panama
- Singapore
- Uruguay
- USA
- Special Administrative Regions of the People's Republic of China (only passport holders of Hong Kong SAR and Macao SAR).

Latvia has unilaterally established visa-free entry with the following countries:

- Australia
- Brazil
- Brunei
- Canada
- Chile
- El Salvador
- Honduras
- Guatemala
- Malaysia
- Mexico
- New Zealand
- Nicaragua
- Paraguay
- San Marino
- USA
- Vatican City State
- Venezuela.

Appendix 2

Double Tax Treaties and Reliefs

The applicable double tax treaties signed by Latvia stipulate the following preferential tax rates (they do not reflect tax reliefs available for dividends, interest and royalties distributed to the EU companies under EU directives 90/435/EEK and 2003/49):

Recipient	Dividends (1) %	Interest (2) %	Royalties (3) %	Rentals of Industrial, Commercial or Scientific Equipment and Real Estate %	Management Fees (4) %	Disposal of Real Estate (5) %
Treaty:						
Austria	10/5	0/5/10	5/10	5	0	2
Azerbaijan	10/5	0/5/10	5/10	5	0	2
Armenia	10/5	0/5/10	5/10	5	0	2
Belarus	10	0/5/10	5/10	5	0	2
Belgium	10	0/5/10	5/10	5	0	2
Bulgaria	10/5	0/5	5/7	5	0	2
Canada	10/5	0/5/10	5/10	5	0	2
China	10/5	0/5/10	5/10	5	0	2
Croatia	10/5	0/5/10	5/10	5	0	2
Czech Republic	10/5	0/5/10	5/10	5	0	2
Denmark	10/5	0/5/10	5/10	5	0	2
Estonia	10/5	0/5/10	5/10	5	0	2
Finland	10/5	0/5/10	5/10	5	0	2
France	10/5(6)	0/5/10	5/10	5	0	2
Georgia	10/5(7)	0/5/10	5/10	5	0	2
Germany	10/5	0/5/10	5/10	5	0	2
Greece	10/5	0/5/10	5/10	5	0	2
Hungary	10/5	0/5/10	5/10	5	0	2
Iceland	10/5	0/5/10	5/10	5	0	2
Israel	10/5(6)	0/5/10	5	5	0	2
Ireland	10/5	0/5/10	5/10	5	0	2
Italy*	5/15(6)	0/5/10	5/10	5	0	2
Kazakhstan	10/5	0/5/10	5/10	5	0	2
Kirghizia*	10/5	0/5/10	5	5	0	2
Lithuania	10/0	0	0	0/5(5)	0	2
Luxemburg	10/5	0/5/10	5/10	5	0	2
Macedonia	10/5(6)	0/5	5/10	5	0	2
Malta	10/5	0/5/10	5/10	5	0	2
Moldova	10	0/5/10	5/10	5	0	2
Montenegro	10/5	0/5/10	5/10	5	0	2
The Netherlands	10/5	0/5/10	5/10	5	0	2
Norway	10/5	0/5/10	5/10	5	0	2
Poland	10/5	0/5/10	5/10	5	0	2
Portugal	10	0/5/10	5/10	5	0	2
Romania	10	0/5/10	5/10	5	0	2
Serbia	10/5	0/5/10	5/10	5	0	2
Singapore	10/5	0/5/10	5/7.5	5	0	2
Slovak Republic	10	0/5/10	5/10	5	0	2
Slovenia	10/5	0/5/10	5/10	5	0	2
Spain	10/5	0/5/10	5/10	5	0	2
Sweden	10/5	0/5/10	5/10	5	0	2
Switzerland	10/5(7)	0/5/10	5/10	5	0	2
Turkey	10/5	0/5/10	5/10	5	0	2
United Kingdom	10/5	0/5/10	5/10	5	0	2
United States	10/5(6)	0/5/10	5/10	5	0	2
Ukraine	10/5	0/5/10	5/10	5	0	2
Uzbekistan	10	0/5/10	5/10	5	0	2

*Effective from 1 January 2009

Explanations:

(1) 5% applies if the beneficial owner is a company that directly holds a minimum of 25% of the shares. According to the majority of the double taxation treaties, the 25% requirement is fulfilled if the shareholder has 25% of the capital. Some treaties provide a withholding tax rate of 15% on dividends; Latvian legislation applies a maximum rate of 10%, which is the highest applicable rate for dividends paid to all countries (except dividends distributed to the EU residents holding over 25% of the shares based on EU directive 90/435/EEC)
(2) 10% applies if the recipient is a related party. 5% applies if the payment is made by a commercial bank registered in Latvia
(3) 10% or 7.5% applies on royalties for literary or artistic works, including movies, videos and recordings
(4) Treated as part of business profits. 0% if permanent establishment does not exist
(5) Also applies on the disposal of shares if more than 50% of a company's assets form real estate located in Latvia. 5% is charged on rentals
(6) At least 10% shareholding required
(7) At least 20% shareholding required
(8) At least 10% shareholding and US$75,000 capital contribution required.

Tax relief can be applied in two ways:

- Complete the residence application form and submit it for approval to the fiscal offices of the two countries before exercising a transaction and making mutual payments to overseas

- Carry out the transaction and withhold statutory taxes from the payments to overseas and afterwards apply to the tax office for a tax refund.

Appendix 3

Listed Off-shores

Certain jurisdictions are qualified as "black listed", payments to which are subject to disadvantageous tax rates:

- Andorra
- Anguilla (United Kingdom of Great Britain and Northern Ireland)
- Antigua and Barbuda
- The Antilles (Kingdom of the Netherlands)
- United Arab Emirates
- Aruba (Kingdom of the Netherlands)
- The Bahamas
- Bahrain
- Barbados
- Belize
- The Bermudas (United Kingdom of Great Britain and Northern Ireland)
- British Virgin Islands
- Brunei Darusalim
- Dominica
- Jersey (United Kingdom of Great Britain and Northern Ireland)
- Djibouti
- Ecuador
- Guernsey
- Gibraltar (United Kingdom of Great Britain and Northern Ireland)
- Grenada
- Guam (United States of America)
- Guatemala
- Hong Kong
- Jamaica
- New Caledonia
- Jordan
- Cayman Islands (United Kingdom of Great Britain and Northern Ireland)
- Campione (Republic of Italy)
- State of Qatar
- Kenya
- Costa Rica
- Cook Islands
- Kuwait
- Labuan (Malaysia)

- Lebanon
- Liberia
- Liechtenstein
- Madeira
- Macao
- Maldives
- Republic of Mauritius
- The Marshall Islands
- Isle of Man
- Monaco
- Montserrat
- Nauru
- Niue (New Zealand)
- Olderne (United Kingdom of Great Britain and Northern Ireland)
- Panama
- Independent State of Samoa
- San Marino
- St Mary Islands
- Democratic Republic of Sao Tome and Principi
- Seychelles
- Saint Pierre and Miquelon
- Saint Kitts-Nevis
- Saint Lucia
- Saint Vincent and the Grenadines
- Saint Helena Island (United Kingdom of Great Britain and Northern Ireland)
- Tahiti (French Polynesia)
- Turks and Caicos Islands (United Kingdom of Great Britain and Northern Ireland)
- Tonga
- Uruguay
- Vanuatu
- Venezuela
- Virgin Islands (United States of America)
- Island of Zanzibar (United Republic of Tanzania).

Unless there is a prior exemption from the tax authorities, payments to off-shores are subject to ordinary corporate income tax (15%) with certain exceptions.

On certain occasions this also applies to Latvian resident individuals.

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