Cabinet Order No. 72

Adopted 25 January 2024

**Shadow Economy Restriction Plan for 2024–2027**

RIGA

2023

**Abbreviations and terminology**

MTI – medical treatment institutions

CIS – Construction Information System

SCCB – State Construction Control Bureau

B2B – international term for business-to-business, a situation where a commercial transaction is conducted between one business and another

RTSD — Road Traffic Safety Directorate

DAGR – Data Dissemination and Management Platform

RoE – report of employer

DSI – Data State Inspectorate

EDLUS – electronic working time recording system

EC – European Commission

MoE – Ministry of Economics

EU – European Union

FIU – Financial Intelligence Unit of Latvia

MoF – Ministry of Finance

MoI – Ministry of the Interior

MoI IC – Information Centre of the Ministry of the Interior

PIT – personal income tax

GDP – gross domestic product

IUB – Procurement Monitoring Bureau

MoES – Ministry of Education and Science

LMA – Latvian Medical Association

UPOMPL – Union of Professional Organisations of Medical Practitioners of Latvia

LIA – Latvian Insurers Association

BoL – Latvijas Banka (Bank of Latvia)

LBAS – Free Trade Union Confederation of Latvia

LBNA – Latvian Construction Industry Trade Union

LBP – Construction Council of Latvia

LBPA – Latvian Association of Structural Engineers

LDDK – Employers’ Confederation of Latvia

LIAA– Investment and Development Agency of Latvia

LKKA – Latvian Association of Beauticians and Cosmetologists

MoW – Ministry of Welfare

LPOT – Latvian Network of Patient Organizations

LALRG – Latvian Association of Local and Regional Governments

LSSA – Latvian Association of Beauty Specialists

LCCI – Latvian Chamber of Commerce and Industry

LVSADA – Trade Union of Health and Social Care Employees of Latvia

LDA – Latvian Dental Association

Cabinet – Cabinet of Ministers

NHS – National Health Service

NGO – non-governmental organisations

OECD – Organisation for Economic Cooperation and Development

POS – point of sale, card and contactless payment terminals

CRPC – Consumer Rights Protection Centre

VAT – value added tax

MoT – Ministry of Transport

SPKC – Centre for Disease Prevention and Control

MoJ – Ministry of Justice

HEA – Healthcare Employers’ Association

MoEPRD – Ministry of Environmental Protection and Regional Development

VEDLUDB – Unified Electronic Working Time Recording Database

HI – Health Inspectorate

SRS – State Revenue Service

SRS IS – Information System of the State Revenue Service

MoH – Ministry of Health

SP – State Police

SRDA – State Regional Development Agency

SBG – State Border Guard

MSSIC – Mandatory State social insurance contributions

SES – State Environmental Service

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1. Summary

The Shadow Economy Restriction Plan for 2024–2027 (hereinafter – the plan) is a medium-term policy planning document which prioritises the reduction of shadow economy for the next four years by implementing both horizontal measures and targeted measures in specific economic sectors through close cooperation with sectoral ministries and representatives of non-governmental organisations.

Cabinet Order No. 178 of 30 March 2023, On the Development of the Shadow Economy Restriction Plan for 2023–2025,[[1]](#footnote-2) identifies the following three priority sectors of the national economy for the reduction of the shadow economy:

* construction – building construction, civil engineering, specialised construction activities;
* human health and social work activities – health protection;
* wholesale and retail trade relating to the use of cash mutual transactions and the availability and disclosure of information to public authorities.

The Cabinet Order strengthened the governance model of the plan, stating that the development, implementation and monitoring of the measures of the plan in a specific sector shall be the responsibility of the relevant sectoral ministry. Therefore, four working groups were set up to draft proposals for the Shadow Economy Restriction Plan for 2024–2027 (hereinafter – the plan):

* on the use of cash in mutual transactions (MoF);
* on the exchange of information and data between public authorities (MoF);
* on improvement of the policy and regulatory framework in the construction sector, i.e. specialised construction activities, building construction and civil engineering (MoE);
* on improvement of the policy and regulatory framework in the health protection and also beauty care sectors (MoH).

Representatives of the MoE, MoH, MoEPRD, the Ministry of the Interior, MoT, MoES, MoW, SRS, BoL, LDDK, LCCI, the Foreign Investors Council in Latvia, the Corruption Prevention and Combating Bureau, and also more than 30 sectoral associations were involved in the work of the working groups. In the period from April to May 2023, four working groups developed a total of more than 50 proposals for the measures of the draft plan, outlining the main courses of action and the resultative indicators to be achieved.

In accordance with the Cabinet Order, at the end of May, the MoE and MoH informed of the conclusions of the working groups, providing the draft plan with proposals for measures to improve the policy and legal framework of a specific economic sector and further actions to curb the shadow economy in a specific sector. In addition, the Ministry of Finance, when developing the shadow economy restriction plan for the next period, emphasised communication with sectoral ministries and representatives of the non-governmental sector to identify measures that would both reduce the shadow economy and improve the business environment in priority sectors, reducing distortions of competition.

The plan includes measures that are aimed at reducing the risk of the shadow economy in a specific sector and also provides an estimate of the potential fiscal impact on the State budget from implementing the measures.

Developing Cabinet Order No. 178 of 30 March 2023, On the Development of the Shadow Economy Restriction Plan for 2023–2025, it was initially planned to develop a plan for a three-year period. During the process of developing the courses of action of the plan, the implementation period was adjusted, thus ensuring consistency with the Tax Policy Guidelines by setting a four-year period, i.e. from 2024 to 2027.

Tax policy is an essential prerequisite for a favourable business environment. Furthermore, an attractive business environment is a key instrument for reducing the shadow economy. At the same time, shadow economy participants create unfair competition that has a negative impact on the business environment. The relevant processes are therefore interrelated.

The draft plan has been discussed and agreed with sectoral ministries, SRS, IUB and sectoral associations. A number of proposals for the measures of the plan identified in the working groups have been submitted for evaluation and discussion to the working group which is developing the Tax Policy Guidelines for 2024–2027. It should be noted that the plan includes specifically designed measures to mitigate the risk of the shadow economy that will not duplicate with the tasks included in the Tax Policy Guidelines and development planning documents of other authorities, and also tax administration, operational and supervision measures included in the SRS work plan.

The SRS will continue its work to improve the efficiency of the service provision process, implementing a new approach to tax administration, i.e. tax control, by introducing smart solutions to support the workflow of the control process as laid down in the SRS internal action plans.

In addition, within the framework of the courses of action set out in the plan, measures are being taken to improve sectoral policies and the regulatory framework to reduce the shadow economy, improve the business environment and promote voluntary compliance with tax obligations. The plan includes measures that provide for the use of taxpayer rating in public procurements, restrictions on the circulation of cash, promoting the use of non-cash transactions, identification of opportunities to improve the personal income tax return, strengthening of data analytics in the construction, health and beauty care sectors, improvement of information and data exchange, public education and other measures to improve the competitiveness of businesses.

2. Background

## 2.1. Concept of the shadow economy, motivation of participants and the related risks

The shadow economy is a **term** used by various scholars and organisations to describe the part of the informal economy where taxes are not paid according to national tax regulations. Given that there are several methodologies for measuring the shadow economy, there are also different definitions of the shadow economy. For example, according to the definition by the Organisation for Economic Cooperation and Development (OECD), the shadow economy consists of economic activities, whether legal or illegal, which are required by law to be fully reported to the tax administration but which are not reported and which therefore go untaxed unlike activities which are so reported.[[2]](#footnote-3)

Austrian Professor F. Schneider uses the following definition in his research to measure the size of the shadow economy: the shadow economy includes all economic activities which are hidden from official authorities for monetary, regulatory, and institutional reasons. Monetary reasons include avoiding paying taxes and all social security contributions, regulatory reasons include avoiding governmental bureaucracy or the burden of regulatory framework, while institutional reasons include corruption law, the quality of political institutions and weak rule of law. The shadow economy reflects mostly legal economic and productive activities that, if recorded, would contribute to national GDP.[[3]](#footnote-4)

The shadow economy is ‘the gross domestic product that is not recorded in official statistics because of non-declaration and (or) incomplete declaration’ and ‘the production of legal or illegal goods and services that are not included in the official GDP’.[[4]](#footnote-5)

According to Professor A. Sauka research on the shadow economy index, the components of the shadow economy are ‘envelope wages’, unreported income, illegal employment, bribery and corruption.[[5]](#footnote-6)

The shadow economy carries with it **numerous risks**. It encourages unfair competition, distorts the market and leaves a negative impact on tax collection. Businesses that pay little or no tax are able to increase their current assets and save on expenses by paying ‘envelope wages’. This lowers the prime cost of goods and services, squeezing fully taxed goods and services out of the market. [[6]](#footnote-7) At the same time, people who receive ‘envelope wages’ are exposed to social security, occupational safety and social insurance risks. ‘Envelope wages’ not only have a negative effect on social security contributions of employees, but also prevent the receipt of the State-guaranteed replacement income upon retirement, disability, loss of a family supporter, illness, during the period of maternity leave, when losing a job and also in case of an accident at work or an occupational disease.

Consequently, the shadow economy delays national economic growth, has a negative effect on tax collection and reduces national budget revenues. This reduces the amount of public funding that can be used to improve public welfare and quality of life, develop infrastructure and services that would create the conditions for more economically active businesses and expansion in production.

At the same time, economists recognise that it is impossible to eliminate the shadow economy completely as it is a natural phenomenon under certain conditions and also serves a social function. For example, in difficult economic times, businesses tend to partially or fully shift their activities to the shadow economy, putting their (short-term) interests above the (mostly long-term) interests of society. Similarly, individuals in difficult financial situations engage in the shadow economy by failing to pay labour taxes, thus depriving themselves of future social guarantees and reducing the social budget revenues that serve the common public interest. At the same time, participation in the shadow economy can be caused by low tax morale, i.e. targeted and principled tax evasion unrelated to financial hardship.

***Motivation for involvement in the shadow economy***

Tax evaders who engage in the shadow economy can be divided into non-tax payers, partial tax payers, those who operate outside the scope of the SRS supervision and those who engage in illegal activities. Often, employees themselves want to receive ‘envelope wages’ as a way of avoiding various obligations, such as the payment of **child maintenance**. Each group of taxpayers is likely to have its own motivations for tax evasion.

The study by the European Parliament Committee on Fiscal Affairs[[7]](#footnote-8) mentions eight main hypotheses on **the driving forces of the shadow economy and their causal links** in the OECD countries that stimulate involvement in the shadow economy:

* high tax burdens increase the shadow economy;
* excessive government regulation;
* poor quality of services by public authorities;
* **low tax morale**;
* high unemployment rate;
* high self-employment rate;
* low GDP per capita in the country;
* low levels of freedom.

It is crucial for each country to identify the reasons why **taxpayers lose their motivation to pay taxes** by defining strategies and measures to tackle the causes of tax evasion for each target group. Causes can vary from country to country, and even within the same country, over time and throughout history. The studies by the Inter-American Center of Tax Administrations (CIAT) point out a number of **reasons** for tax evasion that reduce the motivation to pay taxes:

* inconsistency in political decisions and lack of trust in the government;
* structure of the national tax system;
* low efficiency of tax administrations;
* unfair tax policies;
* tax burden and high rates;
* lack of simplicity and accuracy in tax legislation;
* different tax regimes with different tax burdens;
* possibility to violate statutory provisions without greater risks;
* poor quality of public goods and services (infrastructure, social protection);
* trade barriers;
* low level of education of the population;
* lack of awareness about the use of tax resources;
* lack of tax integrity of the population, etc.[[8]](#footnote-9)

Successful restriction of the shadow economy requires the implementation of comprehensive and carefully designed policies, focusing on the determinants that are most important for improving the business environment. Such measures may vary from reducing regulatory and administrative burdens, promoting transparency and improving government efficiency to improving tax compliance, automating procedures and promoting electronic payments.

***Tax morale***

Tax morale measures taxpayer perceptions and attitudes towards paying and evading taxes and also indicates to the intrinsic motivation to pay taxes.[[9]](#footnote-10) This is an important aspect of the tax system as most tax administrations rely on the honesty of taxpayers. Therefore, in building a sustainable tax culture, it is important to focus on tax morale that would contribute to raising voluntary tax compliance.

The research by both prof. A. Sauka and prof. F. Schneider suggests that tax evasion cannot be explained solely by so-called rational choice, i.e. that involvement in tax evasion by individuals is explained by the potential benefits of tax evasion as opposed to the likelihood of being caught and the level of penalties imposed. On the contrary, it is considered that the existence of low tax morale has a major role in explaining why the shadow economy in some countries is higher than rational choice can explain.[[10]](#footnote-11) In this context, it should be stressed that the external environment has an important influence on the formation of tax morale, i.e. the attitude of entrepreneurs towards the fairness of the tax system, the way in which the money paid in taxes is used, the prestige of the government in the eyes of entrepreneurs.

Tax morale is related to the following factors:

* financial indicators – satisfaction with income, national economic situation, income distribution and market economic performance;
* political indicators – satisfaction with democracy, trust in the government;
* demographics – age, gender, education.

Countries with high GDP, effective social protection and transparent use of public funds have higher tax morale. However, such factors as high inflation, income inequality, high tax rates, corruption and low trust in public authorities have a negative impact on tax morale. The results of the research by prof. A. Sauka show that merchants with low tax morale believe that fraud and tax evasion are perfectly justified and engage in the shadow economy up to 57.3 per cent of the time[[11]](#footnote-12), because seeing others evading taxes in society makes evasion seem rational and justified. This is why tax evasion is used by merchants as a self-defence mechanism. Low tax morale is associated with higher levels of tax evasion, lower tax compliance, higher levels of the shadow economy, more undeclared labour and a higher risk of ‘envelope wages’.

These findings show that achieving a significant change in the prevalence of the shadow economy is a challenging task, namely, it is necessary to change the mindset of a large part of society, in particular with regard to the usefulness of paying taxes. Although policy programmes that fundamentally change public thinking are likely to be more complex and difficult to implement and also more time-consuming than quick-fix tax policy solutions, such as tax incentives, tax control or penalty policies, tax legislation, the results of the research suggest that they could be the most effective way to significantly reduce the size of the shadow economy in Latvia.

The report of science-based policy recommendations by prof. A. Sauka identifies the main factors influencing the size of the shadow economy and ‘envelope wages’:

1. trust of businesses and individuals in different authorities and satisfaction with public services;

2. likelihood of being caught and proportionality of penalties when engaging in the shadow economy activities;

3. tax policy;

4. tax morale;

5. reasons relating to specific industries and businesses: determinant factors for envelope wages, including administrative burden.

A diagram of a graph and a diagram of a graph

Description automatically generated with medium confidenceIn addition, the OECD concludes in the research that one of the most important factors influencing tax morale is trust in the government, parliament, courts, tax administration, public officials, politicians, the president and political parties. A survey on public trust in public authorities conducted by the OECD in 2022 shows that only 24.5 per cent of the Latvian population trusts the government that is significantly lower than the OECD average (41 per cent)[[12]](#footnote-13).

**LATVIA**

**Public trust in government**

Have trust

Neutral attitude

No trust

No trust

Neutral attitude

Have trust

Within the scope of the national research programme “Reduction of the Hidden Economy for Ensuring Sustainable Economic Development”, prof. A. Saulītis in his report on the involvement of the Latvian population in the shadow economy emphasises the importance of the tax morale aspect. The research on the involvement of the population in the shadow economy concluded that tax evasion and the shadow economy are linked to three key factors:

Do not know

Do not know

1. *structural factors* – tax system and regulatory framework. This includes the effectiveness of tax administration, i.e. the level of fines and the likelihood of being fined, the incidence of corruption and the quality of public services;
2. *payment factors* – the availability of goods and services and the difference in costs between the formal and informal economies, as well as purchase anonymity, security, etc.;
3. *historical factors –* related to tax morale, identity, the work ethics of tax administrations and broader political and social environments.[[13]](#footnote-14)

When assessing different situations where taxes are not paid in full, the inhabitants of Latvia most frequently condemn tax evasion by companies (paying employees envelope wages or providing a service to another company without paying taxes) and also situations where someone is defrauding social benefits. Tax evasion in general (‘someone evades taxes by not paying or only partially paying the national tax’) is much more favourably viewed, while provision of a service by a private individual to a private individual is the least frowned upon (Figure 1). **It should be highlighted that overall tax morale is low**: most respondents did not consider any of the examples of tax evasion mentioned in the survey to be completely unacceptable.

Do not know/NA

Fully acceptable

Fully unacceptable

A company provides services to another company but does not inform the tax or social security authorities of its activities

A company provides its services to a private household but does not inform the tax or social security authorities of the fees received

A private individual is employed in a private household and does not inform the tax or social security authorities of the remuneration he/she receives, even though it should be reported

Someone receives social benefit payments (unemployment benefit, sickness benefit, etc.) while hiding the actual circumstances that would prevent receipt of such payments

A company hires a private individual, but all or part of the wage is paid in an envelope

Someone evades taxes by not paying or only partially paying the national taxes

*Figure 1. Tax morale in Latvia “To what extent do you consider this behaviour to be acceptable or unacceptable”, survey of 2020.*

Trust is a set of different beliefs and judgements. In the field of taxation, trust is largely linked to the focus strategies in the work of tax administrations: actions based on mutual respect and understanding, rather than fear of being caught or punitive actions that in turn are linked to strategies to prevent tax collection. The failure of prevention strategies in the context of Latvia is also indicated by the fact that in none of the situations the moral judgement of respondents depends on their perception of the likelihood of being caught for tax evasion.

It also matters whether the individual is employed in the shadow economy and in such case tax morale is significantly lower than if the entire wage is earned and all taxes are paid in good faith. This suggests that once an individual is involved in the shadow economy activities, tax morale becomes weaker and such persons much less likely to be drawn into paying taxes. Moreover, the shadow economy is becoming self-sufficient, i.e. goods and services are much more likely to be purchased by those who themselves receive undeclared income.

In contrast, Latvia has a part of society that has a relatively high tax morale. These are mostly general taxpayers who consider their tax burden too high. This shows that law-abiding individuals do not regard the payment of taxes as a personal matter, but as a matter of common interest for society as a whole. In other words, also in this case the payment of taxes is mainly linked to focus strategies and historical factors: trust in the SRS. At the same time, inequalities in society make people less willing to pay taxes.

Within the scope of the national research programme “Reduction of the Hidden Economy for Ensuring Sustainable Economic Development”, the results of the survey conducted by prof. A. Sauka show that in Latvia the most common reason that would encourage people to purchase goods or services without a justification document, or without paying all applicable taxes, is a lower price [[14]](#footnote-15) (Figure 3).

|  |  |
| --- | --- |
| A graph with numbers and text  Description automatically generated  Nothing would encourage me  Greater anonymity  Faster servicing  Possibility to help someone who needs money  Better quality  The goods or services not available on the regulated market or difficult to access  This was a service between friends, relatives or colleagues  Lower price  What would encourage you to purchase goods or services without receipt or without paying all stipulated taxes? | A graph with red and grey bars  Description automatically generated  Better quality  The goods or services not available on the regulated market or difficult to access  It was realised only later that the goods or services were not declared  Possibility to help someone who needs money  Faster servicing  This was a service between friends, relatives or colleagues  Lower price  Why did you purchase these goods or services without declaring the transaction instead of making the purchase on a regular market? (SEVERAL ANSWERS POSSIBLE) |
| *Figure 2. Motivation to purchase undeclared goods and services* | *Figure 3. EC* [*Special Eurobarometer 498 survey: Undeclared work in the EU*](https://data.europa.eu/data/datasets/s2250_92_1_498_eng?locale=lv) *September 2019* |

The survey also shows that the majority (39 per cent) believes that it is acceptable not to declare transactions in Latvia between friends, relatives or colleagues. At the same time, according to the survey data, this view is less common in Latvia than in the EU-28 average.

*Figure 4. Reasons for providing services in the shadow economy, survey of 2020.*

In the survey, respondents indicate that the most frequent reason they think people are tempted to work or provide services without paying all or part of their taxes is that taxes and social security contributions are too high. This is followed by a lack of jobs, a lack of trust in the State and its social guarantees, and also the existing bureaucracy (Figure 4).

When defining measures to reduce the size of the shadow economy, it should be borne in mind that whatever measures are implemented to reduce the shadow economy, there will always be individuals operating in the grey sector who will purposefully seek to continue to evade taxes and remain outside the formal economy by changing their behaviour and using other tools and techniques.

Given that the risk of the shadow economy is closely linked to the principle of tax morale, the involvement of individuals in the shadow economy also exists among high-income individuals with low tax morale. Therefore, keeping the overall welfare of the country in mind, it is necessary to take smart measures to raise tax morale in the country as a whole and among groups of people with different levels of wealth and motivation.

***Correlation between the shadow economy and GDP***

Economists recognise that the size of the shadow economy is highly correlated with the development of national economy; therefore, GDP growth is one of the most important driving forces of changes in the scale of the shadow economy. The higher the level of GDP per capita, the higher the welfare, the less prone people are to breaking the law, including tax evasion. This pattern can also be clearly seen in the graph below, depicting GDP per capita[[15]](#footnote-16) and the scale of the formal economy as a percentage of GDP, calculated as the inverse of the share of the shadow economy as a proportion of GDP according to the method of prof. F. Schneider (Figure 5).

Share of the formal economy, % of GDP

GDP per capita, EUR

*Figure 5. Correlation between gross domestic product per capita and the share of formal economy*

Similarly, the EC study on the scale of the VAT gap in EU Member States[[16]](#footnote-17) shows a high dependence of the VAT gap on GDP and economic structure. In the report, the EC highlights GDP growth, general government surplus, information technology expenses and the shares of the agricultural and financial sectors in the economy as statistically significant factors. According to the study, **in order to reduce the** **VAT gap by one percentage point, GDP would need to increase by three percentage points**.

The 12-year VAT gap statistics and the 9-year labour tax gap statistics accumulated by the SRS, which show a high inverse correlation between GDP and the tax gap percentage, also suggest that macroeconomic growth has a significant impact on the size of tax gaps. In fact, changes in the GDP factor can account for 86 per cent up to 94 per cent of the tax gap dynamics (Figures 6–8).

*Figure 6. Correlation between VAT gap and GDP Data source: SRS data*

*Figure 7. Correlation between PIT gap and GDP Data source: SRS data*

*Figure 8. Correlation between MSSIC gap and GDP Data source: SRS data*

Figure 9 below shows the link between the economic situation and the share of the shadow economy in the countries of the European Economic Area, depicting GDP per capita and the size of the shadow economy according to prof. F. Schneider research data. The data show a strong inverse proportional correlation, i.e. the higher the GDP per capita, the lower the share of the shadow economy in the country.

*Figure 9. Correlation between the share of the shadow economy and GDP per capita in 2022.*

*Developed by the Ministry of Finance on the basis of Eurostat data and F. Schneider research data.*

As shown in the figure, advanced economies, e.g. Germany, Austria, Luxembourg and Switzerland, have a higher GDP per capita[[17]](#footnote-18) and a lower shadow economy rate, while such countries as Bulgaria, Croatia, Hungary, Romania have a lower GDP per capita and a relatively high shadow economy rate[[18]](#footnote-19).

GDP per capita shows the material welfare level and purchasing power of the population of the respective country. If people cannot meet their basic needs and have a choice between meeting their basic needs and meeting their tax obligations, the choice will be in favour of personal rather than public interests. The higher value the population of a country can produce, the higher the material welfare of its inhabitants and the greater their interest in contributing to common public needs, including the payment of taxes.

In accordance with the data of the OECD study conducted in 2022, Figure 10 shows the satisfaction of European citizens with their level of income[[19]](#footnote-20) and the link with the size of the shadow economy according to F. Schneider research data.

*Figure 10. Correlation between the share of the shadow economy and public satisfaction with the income level in 2022.*

*Developed by the Ministry of Finance on the basis of the OECD data and F. Schneider research data.*

In countries where people have lower income satisfaction levels, there is greater involvement in the shadow economy. Consequently, if a person has sufficient income to meet his or her basic needs, he or she is less likely to engage in tax evasion. Conversely, the lower the level of income satisfaction, the more people are inclined to prioritise their personal short-term interests by avoiding the payment of taxes, rather than complying with the law by fulfilling their tax obligations, and thus also contributing to the financing of common national (public) needs.

*Figure 11. Correlation between the share of the shadow economy and the level of corruption in 2022.*

*Developed by the Ministry of Finance on the basis of DELNA research data and F. Schneider research data.*

Another indicator related to the shadow economy is the perception of the level of corruption in the country by private sector (Figure 11). The figure shows that such countries as Switzerland, Denmark, Finland, Sweden and Germany have a higher corruption perception index, which could indicate a lower level of corruption and less involvement in the shadow economy. In contrast, such countries as Hungary, Greece and Slovakia have a lower corruption perception index and a higher level of the shadow economy. Widespread corruption is linked, among other things, to high levels of the shadow economy and low levels of morale.

In summary, research shows that the creation of a favourable business environment plays a crucial role in reducing the shadow economy that would facilitate an increase in the number of companies that would be competitive in Latvian and foreign markets, increase the volume of exports of Latvian goods and services, improve the quality and creation of products with high added value.

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* National Development Plan of Latvia for 2021-2027
* Digital Transforamtion Guidelines for 2021-2027
* Corruption Prevention and COmbating Action Plan for 2023-2025
* Medium-term national tax policy guidelines **Shadow Economy Restricction Plan for 2024-2027 (draft), etc.**

Policy planning documents

Shadow economy

GDP

* Number of economic agents
* Export capacities
* Investments
* Etc.

*Figure 12. Factors contributing to the shadow economy and correlation thereof with GDP.*

Changes in the size of the shadow economy depend significantly on the development of national economy and the factors influencing the business environment. At the same time, targetedmeasures to reduce the shadow economy or discipline, including improving tax morale, reducing regulatory and administrative burdens, improving transparency, promoting tax compliance, automating procedures, introducing electronic payments, etc. also play an important role. It should be noted that the business environment cannot be fully organised without targeted measures to restrict the shadow economy and consequently the share of the shadow economy cannot be minimised only through economic development. Thus, to improve the attractiveness of the business environment, the measures of the policy planning documents and the measures of the plan to restrict the shadow economy are interrelated and produce a synergy effect (Figure 12).

Accordingly, in order to reduce the scale of the shadow economy in the country, it is important to work in parallel on a number of interrelated documents, including the Declaration on the Intended Activities of the Cabinet Chaired by Evika Siliņa (approved on 15 September 2023)[[20]](#footnote-21) and the objectives set out therein, namely:

* National Development Plan of Latvia for 2021–2027 (approved by the *Saeima* on 2 July 2020);
* Digital Transformation Guidelines for 2021–2027 (approved by Cabinet Order No. 490 of 7 July 2021);
* Corruption Prevention and Combating Action Plan for 2023–2025 (approved by Cabinet Order No. 199 of 11 April 2023);
* informative report “On Progress in the Development of the National Tax Policy Guidelines for 2024–2027” (examined and approved by the Cabinet on 26 September 2023);
* Shadow Economy Restriction Plan for 2024–2027 (draft), etc.

At the same time, the Shadow Economy Restriction Plan for 2024–2027 does not duplicate with the tasks included in the Tax Policy Guidelines and development planning documents of other authorities, and also tax administration, operational and supervision measures included in the SRS work plan.

## 2.2. Estimate of the size of the shadow economy

Methods for estimating the size of the shadow economy cannot be regarded as unambiguously accurate and comparable. As mentioned above, a number of internationally renowned economists are working on estimating the size of the shadow economy. In order to get a comprehensive overview of the size of the informal economy, the results of several studies are compared, based on both direct (survey) and indirect (macroeconomic) methods. Most of these methods only allow an assessment of the direction of change and the approximate scale of the increase or decrease in the shadow economy, i.e. the trends, rather than its specific size.

According to the method by F. Schneider, the Shadow Economy Index is measured as a percentage of GDP using the **indirect modelling method**. The measurement of the size of the shadow economy is based on the cash demand approach and the multiple-indicator, multiple-cause (MIMIC) model (Figure 13), allowing to obtain index time series of the ratio of unrecorded to recorded output in a country. The basic idea of the demand for currency approach is that goods and services sold in the shadow economy are settled in cash and that by using the demand for cash function it is possible to measure such goods and services respectively provided and delivered in exchange for cash and thus to estimate the size of the shadow economy.

Estonia

Lithuania

Latvia

*Figure 13. Size of the shadow economy in the Baltic States from 2009 to 2022 (% of GDP) according to prof. F. Schneider research data.*

According to the method by A. Sauka, the Shadow Economy Index is measured as a percentage of GDP using the **direct survey approach**, i.e. business questionnaires (including telephone interviews) with open-ended responses and analysis of tax audit data and a revenue approach to measuring GDP; GDP is calculated as the sum of gross compensation of employees and gross operating income of companies (Figure 14). The shadow economy includes unreported business profits, unreported wages and unregistered employees. The size of the shadow economy is assessed by looking at businesses that are legally registered and engaged in the field of legal goods and services. The calculations do not include illegal trade in goods or services, including cross-border trade, smuggling or imports of illegal goods.

Estonia

Lithuania

Latvia

*Figure 14. Size of the shadow economy in the Baltic States from 2009 to 2022 (% of GDP) according to prof. A. Sauka research data.*

According to the estimates obtained within the scope of the national research programme “Reduction of the Hidden Economy for Ensuring Sustainable Economic Development” by prof. A. Sauka and his team, the potential amount of taxes to be collected from the shadow economy in Latvia is between EUR 2 billion and EUR 3.6 billion.The report of prof. T. Putniņš estimates the amount of tax revenue lost in Latvia due to the shadow economy, tax evasion, concealment and also smuggling. The results show that tax evasion varies significantly between different tax types:

* labour taxes (PIT and MSSIC) account for the largest amount, i.e. 77 per cent, of the lost tax revenue. The study shows that there is significant potential to increase tax revenues through political actions aimed at reducing the amount of lost revenues from labour taxation. At the same time, it is pointed out that this could include any measures to reduce wage envelopes, in particular any policies aimed at preventing schemes designed to avoid tax payments by high-income earners who generally account for the largest share of uncollected taxes compared to how much tax revenue such individuals should be provide;
* the study mentions that the next largest contributor to the tax gap is excise duty which accounts for 10 per cent of the lost tax revenue. Among excise duties, petroleum products, in particular diesel and petrol used in vehicles, are the largest source of the lost tax revenue as they account for a large share of excise duty revenue. Tobacco is next in the category of excise duty, mostly due to smuggled cigarettes, although this component is showing a downward trend over time, followed by alcohol. Only a small part of the estimated undeclared, illegal consumption of petrol and diesel is detected and recovered by law enforcement authorities, meaning that policies to collect excise duties on petroleum products could be much more effective;
* VAT constitutes a significant share of the lost tax revenue, accounting for 9 per cent of all lost tax revenue. The study shows that VAT evasion is estimated at 3.8 per cent which is lower than for other tax categories. However, VAT accounts for a large share of uncollected taxes due to its high share in the tax revenue structure (29 per cent). Evidence from EU countries shows that effective policies to fight VAT evaders include investments in information technology to better track VAT payment obligations and to encourage taxpayers to comply with additional information obligations, e.g. real-time reporting and e-invoicing.[[21]](#footnote-22)

The SRS assesses gaps in VAT, PIT, MSSIC and excise duties. The **tax gap** is the ratio of the amount of undeclared and declared but unpaid taxes to the potential tax mass that would be calculated and collected under the assumption that all taxpayers fully comply with their tax obligations. It should be noted that the total tax gap is not the same as the size of the shadow economy as measurements of the shadow economy determine the share of unregistered economic activity, not lost tax revenue.

According to the SRS estimate, Table 1 shows that the **potential amount of taxes to be collected from the shadow economy in 2021 is estimated at EUR 992 million.** The potential amount to be collected (VAT, PIT, MSSIC, excise duty losses) is estimated by the SRS **at 2.95 per cent of GDP.** (GDP of 2021 equals to EUR 33 617 mln.) At the same time, the present tax gap excludes data that has not come to the attention of the SRS at all.

|  |  |
| --- | --- |
| Potentially collectable amount | mln. EUR |
| VAT gap | 162 |
| PIT gap from undeclared wages for general tax regime employees | 280 |
| MSSIC gap from undeclared wages for general tax regime employees | 516 |
| Excise duty gap from fuel products | 34 |
| **TOTAL** | **992** |

*Table 1. Estimates of the current level of undeclared and unpaid taxes in 2021.* Excise duty gap for 2020

*Data source: SRS data.*

Another indicator that indirectly shows the size of the shadow economy in a country is the share of **cash in circulation**.[[22]](#footnote-23) The EC study concludes that one of the main driving forces of the shadow economy is the continued use of cash as the main method of payment. Moreover, the driving forces of demand for cash are the same whether they are large or small countries, northern or southern countries, countries with an interest in using cash, or countries where consumers pay predominantly in non-cash currency, or where there is a policy of restricting the use of cash.

The development of cashless payment methods encourages people to replace cash. Thus, the widespread use of new payment innovations such as contactless and mobile payments will further reduce cash hoarding. It has been studied that every crisis so far has increased the demand for cash. During the COVID-19 crisis, the amount of cash in circulation increased worldwide, even in the Scandinavian countries. For example, the euro area has seen a significant increase in the demand for cash since its existence[[23]](#footnote-24).

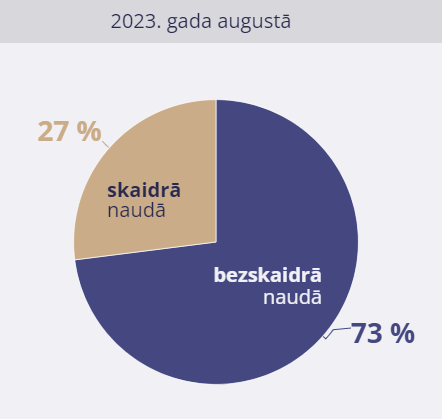
According to the BoL, a total of **EUR 2.4 billion** of cash was deposited in the ATMs in 2022. Retailers have paid **EUR 3.9 billion** to cash collection companies, representing a total of EUR 6.3 billion or **16.2 per cent** of GDP. It should be noted that there are also objective reasons for depositing cash in the ATMs that do not necessarily indicate that the money is derived from the shadow economy activities. In the retail sector, not all cash is passed on to cash collection companies, some of it is returned to customers and used in mutual settlements with suppliers. At the same time, this cash flow indicator can also be seen as one of the signs characterising the shadow economy trend.

Latvian payment service providers (credit institutions, electronic money institutions, payment institutions, credit unions, Latvijas Banka and the Treasury) **made 394.2 million customer non-cash payments in H1 of 2023**, totalling **EUR 150.7 billion**. Compared to H1 of 2022, the total **number of customer non-cash payments increased by 10 per cent** and the **total volume** of payments by **26 per cent**. The most commonly used non-cash payments by customers were card payments (61.2 per cent of total non-cash payments) and customer credit transfers (36.4 per cent of total non-cash payments). It should be noted that **24.2 million instant payments amounting to EUR 6.9 billion** were made in H1 of 2023.[[24]](#footnote-25)

non-cash

cash

August 2023



Data: *Latvijas Fakti*

Given that cash is often used as a tool by targeted participants in the shadow economy, it is necessary to create a system that makes it commercially unattractive to obtain illicit cash. At the same time, it is also necessary to promote digital payments, motivating society as a whole to use less cash in everyday transactions, which will also reduce the attractiveness of using cash for targeted participants in the shadow economy. This fact is also confirmed by the recommendation provided in the research led by prof. A. Sauka, i.e. recommendation on incentives and disincentives for electronic payment systems to reduce the amount of cash that can potentially be used to pay envelope wages in cash, e.g. cash payment caps, availability of point of sale (POS) terminals in all sectors, electronic-only payments in public institutions, incentives to use cards at the point of sale[[25]](#footnote-26).

Current data from F. Schneider research show that the size of the shadow economy has continued its downward trend, accounting for 20.2 per cent in 2021 and 19.9 per cent in 2022[[26]](#footnote-27) (Figure 15).

*Figure 15. Share of the shadow economy in 31 European countries in 2022 (% of GDP) according to prof. F. Schneider research data*

In contrast, according to SSE Riga Centre for Sustainable Business researcher prof. A. Sauka and prof. T. Putniņš research “Shadow Economy Index for the Baltic Countries 2009–2022” data, the size of the shadow economy in Latvia in 2022 was 26.5 per cent of GDP, almost unchanged, down by 0.1 percentage point compared to 2021. It should be noted that the shadow economy index is used in various studies as an indicative indicator to describe the trend of an indicator.

The largest component of the shadow economy in Latvia in 2022 was ‘envelope wages’ that increased by 0.5 percentage points compared to the previous year to 46.7 per cent. The share of average wages that entrepreneurs hide from the State, or ‘envelope wages’, increased by 1.2 percentage points to 25 per cent in Latvia in 2022 compared to 2021.

In 2022, the share of the shadow economy in Latvia reached 34.5 per cent in the construction sector (31.2 per cent in 2021), 30.5 per cent in the retail trade sector (29.8 per cent in 2021), 28.6 per cent in the service sector (27.5 per cent in 2021), 23.9 per cent in the manufacturing sector (25 per cent in 2021) and 20.5 per cent in the wholesale trade sector (24.4 per cent in 2021).[[27]](#footnote-28)

Considering the estimates of various researchers and other indirect indicators of the shadow economy, including the estimates of the shadow economy by the Latvian researchers prof. A. Sauka and prof. T. Putniņš, and Austrian researcher prof. F. Schneider, the SRS tax gap calculations and the cash flow indicator, it can be concluded that the **potential amount of taxes to be collected from the shadow economy in Latvia is within the range of EUR 2 billion to EUR 3.6 billion.**

It is important to keep in mind that national GDP is comprised of different sectors and that there are sectors where the shadow economy is unlikely, e.g. public administration, and sectors where the intensity of the shadow economy is higher. Given that researchers do not use a uniform approach to calculating the size of the shadow economy, i.e. the same GDP component (base) is not used, the results of estimating the size of the shadow economy vary. In addition, researchers extrapolate some of the available analytics to GDP when making assumptions about the overall size of the shadow economy. In order to assess the size of the shadow economy objectively and accurately, **it is required to conduct further in-depth analysis of the size of the shadow economy and its causes in specific sectors.**

Reducing the share of the shadow economy is a priority task as its size in Latvia is still high compared to other European countries, and it is therefore important to continue implementing measures to restrict the shadow economy in order to improve the business environment and promote voluntary compliance with tax obligations, reducing the administrative burden on taxpayers and increasing tax revenues in the State budget.

***Economic trends***

When assessing measures to reduce the shadow economy, it is important to take into account not only the actual situation of the national economy and the shadow economy, but also trends in recent years.

As regards labour tax revenues, to mitigate the negative impact of the measures introduced to limit the spread of COVID-19, the furlough support and subsidy support were paid in certain periods to the employees who are payers of national taxes in order to compensate for the absence of income and from which no labour taxes were withheld, in contrast to the labour income of employees. A total of EUR 156.24 million was paid in furlough support and subsidy support in 2021 and EUR 1.98 million was paid in 2022.

In 2022, labour tax revenue increased by EUR 1.00 billion or 17.6 per cent to EUR 6.64 billion. Such an increase in labour tax revenue has not been recorded before. Taxpayers reassessed their business activities in line with overall economic growth and also the impact of external factors that also resulted in higher incomes for employees which is the basis for the increase in labour income.

An analysis of the data reported by legal entity employers (excluding budgetary institutions) shows that the share of employers whose average calculated income for employees is above the national minimum wage is increasing (by 5.3 percentage points in 2022 compared to 2021).

At the same time, the current debt on labour taxes has also decreased, i.e. by EUR 26.35 million or 7.9 per cent to EUR 308.37 million on 1 January 2023 compared to 1 January 2022, the fastest decrease in current debt at the beginning of the year observed in recent years.

In summary, with regard to labour tax revenues, taxpayers are adapting to the current situation, while at the same time taking into account past experience during the period of restrictions, when aid was received in line with the reporting and tax situation, and trying to settle their obligations towards the State. Of course, all these processes are also the result of long-term work on behalf of the SRS both by providing support and facilitating compliance with obligations.

Considering the current economic situation and the ability of taxpayers to pay all taxes voluntarily, the SRS is cautious when assessing the fiscal benefit from implementing the measures for reducing the shadow economy.

It should be noted that the costs for ensuring the tax administration function increases with each successive supervision reinforcing measure, making each collected euro more expensive. Accordingly, the State should assess the implementation of effective measures, considering the costs of tax administration, minimising the administrative burden and weighing all the benefits for the common interest of society.

The Latvian economy grew moderately in the final months of 2022. According to data compiled by the Central Statistical Bureau of Latvia, gross domestic product (GDP) in 2022 increased by 2 per cent compared to 2021. Last year, GDP at current prices reached EUR 39.1 billion.[[28]](#footnote-29) The high uncertainty in the geopolitical environment affected both consumer habits and business investments, while foreign trade and substantially increased imports had a negative effect on economic growth rates. High inflation, with price growth rates outpacing wage growth, is eroding real income and purchasing power of the population. Economic growth is expected to return in Q3 of 2023, whereas overall GDP growth in 2023 is expected to be much more moderate than in 2022.

Retail trade increased by 4.3 per cent, including 6.5 per cent in non-food retail and 0.5 per cent in food retail. Wholesale, retail and repair of motor vehicles and motorcycles increased by 10.1 per cent, while wholesale trade declined significantly by 18.7 per cent.

Digital technologies are playing an increasingly important role in the area of health protection, enabling better health outcomes, allowing healthcare practitioners to spend more time with patients and taking of better data-driven and data-analysed systemic change decisions by administrative bodies. The recent crisis has also highlighted the necessity of timely access to electronic health records in order to ensure preparedness and responsiveness to health threats, not only for treatment but also for research, innovation, patient safety and regulatory, policy-making, statistical or personalised medicine purposes.[[29]](#footnote-30)

Given that the economy is not expected to grow rapidly in the next few years, it is not reasonable to expect a significant decrease in the shadow economy.

***Construction sector***

According to the data at the disposal of the Central Statistical Bureau of Latvia, the added value of construction output declined by 11.3 per cent in 2022, caused by declines in all three subsectors in all four quarters of the year. During the year, the volumes of building construction decreased by 9.8 per cent, that of civil engineering by 13.1 per cent, including roads and railways by 8.5 per cent, urban infrastructure by 17.3 per cent and other civil engineering by 36.4 per cent. Specialised construction activities decreased by 11.3 per cent year-on-year, including demolition and site preparation by 26.9 per cent, electrical installation, piping and other similar activities by 7.8 per cent, construction completion works by 18 per cent and other specialised construction activities by 7.8 per cent. In addition, from the end of 2020 there is a steady rise in the price of construction materials, increasing the risk of the shadow economy in the sector. Compared to September 2020, there was an overall increase in construction costs by 10.0 per cent, including a 14.3 per cent increase in construction material prices.

Historically there has been a high level of the shadow economy in the construction sector, reaching 40 per cent in 2015. Since 2016, sector-focused measures have been consistently introduced to reduce the shadow economy in the construction sector, with the construction sector itself participating and contributing significantly to improving the business environment in the sector. From 2015 to 2020, smart and comprehensive measures to restrict the shadow economy in the construction sector, including the introduction of the EDLUS, have had a positive effect, reducing the shadow economy rate by 11.3 percentage points over the period of six years.

According to the results of SSE Riga Centre for Sustainable Business researcher prof. A. Sauka and prof. T. Putniņš research “Shadow Economy Index for the Baltic Countries 2009–2022”[[30]](#footnote-31), the share of the shadow economy in the construction sector increased to 31.2 per cent in 2021 and by another 3.3 per cent in 2022, reaching 34.5 per cent (Figure 16).

Construction sector

Latvia

*Figure 16. Shadow Economy Index in Latvia and the construction sector from 2015 to 2022, % of GDP.*

Despite being one of the least affected sectors by the COVID-19 pandemic, construction continues to be affected by the global impact of the pandemic, with a continued decline in construction output in 2021. In 2022, Russia launched its military aggression against Ukraine and caused significant turbulence in the construction sector, with inflation reaching 28 per cent in some segments, making it very difficult to meet contractual commitments, including in public infrastructure projects. It should be noted that the cost of construction products increased the most, but labour costs also rose sharply, putting a heavy financial burden on the companies operating in the sector. An analysis of the conditions in the construction sector suggests that as the sector stabilises and businesses regain confidence, the share of the shadow economy will naturally start to decline.

However, to achieve an adequate reduction in the shadow economy, which is vital for the competitiveness of the sector, it would be necessary to improve the functioning of existing measures and to introduce additional measures in segments not covered by existing measures or where they fail to have an adequate impact.

In addition, the commitment of the construction sector to continue with the measures started to restrict the shadow economy and to develop new ones is positive, given the short-term trend of an increasing share of the shadow economy in the construction sector.

When analysing the measures taken in the past to restrict the shadow economy, the working group concluded that, overall, the measures taken in the construction sector were effective, yet some improvements were necessity in the future. The two most effective measures are the introduction of the EDLUS and a general binding agreement setting a sector-specific minimum wage.

What regards the use of the EDLUS and records in labour tax administration processes, the working group proposed measures to strengthen the control of the introduction of the EDLUS. According to the VEDLUDB data, only one third of construction contractors provide their services on sites subject to the EDLUS. Accordingly, two thirds of the construction contractors operate on sites where the EDLUS is not in place.

In order to ensure greater transparency in the sector, amendments to the law On Taxes and Fees were adopted on 22 June 2023, requiring the construction contractors to register in the EDLUS and submit to the VEDLUDB information on settlements made with subcontractors under construction contracts. Information on contracts and settlements will contribute to a stable financial flow in the fulfilment of construction contracts, in particular for small and medium-sized enterprises, and also to their gradual exit from the shadow economy.

At current construction prices and taking into account that the EDLUS has to be implemented in all construction works of group III structures and also in all construction works with a value exceeding EUR 350,000, it can be concluded that the EDLUS has not been implemented in all sites where it has to be implemented under the law On Taxes and Fees. In order to improve the functioning of the EDLUS framework and also its performance in restricting the shadow economy, it would be necessary to further:

* enhance and strengthen the supervision of the implementation of the EDLUS through regular inspections of construction sites;
* continue to base this supervision on risk assessments and analysis, making greater use of data from the construction information system where necessary.

The EDLUS is one of the most effective tools to reduce the shadow economy, but only under the condition that the use of the EDLUS is supervised and companies are aware of the serious consequences if the EDLUS is not used on construction site in accordance with the regulations.

It should be noted that the measures introduced in the construction sector until now have mainly targeted large construction sites. In order to achieve more effective restriction of the shadow economy, the draft plan includes a number of measures that can be applied to different sizes of construction sites according to the construction process, divided into three relative groups: continuing the measures for large construction sites and also focusing on medium-sized and small construction sites.

## 2.3. Scenarios and measures for reducing the shadow economy

Recognising that there are different approaches and methods for measuring the shadow economy, this plan uses data from the Austrian study by professor F. Schneider as a reference in developing possible scenarios for reducing the shadow economy by 2027, thus allowing a comparison with more than 30 countries, both European and global, and also comparison with the average indicators of European countries.

Several factors need to be taken into account when choosing a target scenario for reducing the size of the shadow economy:

1. In Latvia, most macroeconomic indicators are below the EU average, so these indicators have a greater impact on the shadow economy in Latvia than on average in other EU countries. In 2022, GDP per capita in the EU-27 was EUR 28 820, while in Latvia it was EUR 13 320, 56 per cent lower than in the EU-27[[31]](#footnote-32). The potential for reducing the size of the shadow economy would naturally be comparable. Latvia is unlikely to reach the EU average size of the shadow economy without reaching the EU average GDP over the same period.
2. The national research programme “Reduction of the Hidden Economy for Ensuring Sustainable Economic Development” concludes that the reduction projected under the preferred model would be around one percentage point over the next four years (note by the MoF: the research does not distinguish the public sector where the shadow economy is unlikely), but could be significantly higher than this ‘natural tendency’ if policy actions to reduce the shadow economy are successfully implemented.[[32]](#footnote-33) The projected reduction in the shadow economy would mitigate the recent increase in the shadow economy that emerged during the COVID-19 pandemic and continue the long-term trend of a gradual decline in the level of the shadow economy.
3. Tax morale in Latvia is lower than in Lithuania and Estonia (as evidenced by prof. A. Sauka research and the report by the European Parliament Committee on Fiscal Affairs), while changing people’s habits usually takes longer.
4. The costs for ensuring the tax administration function increases with each successive supervision reinforcing measure, making each collected euro more expensive. Accordingly, the State should assess the implementation of effective measures, weighing up all the benefits for the public interest.
5. Whatever measures are implemented to reduce the shadow economy, there will always be individuals operating in the grey sector who will purposefully seek to continue to evade taxes and remain outside the formal economy by changing their behaviour and using other tools and techniques.
6. It is important to keep in mind that national GDP is comprised of different sectors and that there are sectors where the shadow economy is unlikely, e.g. public administration. Researchers extrapolate some of the available analytics to GDP when making assumptions about the overall size of the shadow economy. In order to assess the size of the shadow economy objectively and accurately, **it is required to conduct further in-depth analysis of the size of the shadow economy and its causes in specific sectors.**

The shadow economy which according to the methods of Austrian prof. F. Schneider and Latvian researchers prof. A. Sauka, prof. T. Putniņš varies between 19.9 per cent and 26.5 per cent of GDP is a major constraint on economic growth and the business environment.

In compliance with the resultative indicators outlined in the plan for the purpose of reducing the shadow economy, i.e. to bring the shadow economy rate in Latvia closer to the European average, four scenarios were developed to reduce the scale of the shadow economy by 2027.

|  |  |
| --- | --- |
| Aggressive goal: -2.7 per cent (i.e. from 19.9 per cent to 17.2 per cent) | EUR 326 million |
| Ambitious goal: -1.8 per cent (i.e. from 19.9 per cent to 18.1 per cent) | EUR 218 million |
| Most realistic goal: -1 per cent (i.e. from 19.9 per cent to 18.9 per cent) | EUR 120 million |
| Moderate goal: -0.6 per cent (i.e. 19.9 per cent to 19.3 per cent) | EUR 72 million |

*Table 2. Scenarios for reducing the shadow economy.*

When assessing the scenario which aggressively aims at reducing the shadow economy by 2.7 percentage points to the EU average of 17.2 per cent, it was concluded that this scenario is too ‘disruptive’ for the current business environment and that there are many risks to achieving this aim in the short term. This would cause significant losses to merchants with long-term consequences, pushing them out of economic activity which does not outweigh the one-time budgetary benefit of EUR 326 million.

A similarly ambitious scenario which aims at reducing the shadow economy by 1.8 percentage points to 18.1 per cent of GDP over four years would require quite intense repressive actions by the SRS, pushing dishonest taxpayers out of economic activity rather than redirecting them from the shadow economy into the legal environment.

Given that the correlation of changes in the GDP rate with the shadow economy is around 1 to 3, when considering the scenarios for restricting the shadow economy and their fiscal effects, the implementation of the plan to restrict the shadow economy offers a scenario with a realistic goal.

**The realistic goal is to advance towards the EU average (17.2 per cent), reducing the size of the shadow economy by 1 percentage point to 18.9 per cent by 2027.** At the same time, the State should also set the most ambitious goal, i.e. to reach the average level of the shadow economy in European countries by 2030.

The realistic scenario can be achieved through an ambitious set of measures, as illustrated in the table of the shadow economy plan. The package of measures included in the plan is expected to generate EUR 120 million in additional revenue for the budget that in a way is also a challenge.

Conversely, the scenario which aims at reducing the shadow economy by 0.6 percentage points to 19.3 per cent of GDP by 2027 would be a moderate goal and would provide the government with additional funds of EUR 72 million by 2027 (Figure 17).

A graph of a number of colored lines

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31 European country average, F. Schneider research data

Ambitious goal. Moderate goal

Optimistic goal

F. Schneider research data. Realistic goal

*Moderate goal*

**EUR 72 million**

*More realistic goal*

**EUR 120 million**

*Ambitious goal*

**EUR 218 million**

*Aggressive goal*

**EUR 326 million**

*Figure 17. Scenarios for reducing the shadow economy and their impact on national budget.*

***Calculation methodology:***

GDP (2022) – EUR 38 870 million

1 per cent of GDP EUR 389 million

31 per cent share of taxes of GDP

EUR 389 million \* 31 per cent = EUR 120 million

Table 3 shows the annual breakdown of revenue according to the implementation of the measures.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Measures | Fiscal impact, mln. EUR | | | |
| 2024 | 2025 | 2026 | 2027 |
| Restriction of the shadow economy | 12 | 40 | 80 | 120 |

*Table 3. Fiscal impact of the measures of the Shadow Economy Restriction Plan for 2024–2027 on an annual basis.*

The implementation of the measures included in the plan will be ensured by the responsible and participating ministries within the existing funding or, where necessary, through fiscally neutral proposals during the preparation of the current annual budget.

According to the scenario developed for reducing the size of the shadow economy by 2027, aiming to reduce the shadow economy by 1 percentage point, and the package of measures included in the plan, it is expected to generate additional revenue for the budget in the amount of EUR 120 million.. The measures of the plan were divided into five courses of action, determining an expected fiscal benefit for each:

Course of action 1 – Horizontal measures and reduction of cash in circulation – EUR 55 million;

Course of action 2 – Information and data exchange – EUR 1 million;

Course of action 3 – Measures in the construction sector – EUR 16 million;

Course of action 4 – Measures in the health sector – EUR 7 million;

Course of action 5 – Other measures to improve business competitiveness – EUR 41 million.

Figure 18 below illustrates the key measures of the plan to restrict the shadow economy. A full outline of the measures is provided in Section 4 herein.

**1. Horizontal measures and reduction of cash in circulation**

A screenshot of a computer

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1. Reduction of the **market share of illegal excisable goods.**

2. Reduction of the number of companies with long-term **negative equity**, improvement of simplified winding-up proceedings, educating of companies.

1. Provision of **e-referral** data and related specialist reports, laboratory referrals and results data **in the patient’s electronic health records in the Unified Electronic Information System of the Health Sector.**

2. Introduction of a **risk** system in the National Health Service data accrual systems.

3. **Revision** of the **laws and regulations** and standards.

4. Separate identification of telemedicine service providers in **the Register of Medical Treatment Institutions.**

1. Lowering of the **threshold for the EDLUS implementation** from EUR 350 000 to **EUR 170 000.**

2. Encouraging of construction sector associations to conclude **general** **agreements** in line with current wage levels in the sector.

3. Imposing of a statutory obligation to submit **information to the CIS** on the data included in a **construction contract.**

4. Imposing of an obligation on a private individual to submit information to the CIS **on the** **origin of funds intended for construction works.**

5. Reduction of the area of the construction site where **the builder can construct the house on his or her own** from 400 m3 to **170 m2.**

6. Imposing of the obligation that **payments for services** for which the client is obliged to submit documents after completion of the construction works envisaged in the project in order to put the building or civil engineering structure into operation are made only **in the form of non-cash payments.**

1. Introduction of **e-receipts** as a mandatory requirement for the use of medical services to be included as eligible expenses in the annual income tax return.

2. Identification databases and registers for structured data dissemination in the DAGR in order to facilitate information exchange and data use between institutions.

3. Expansion of the SRS public databases, publishing information on the amount of taxes paid on a quarterly basis.

1. Use of taxpayer rating in **public procurements.**

2. Further discussions on the approach to indirect taxation, inter alia, in respect of sectoral exceptions where there is a general agreement.

3. Encouraging of sectoral associations to conclude **general** **agreements** in line with current wage levels in the sector.

4. Implementation of the electronic circulation system for **e-invoices.**

5. Assessment of whether the existing personal income declaration procedures needs to be supplemented in order to reduce the shadow economy, promote a tax-paying culture, and at the same time not increase the administrative and bureaucratic burdens. Identification of a conceptual solution for the phasing-in of the general principle of **declaring personal income.**

6. Determining **non-cash payments as the primary method for the payment of wages.**

7. Imposing of reporting of cash **deposits and withdrawals in ATMs.**

8. Obligation for businesses with an annual turnover **exceeding EUR 50 000** to allow customers **to pay** also **using non-cash payments.**

9. Promotion of non-cash payments (POS terminals)

**5. Measures to improve business competitiveness**

**4. Measures in the health sector**

**2. Information and data exchange**

**3. Measures in the construction sector**

*Figure 18. Key measures of the Shadow Economy Restriction Plan for 2024–2027.*

In order to ensure the development of the most efficient and effective policy recommendations, a national research programme was implemented, using the ‘knowledge bank’ of good practice policy measures to restrict the shadow economy developed by both Eurofoundand the European Platform Tackling Undeclared Work (EPTUW) and also the technical reports on specific policy measures prepared by the EPTUW, resulting in science-based policy recommendations. Following the policy recommendations developed by the researchers, the plan included a number of measures, e.g.:

* an awareness-raising campaign for employees, communicating to the public the benefits of fully declared labour and the risks of insufficient payment of labour taxes;
* use of taxpayer rating in public procurements (including assessing the possibility of using rating in companies related to public procurement);
* implementation of the electronic circulation system for supporting documents (e-invoices);
* replacement of cash with digital payments by promoting the introduction of POS terminals at trading venues;
* integration of existent information systems by State and municipal authorities with the DAGR in order to start receiving data from other authorities that is necessary for the analysis and identification of the shadow economy risks in the core business processes;
* expansion of the SRS database;
* further discussions on the approach to indirect taxation. Inter alia, in respect of sectoral exceptions where there is a general agreement providing for a substantial increase in the national minimum wage or hourly rate in the sector of at least 50 per cent above the national minimum wage or hourly rate.

In the light of the aspects emphasised in science-based policy recommendations by prof. A. Sauka regarding the necessity to facilitate closer cooperation between different authorities, a measure was included in the plan to implement pilot projects on the exchange of information and data between public authorities using the Data Dissemination and Management Platform (hereinafter – the DAGR). The DAGR aims at improving information exchange and interoperability in public administration and making data available with definite access times. By connecting to the DAGR, national registers and information systems will be provided with a single, centralised data dissemination platform optimised for high performance in processing data requests. Consequently, each authority will have the possibility of significantly reducing the capacity of its data dissemination solutions, or even abandoning the development and maintenance of its data dissemination solutions altogether. Public administration will be given the opportunity to aggregate data from potentially all public authorities into a single data dissemination platform that can be used by data recipients to retrieve real-time data from the information systems of data providers. By implementing the project, a basic infrastructure will be built for the unified management of data dissemination and data access authorisations that will ensure an environment for managed data flows between businesses, population and public administration.

When considering the possibility of influencing the behaviour of taxpayers, educational and awareness-raising information campaigns are planned to raise tax morale, which is in line with the recommendations of prof. A. Sauka. It is also important to communicate with the public, explaining government decisions and raising awareness of government processes, which is an important way to stimulate greater public involvement and trust.

3. Aim and Courses of Action of the Plan

**The aim of the plan** is to implement targeted measures to reduce the shadow economy in priority sectors of the national economy and horizontal measures to improve the business environment and promote voluntary compliance with tax obligations, while focusing on the identified factors and risks affecting the shadow economy, in cooperation with sectoral ministries, social and cooperation partners.

For the achievement of the aim of the plan, the measures are structured according to the following courses of action:

1. Horizontal measures and reduction of cash in circulation.

2. Information and data exchange.

3. Measures in the construction sector.

4. Measures in the health sector.

5. Other measures to improve business competitiveness.

**The resultative indicator of the plan**: as a result of the implementation of the measures included in the plan in the horizontal direction and within the priority sectors of the national economy, provided that the country maintains a stable economic development, the overall scale of the shadow economy will decrease by 1 per cent of gross domestic product by 2027, bringing the shadow economy rate in Latvia closer to the European average, down from 19.9 per cent to 18.9 per cent.

Reduction of the share of the shadow economy is a priority task that is important for the development of the national economy sectors, boosting of competitiveness and social welfare, and it is therefore necessary to continue to pursue the national policy to restrict the shadow economy by fostering cooperation between public authorities. In order to ensure a high-quality and orderly business environment for entrepreneurs, promoting the development of business and enhancing competitiveness, the Shadow Economy Restriction Plan for 2024–2027 has been developed in cooperation with sectoral experts, prioritising the reduction of the shadow economy in specific sectors of the national economy and the implementation of horizontal measures.

In order to analyse the effectiveness of the measures implemented and to track changes in the shadow economy, it is important to regularly monitor indicators of the size of the shadow economy throughout the implementation period, such as:

* the share of taxpayers with no significant tax compliance risks, e.g. the share of ‘A’ class rated companies;
* changes in the volume and use of cash;
* scientific research data, e.g. A. Sauka and T. Putniņš research “Shadow Economy Index for the Baltic Countries”, F. Schneider research on the shadow economy in European countries, etc.;
* results of sociological surveys of the population on tax morale;
* sectoral data, e.g. the ‘envelope wage’ index in the field of construction;
* sector-specific indicators, e.g. insolvency rates of contractors in the field of construction, etc.

4. Shadow Economy Restriction Plan for 2024–2027

| No. | Measure | Operating result | Resultative indicator | Responsible authority | Co-  responsible authorities | Deadline |
| --- | --- | --- | --- | --- | --- | --- |
| Course of Action 1 – **Horizontal measures and reduction of cash in circulation** | | | | **Fiscal benefit: EUR 55 million** | | |
| Course of Action 1. Task 1. **Strengthening of public-private partnerships: use of ratings in public procurements and public procedures.** | | | | Fiscal benefit: EUR 15 million | | |
| 1.1.1.1. | Use of the overall taxpayer rating for procurements specified in Section 9 of the Public Procurement Law (PPL), thus promoting the advantages of ‘A’ class rated taxpayers. | Amendments to the regulatory framework have been drafted to give ‘A’ class rated taxpayers an advantage in small procurements. | The share of ‘A’ class rated taxpayers in the total number of segmentable taxpayers in the sector increases by 1 per cent. | MoF | IUB | 30.12.2025 |
| 1.1.1.2. | Use of taxpayer rating in public procurements without imposing requirements to verify tax compliance for ‘A’ class rated taxpayers. | Amendments to the regulatory framework have been drafted regarding the use of taxpayer ratings in public procurements. | Reduced administrative burden for ‘A’ class rated merchants. | MoF | IUB,  SRS,  SRDA | 30.12.2025 |
| 1.1.1.3. | Use of taxpayer rating in public procurements, cascading down to the companies involved. | Proposals and, where necessary, amendments to the regulatory framework have been drafted regarding the use of taxpayer ratings in public procurements. | Increase in voluntary tax compliance. | MoF | IUB | 30.12.2025 |
| 1.1.2. | Incentives and advantages offered to ‘A’ class rated companies in public administration procedures, including shortened deadlines for providing responses, licences, permits. | In order to maintain and develop the advantages of the In-depth Cooperation Programme, the regulatory framework will be amended to move towards a new approach based on publicly available ratings, so that there would be motivation for improving the ratings, and so that the rating criteria contribute to overarching economic policy objectives, including boosting exports and productivity. | Reduced administrative burden for ‘A’ class rated merchants. | ministries,  SRS | - | 30.12.2026 |
| 1.1.3. | Provision of information on merchants in a user-friendly format for use in the process of issuing and monitoring street trading permits.  Ensuring that local authorities verify that merchants pay their taxes and create jobs before issuing permits for street trading. | Procedures have been established to ensure that the merchant pays taxes and creates jobs before municipal authorities issue permits for street trading.  The SRS prepares informative material on the level of tax payment by merchants and its significance from the point of view of the risks of non-payment of taxes. | Decrease in the number of people receiving envelope wages and employers not paying taxes. | MoEPRD | LALRG,  SRS | 30.12.2025 |
| Course of Action 1. Task 2. **Restrictions on the circulation of cash.** | | | | Fiscal benefit: EUR 18 million | | |
| 1.2.1. | Determining non-cash payments as the primary method for the payment of wages. | Improved solutions to enhance employee rights and protection in the area of remuneration, without restricting the employee’s ability to pay for consumer goods and services if this is not possible in cashless form and leaving the employee and employer the option to agree on the payment of wages in cash. | Decrease in the number of people receiving envelope wages and employers not paying taxes. | MoW | MoF,  SRS | 30.12.2024 |
| 1.2.2. | Imposing the obligation on employers to inform the SRS of the fact that an employee’s wage is paid in cash. | Amendments to laws and regulations have been drafted, specifying the document (e.g. a RoE or a statement) by which an employer informs the SRS of a cash payment. | Decrease in the number of people receiving envelope wages and employers not paying taxes. | MoW | MoF,  SRS | 30.12.2024 |
| 1.2.3. | Introduction of threshold declarations for cash deposits and withdrawals (reporting of cash deposits and withdrawals in ATMs). | A regulatory framework has been developed which imposes the obligation on credit institutions to provide quarterly information to the SRS on deposits and withdrawals in ATMs or branches of credit institutions. | Increased transparency of the circulation of cash and the ability of credit institutions to report all transactions above a certain threshold, without having to assess whether the transactions are suspicious. | MoF | SRS | 30.12.2024 |
| 1.2.4. | Further discussions on the approach to indirect taxation. Inter alia, in respect of sectoral exceptions where there is a general agreement. | Discussions will continue on the approach to indirect taxation. Inter alia, in respect of sectoral exceptions where there is a general agreement providing for a substantial increase in the national minimum wage or hourly rate in the sector of at least 50 per cent above the national minimum wage or hourly rate. | Promoting voluntary compliance with tax obligations. | MoF | SRS | 30.12.2025 |
| 1.2.5. | Encouraging of sectoral associations to conclude or revise general agreements in line with current wage levels in the sector (e.g. health, beauty care, construction, etc.). | Supplementing the terms of general agreements with appropriate remuneration according to occupation and qualifications. | Voluntary tax compliance is increasing, including labour tax revenue for the budget. | Responsible sectoral ministries  (practical action: LBNA,  LBAS,  LBP) | - | 30.12.2027 |
| 1.2.6. | Encouraging of sectoral associations to stimulate their members to conclude collective agreements. | Promoting collective agreement initiatives. | Improved competitiveness of businesses, working conditions and social guarantees for employees, while reducing the involvement of subjects in the shadow economy. | MoW responsible for the sector  (practical action: LBAS, sectoral associations) | - | 30.12.2027 |
| 1.2.7. | Monitoring of cash flow. | Preparation of reports on cash flow analysis (with an emphasis on cash of unknown origin), explaining the reasons for the origin and the dynamics of cash use. | Annually updated reports on cash flow analysis, explaining the reasons for the origin and dynamics of cash use. | FIU,  SRS,  (in cooperation with the BoL) | MoF | 30.12.2024  30.12.2025  30.12.2026  30.12.2027 |
| Course of Action 1. Task 3. **Conceptual solution for the general principle of declaring personal income is identified.** | | | | Fiscal benefit: EUR 7 million | | |
| 1.3.1. | Assessment of whether the existing personal income declaration procedures needs to be supplemented in order to reduce the shadow economy, promote a tax-paying culture, and at the same time not increase the administrative and bureaucratic burdens.  This includes identification of a conceptual solution for the phasing-in of the general principle of declaring personal income, identifying the necessary exceptions. | Assessment of the existing declaration solution to ensure that filing personal income tax returns is simple and convenient, including assessment of whether additions to the system are needed to reduce the shadow economy, improve tax morale, while avoiding additional administrative and bureaucratic burdens.  This includes:  1. Discussions with the public on the concept of declaring personal income.  2. Identification of the data available to the SRS and the potential for the use thereof.  3. Identification of data missing for quality analytics. | The basic principles of equality, certainty, convenience, efficiency are complied with.  Administrative burden reduced and efficiency of tax administration supervision improved.  Ensuring of communication with the public. | MoF | SRS | 30.12.2025 |
| 1.2.3. | In conjunction with measure 1.3.1, assessment of the need to require the manager of portfolio investments and similar financial instruments to withhold tax at source and report the amount of taxable income to the SRS. | In order to reduce the possibility of income concealment and to provide the SRS with an overview of the income earned by natural persons subject to PIT and the changes thereof in relation to the transactions conducted by them and income earned during the tax year, the scope of information to be provided to natural persons should be expanded. | The payer of income withholds PIT at source on the income from the portfolio management service or provides information to the SRS on the income from the portfolio management service. | MoF | SRS | 30.12.2025 |
| 1.2.4. | Assessment of the profile of people of working age with no income and/or with long-term outstanding debts. | Assessment of the profile of working-age people with no income and/or with long-term outstanding debts (including non-payers of child maintenance who exceed 40 thousand) and a possible solution for returning them to the legal labour market. | A solution is found to bring debtors back into the legal labour market by reducing the number of entities operating in the shadow economy. | MoF | MoJ,  LDDK | 30.12.2025 |
| Course of Action 1. Task 4. **Promoting the use of non-cash transactions.** | | | | Fiscal benefit: EUR 15 million | | |
| 1.4.1. | Implementation of the electronic circulation system for supporting documents (e-invoices). | Introduction of a mandatory requirement for merchants operating in the B2B segment to use e-invoices in structured electronic form and provision of a technical solution for the circulation of e-invoices. | Ensuring of the use of e-invoices in structured electronic form. Better tracking of VAT payment obligations through the introduction of real-time reporting. | 1. SRS  2. MoEPRD | MoF | 30.12.2025 |
| 1.4.2. | Obligation for businesses with an annual turnover exceeding EUR 50 000 to allow customers to pay also using non-cash payments. | Reduced cash transactions in trade that will contribute to more transparent tax administration in this sector.  According to the preliminary assessment of the SRS, 779 taxpayers could be affected, whereof 177 taxpayers are active in the trade sector (NACE 46 and NACE 47). | Reduced number of cash transactions in trade. | MoF | SRS | 30.12.2024 |
| 1.4.3. | Promotion of cashless payments. | Encouraging the public and businesses to use more cashless payment solutions in their daily payments, including by promoting financial literacy, educating the public about the benefits of cashless solutions and their safe use, thereby changing cash use habits. | 1. Solutions are developed to promote the use of cashless payments. 2. Public financial literacy for the safe use of cashless solutions is enhanced. 3. Public interest in more frequent use of cashless solutions in everyday life is enhanced. | MoF responsible for the sector  (practical action: FLA) | - | 30.12.2025 |
| 1.4.4. | Attribution of the statutory provision provided for in the Road Traffic Law with regard to reporting to the SRS also to the registration of the prohibition on alienation to vehicles aged between 5 and 10 years. | Encouraging the implementation of measures to reduce tax evasion in the field of trade in used vehicles involving natural persons and preventing tax evasion.  Faster, more effective prevention of tax evasion by individuals (PIT, VAT). | Increasing tax revenue from the trade of motor vehicles. | MoF | SRS,  MoT,  RTSD | 30.12.2024 |
| Course of Action 2 – **Information and data exchange.** | | | | **Fiscal benefit: EUR 1 million** | | |
| Course of Action 2. Task 1. **Introduction of e-receipts.** | | | | Fiscal benefit: EUR 0.3 million | | |
| 2.1.1 | Introduction of e-receipts as a mandatory requirement for the use of medical and therapeutic services and for the improvement of qualifications, the acquisition of a speciality, the acquisition of education, including interest-based education programmes for children, to be included as eligible expenses in the annual income tax return. | Reduced time and resources spent on filing and processing annual income tax returns, facilitated exchange of data between institutions and service providers and the SRS, and also faster tax refunds for the population.  The possibility of simplifying data transfer for service providers has been assessed. Where necessary, amendments made to laws and regulations. | Simplified processes and reduced administrative burden. | MoF,  SRS | MoH,  MoES,  MoE | 30.12.2026 |
| Course of Action 2. Task 2. **Interinstitutional information exchange and disclosure.** | | | | Fiscal benefit: EUR 0.7 million | | |
| 2.2.1. | Public administration and municipal authorities identify their information resources maintained outside of information systems, organise the information in the form of structured data and start publishing the datasets needed by other institutions to facilitate the exchange and use of information and data between institutions to restrict the shadow economy. | Identification of information resources (databases and registers) maintained, structured data and improved information exchange and data use between institutions.  Data sources in the pilot project sectors:   * commercial carriage of passengers by taxi (Taxi Drivers Register); * SRS information from databases; * Register of Security Guard Activities; * Register of Educational Institutions of the State Education Information System; * information on allowances granted by local governments; * information from the State Environmental Service databases.   The SRS identifies information[[33]](#footnote-34) (structured data) that is necessary to enable automated processes based on data analysis and is available to other institutions by submitting it to the MoEPRD. | Creation of a single information access point that will provide State administration institutions with data to be used in institutional data analysis solutions and core business processes to identify shadow economy risks.  Improved data exchange between public authorities. | MoEPRD  MoT  SRS,  MoI IC,  MoES,  local governments,  SES | - | 30.12.2025 |
| 2.2.2. | Integration of existent information systems by State and municipal authorities with the DAGR in order to start receiving data from other authorities that is necessary for the analysis and identification of the shadow economy risks in the core business processes. | The technical access rights of the DAGR will be ensured in accordance with the Data Protection Regulation, in the context of the rights enshrined in the legal framework.  Improvement of supervision measures and timely identification of risks in core business processes:   * SRS; * municipal registers (development can be ensured, including through EU funds[[34]](#footnote-35)). | Creation of a single information access point that will provide State administration institutions with data to be used in institutional data analysis solutions and core business processes to identify shadow economy risks. | MoEPRD  SRS  local governments | - | 31.12.2025 |
| 2.2.3. | The possibility to improve data exchange between the SRS and the Latvian Insurers Association assessed. | Possibilities to improve data exchange between the SRS and Latvian insurance companies assessed.  Potential risks related to the processing of personal data assessed and the necessary amendments to the laws and regulations identified. | Solutions to improve data exchange identified. | SRS,  MoF,  LIA | DSI | 30.12.2025 |
| 2.2.4. | Expansion of the SRS database. | Amendments to the law On Taxes and Fees have been drafted, envisaging the publishing of quarterly information on the total amount of taxes paid by merchants, separately indicating the total amount of PIT and MSSIC, and also the average number of persons employed. | Public transparency in the collection of taxes (fees) ensured, the public, cooperation and business partners informed. | MoF | SRS | 30.12.2025 |
| 2.2.5. | Communicating to the public the benefits of fully declared labour and the risks of insufficient payment of labour taxes. | 1. Development of a visual tool to show the negative impact of not fully declaring taxes and social contributions on an individual.  2. Youth-targeted informative campaign ‘Where is my money?’ on the importance of a tax-paying culture and compliance with labour laws, involving the SRS in various youth education activities and training for school-age children as part of ‘Ready for Life’.  3. Informing taxpayers about how tax money is spent (infographics, press releases, etc.), improving understanding of how budgets are used for public services, raising tax morale. | 1. Improved understanding among youth of the benefits of paying taxes and the advantages of receiving public services.  2. Number of information and educational events organised. | SRS,  MoF | - | 30.12.2027 |
| Course of Action 3 – **Measures in the construction sector.** | | | | **Fiscal benefit: EUR 16 million** | | |
| Course of Action 3. Task 1. **Strengthening of the EDLUS, VEDLUDB, CIS data analytics.** | | | | Fiscal benefit: EUR 7 million | | |
| 3.1.1. | Lowering of the threshold for the EDLUS implementation  (from EUR 350 000 to EUR 170 000). | The use of the EDLUS on construction sites expanded.  Mainly attributable to large and medium-sized construction sites. | The number of the EDLUS sites and the number of hours of RoE at the VEDLUDB increase. | MoE | MoF,  LBP | 30.12.2024 |
| 3.1.2. | Inclusion of the obligation in laws and regulations for the initiator of a construction plan to submit to the CIS information on the price of the construction contract, the planned price of the construction works in the case of the constructor, and also to provide for the possibility to make a selection of the costs of implementation of construction plans (price of construction works) by type of use of the structures. | Information is provided on the price of the planned construction works according to the types of use. Mainly attributable to large and medium-sized construction sites. | Amendments are made to the regulatory framework.  Improved CIS functionality. | MoE | LBP | 30.12.2025 |
| 3.1.3. | Improvement of data exchange between the CIS and information systems maintained by the SRS. | Establishing of data exchange for better tax administration, setting the scope of mandatory data, including construction costs. Information is exchanged between the CIS and the SRS until the DAGR project is implemented, and after the DAGR project is implemented – using the full DAGR functionality.  Mainly attributable to large, medium-sized and small construction sites. | Requirements and solutions for adapting information systems have been defined and also proposals have been developed for attracting the necessary additional funding. | SRS,  SCCB,  SRDA | LBP | 30.12.2026 |
| 3.1.4. | Reduction of the range of reliability of the VEDLUDB data from 20 per cent to 15 per cent. | Amendments are made to the regulatory framework.  Mainly attributable to large and medium-sized construction sites. | The hours declared by employers and the wages and taxes declared by employees increase. | MoE | - | 30.12.2025 |
| 3.1.5. | Control and monitoring of the use of the EDLUS on construction sites. | The SRS controls and monitoring of the use of the EDLUS on construction sites. | Prepared report to the Cabinet on the effectiveness of the use of the EDLUS and the control and monitoring measures taken. | MoF  (SRS) | MoE,  MoW | 01.03.2024  01.03.2026 |
| Course of Action 3. Task 2. **Requirements for private individuals in the construction process.** | | | | Fiscal benefit: EUR 2 million | | |
| 3.2.1. | In the case of the construction of a residential house, reduction of the area of the construction site where the builder can construct the house on his or her own without involving a construction contractor from 400 m3 to 170 m2. | Amendments to the Construction Regulations of Buildings have been drafted.  Mainly attributable to small construction sites. | Decreased amount of non-declared private sector services. | MoE | - | 30.12.2025 |
| 3.2.2. | Obligation for a private individual to provide information to the CIS on the origin of the funds intended to be used for the works. | Amendments to the regulatory framework have been drafted with regard to the provision of information by natural persons on the origin of funds.  Mainly attributable to medium-sized and small construction sites. | Improved CIS functionality. | MoE | SCCB,  MoF | 30.12.2025 |
| 3.2.3. | Imposing of the obligation that payments for services for which the client is obliged to submit documents after completion of the construction works envisaged in the project in order to put the building or civil engineering structure into operation are made only in the form of non-cash payments. | The regulatory framework has been amended to ensure that, after completion of the construction works envisaged in the project, payments for such services as performance surveys, electrical wiring inspections, inspections of heating appliances, equipment and the technical condition of chimneys and natural ventilation ducts are made only in the form of non-cash payments. | Decreased amount of non-declared private sector services. | MoF | MoE | 30.06.2024 |
| Course of Action 3. Task 3. **Strengthening of the public-private partnership in the construction sector.** | | | | Fiscal benefit: EUR 7 million | | |
| 3.3.1. | Encouraging the construction sector association to revise the general agreements in line with the current wage levels in the sector. | Supplementing the terms of general agreements with appropriate remuneration in construction according to occupation and qualifications. | Voluntary tax compliance has increased, including labour tax revenues to the budget. | MoE responsible for the sector (practical action: LBNA,  LBAS) | MoE,  MoW,  LBP | 30.12.2027 |
| 3.3.2. | Supplementation of public procurement guidelines, encouraging the use of the EDLUS to determine the most economically advantageous tender where this will not be mandatory. | Public procurement guidelines have been supplemented. | Increased number of the EDLUS users. | MoE and MoF responsible for the sector (practical action: LBNA,  IUB) | LBP | 30.06.2024 |
| 3.3.3. | Improvement of the legal framework and strengthening of supervision to prevent the construction of illegal engineering networks. | 1. Improved and simplified legal framework for preventing illegal construction and dismantling of illegal electronic communications networks or illegal overhead lines. 2. Enhanced supervision to ensure that only companies registered in the in the Register of Construction Merchants carry out construction work. Administrative liability imposed for carrying out work without registration.   Municipalities have a detailed plan in place to survey, detect and dismantle (including forcibly dismantle) illegally and improperly constructed electronic communications networks within a set timeframe.  Completed assessment of the necessary solutions to ensure that municipalities, when granting immovable property tax rebates, would verify compliance with construction legislation, including legislation governing electronic communications networks. Informative material on the process of detection and dismantling of illegally constructed electronic communications networks has been developed, communication with construction authorities has been ensured and awareness and involvement of local authorities has been promoted. Communication with owners of electronic communications networks, urging them to take the steps required by the regulation to legalise their networks and informing them of the consequences of failing to do so. | Reduction of illegal construction.  At least 50 per cent of the non-compliant electronic communications networks in five largest municipalities removed (dismantled and/or legalised) by 2027. | 1., 3. MoE, MoT  2. MoEPRD, LIKTA | 1. LIKTA  2. LALRG | 30.06.2025 |
| Course of Action 4 – **Measures in the health sector.** | | | | **Fiscal benefit: EUR 7 million** | | |
| Course of Action 4. Task 1. **Strengthening of data analytics in the health sector.** | | | | Fiscal benefit: EUR 2 million | | |
| 4.1.1. | Provision of e-referral data and related specialist reports, laboratory referrals and results data in the patient’s electronic health records in the Unified Electronic Information System of the Health Sector (including assessment of the possibility of providing this data in a structured format). | 1. Assessment of the necessary amendments to laws and regulations.  2. Amendments have been made to Cabinet Regulation No. 265 of 4 April 2006, Procedures for Keeping Medical Documents, and Cabinet Regulation No. 134 of 11 March 2014, Regulations Regarding the Unified Electronic Information System of the Health Sector. | Information is provided to supervisory authorities for the analysis of the volume of health services according medical treatment institutions and doctors. | 1. MoH, NHS  2. NHS, HI, SRS, MoH | - | 1. 01.01.2025  2. 30.12.2027 |
| 4.1.2. | Extension of the possibilities of the SRS IS to compare the income declared by taxpayers in the health sector with the data declared in the annual income declaration of natural persons in the D4 annex. | Completed extension of the possibilities of the SRS IS to compare the income declared by taxpayers in the health sector with the data declared in the annual income declaration of natural persons in the D4 annex.  The necessity and possibility to separately identify dental expenses in the D4 annex of the declaration has been assessed.  Ensured in-depth risk assessment of the dental sector. | Increased voluntary tax compliance. | SRS,  MoF | - | 30.12.2024 |
| 4.1.3. | Implementation of the risk framework in the NHS data storage systems and use of the results thereof in the supervision of the NHS service providers. | Improved NHS data accumulation systems, including risk management controls. | Risk management controls are integrated with the NHS data storage system and are used in daily work. | NHS | HI | 30.12.2027 |
| Course of Action 4. Task 2. **Definition of a clear legal framework in the health sector.** | | | | Fiscal benefit: EUR 0.25 million | | |
| 4.2.1. | Ensuring of the same terminology for medical treatment institution units and branches in the laws and regulations governing business and healthcare. | 1. Completed assessment of laws and regulations.  2. Amendments have been made to laws and regulations, ensuring that the terminology for medical treatment institution units and branches is the same in the laws and regulations governing business and healthcare. | Improved Register of Medical Treatment Institutions. | 1. HI, MoH  2. MoH | 1. MoE, MoJ, HEA  2. MoE, MoJ, HEA | 1. 30.06.2024  2. 30.12.2024 |
| 4.2.2. | Considering of the possibility of separate identification of telemedicine service providers in the Register of Medical Treatment Institutions. | Assessment of the possibility of including telemedicine service providers in the Register of Medical Treatment Institutions.  In the event of a positive decision, amendments to laws and regulations and changes to the Register of Medical Treatment Institutions are made. | Information on telemedicine service providers is available in the Register of Medical Treatment Institutions. | HI,  MoH | - | 30.12.2025 |
| 4.2.3. | Linking of the recertification of dental specialities to the volume requirements for dental services. | The scope of requirements for dental services in the recertification criteria for dental specialities set by the certifying bodies are introduced. | Promoted tax payments for dental services. | MoH  (in cooperation with the LMA,  LDA) | - | 31.12.2024 |
| Course of Action 4. Task 3. **Strengthening of the public-private partnership in the health sector.** | | | | Fiscal benefit: EUR 3 million | | |
| 4.3.1. | Encouraging of sectoral associations to conclude collective agreements in sectors with a high scale of the shadow economy, including health and beauty care sectors. | By concluding sectoral collective agreements, the minimum wage/hourly rate is determined for persons employed in the sector that will encourage the conformity of private sector wages with actual wages. | Increase in PIT and MSSIC as a result of the monitoring of the general agreements. | MoH  (in cooperation with the LDDK,  LVSADA,  LBAS) in respect of the health sector | HEA,  MoE | 30.12.2024 |
| 4.3.2. | Conclusion of a cooperation agreement (memorandum) between the HI, CRPC, SRS, HEA and other non-governmental organisations on provision of information concerning dishonest commercial practices in the health service and beauty care sectors. | A cooperation agreement has been signed between the HI, CRPC, SRS, HEA and other public organisations and the exchange of information on dishonest commercial practices in the health service and beauty care sectors has been ensured. | Increased voluntary tax compliance. | HI,  CRPC,  SRS,  (in cooperation with the HEA,  NGOs) | - | 31.12.2024 |
| Course of Action 4. Task 4. **Provision of information and public education measures in the health sector.** | | | | Fiscal benefit: EUR 0.5 million | | |
| 4.4.1. | Organisation of an informative campaign to inform people about the health risks of informal beauty care and equivalent services. | Communication implemented and an informative campaign organised to inform about the health risks of informal beauty care and equivalent services (including the importance of proof of payment). | One informative campaign organised. | SPKC,  HI,  (in cooperation with HEA),  CRPC | SRS | 30.12.2027 |
| 4.4.2. | Educating of medical practitioners on the necessity to register economic activities with the SRS or the appropriate form of entrepreneurial activity in the Enterprises Register (if systematic activities are carried out in exchange for remuneration) and the Register of Medical Treatment Institutions to prevent cases where activities are not properly registered but the service is provided in a medical treatment institution where premises are rented. | Medical practitioners are informed of the necessity to register their economic activities with the SRS or the appropriate form of entrepreneurial activity in the Register of Enterprises and the Register of Medical Treatment Institutions. | 1. Informative material for medical treatment institutions has been prepared.  2. The informative material has been published on the websites of the HI and the professional organisations of medical practitioners.  3. Professional organisations of medical practitioners are informed of the necessity to register their economic activities with the SRS or the appropriate form of entrepreneurial activity in the Register of Enterprises and the Register of Medical Treatment Institutions. | HI,  SRS | LMA | 30.12.2025 |
| 4.4.3. | Educating of the public about the Register of Medical Practitioners and Medical Treatment Support Personnel and the Register of Medical Treatment Institutions and the use thereof prior to receiving healthcare services. | Public awareness of the importance of registers in receiving quality healthcare. | Public awareness activities on the social networks and website of the HI, and also in the media. | HI | LPOT | 30.12.2025 |
| Course of Action 4. Task 5. **Definition of a clear legal framework in the beauty care sector.** | | | | Fiscal benefit: EUR 0.25 million | | |
| 4.5.1. | Revision of the laws and regulations regarding beauty care services for the purpose of promoting safe provision of beauty care services to consumers by medical practitioners. | 1. The laws and regulations that are binding in the field of the provision of beauty care services have been revised (Cabinet Regulation No. 268 of 24 March 2009, Regulations Regarding the Competence of Medical Practitioners and Students of First Level or Second Level Professional Higher Medical Education Programmes in Medical Practice and the Scope of Theoretical and Practical Knowledge Thereof, and Cabinet Regulation No. 264 of 23 May 2017, Regulations Regarding the Classification of Professions, Basic Tasks and Basic Qualification Requirements Corresponding to the Profession, etc.).  Possibilities to impose stricter administrative liability in the event of repeated offences have been assessed.  2. Laws and regulations have been drafted in accordance with the assessment. | Safe provision of beauty care services by medical practitioners to consumers has been promoted. | HI,  MoH | MoES,  MoW,  MoE | 1. 30.12.2024  2. 30.12.2025 |
| 4.5.2. | Revision of the profession standard for beauty specialists (in cosmetology) and the standard for cosmetologists in accordance with the European Standard for Aesthetic Medicine, eliminating fundamental inconsistencies. | The inconsistencies between the profession standard for beauty specialists (in cosmetology) and the profession standard for cosmetologists have been resolved. | 1. The profession standard for beauty specialists (in cosmetology) has been clarified.  2. The profession standard for cosmetologists has been clarified. | MoH | LKKA, LSSA, LDDK, UPOMPL,  MoW,  MoES (NCE) | 1. 30.12.2024  2. 30.12.2024 |
| 4.5.3. | Restriction of the use of the word ‘clinic’ and other words that may convey the impression of the provision of medical services in the names of companies providing unrelated services. | Restricted use of the word ‘clinic’ and other words that may convey the impression of the provision of medical services in the names of companies. | The right of consumers to receive objective information about the service provider has been ensured, thereby reducing the risks of misleading choice associated with misleading names of service provision places. | MoJ | MoH | 30.12.2024 |
| Course of Action 4. Task 6. **Strengthening of data exchange and analytics in the beauty care sector.** | | | | Fiscal benefit: EUR 1 million | | |
| 4.6.1. | Registration of cosmetologists and beauty specialists (in cosmetology)  in the SRS database and linking to the Single Register of Health Professionals. | Cosmetologists and beauty specialists (in cosmetology) employed in the beauty care sector are included in the SRS database which will be linked to the new Single Register of Health Professionals.  1. The possibility making amendments to the following laws and regulations has been assessed:  1.1. Cabinet Regulation No. 693 of 8 December 2015, Procedures by which the Beauty Treatment and Tattooing Service Providers shall Inform about the Commencement of the Economic Activity;  1.2. Cabinet Regulation No. 317 of 24 May 2016, Procedures for Establishing, Updating and Maintaining the Register of Medical Practitioners and Medical Treatment Support Personnel.  2. Changes have been made to the SRS information system and data has been exchanged with the Single Register of Health Professionals on cosmetologists and beauty specialists (in cosmetology) employed in the beauty care sector. | The number of unregistered economic operators is decreasing. | 1. HI, MoH  2. HI, SRS | 1. MoE | 1. 30.12.2025  2. 30.12.2027 |
| Course of Action 5 – **Other measures to improve business competitiveness.** | | | | **Fiscal impact: EUR 41 million** | | |
| Course of Action 5. Task 1. **Reduction of the number of companies with long-term negative equity.** | | | | Fiscal benefit: EUR 8 million | | |
| 5.1.1. | Contribution to the reduction of the number of companies with long-term negative equity. | Based on international experience, a framework has been developed to encourage the reduction of the number of companies with long-term negative equity (e.g. the experience of Lithuania[[35]](#footnote-36) or Estonia[[36]](#footnote-37) could be used, mandatory convening of a board meeting, carrying out an assessment of the situation). | Reduced number of companies with long-term negative equity. | MoJ | MoF,  SRS | 30.12.2025 |
| 5.1.2. | Improvement of simplified winding-up proceedings. | The possibility of and, where necessary, amendments to the regulatory framework to improve and speed up the process of simplified winding-up proceedings have been assessed. | Reduced number of companies with long-term negative equity. | MoJ | MoF | 30.12.2025 |
| 5.1.3. | In-depth risk assessment of the situation of affiliated companies (creditors) providing long-term investments to companies with negative equity and the causes thereof. | When assessing specific cases, the risk analysis is important in answering the question why creditors are interested in providing long-term investments to companies with negative equity. | An evaluation has been prepared. | MoF,  SRS | MoE | 30.12.2025 |
| 5.1.4. | Educating of companies about the consequences and causes of negative equity. | Small and medium-sized companies often lack the financial literacy to operate without negative equity. It is important to educate companies about both the consequences (more difficult attraction of capital) and the causes of negative equity. | Reduced number of companies with long-term negative equity. | MoE responsible for the business sector  (practical action: LCCI)  SRS | LIAA | 30.12.2027 |
| Course of Action 5. Task 2. **Reduction of the circulation of illegal excisable goods.** | | | | Fiscal benefit: EUR 33 million | | |
| 5.2.1. | Reduction of the illegal market for excisable goods. | 1. Measures are taken to reduce the market share of illegal excisable goods (cigarettes, fuel, alcohol, etc.).  2. In order to prevent distortions of competition, it is necessary to address the issue of increased controls on vehicles registered in Central Asian countries and Russia. Where necessary, appropriate amendments to laws and regulations have been made to restrict the import of fuel into Latvia, including through cooperation with the Baltic States. | Increased excise duty revenue and reduced damage to the State.  between three to five per cent as a result of measures to restrict the illegal market.  Tax revenues could increase  The restrictions and control measures introduced to restrict the illegal excise market, including cigarette smuggling, have reduced the scope of damage caused to the State and the excise duty gap for cigarettes.  Consumption of fuels of undetermined origin has decreased. | 1. SRS  2. MoF,  VSIA “Road Transport Directorate”,  SRS | 1., 2.  SP,  SBG,  MoT | 1. 30.12.2026  2. 30.12.2025 |

5. Resultative Indicators of the Plan

Measurable resultative indicators have been developed to assess the effectiveness of the measures implemented in accordance with the plan in priority sectors and to analyse the dynamics of business tax compliance.

**Construction of buildings (NACE code 41)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Sector** | **2023** | **2024** | **2025** | **2026** | **2027** | **Notes** |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘A’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 7.3% | 7.8% | 8.3% | -\* | -\* | The expected increase of not more than 0.5 per cent each year, with a maximum growth rate of 10 per cent. |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘B’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 49.2% | 48.7% | 48.2% | -\*\* | -\*\* | The expected reduction of not more than 0.5 per cent each year, with the rate of reduction not exceeding 10 per cent. |
| Share of employees with income exceeding EUR 1000 in the total number of employees in the sector (monthly average), % | 42.1% | 44.0% | 45.7% | 47.3% | 48.8% | Forecast with autoregression, pessimistic scenario. |
| Share of workplaces with income exceeding EUR 1000 in the total number of workplaces in the sector (monthly average), % | 38.8% | 40.6% | 42.2% | 43.7% | 45.0% | Forecast with autoregression, pessimistic scenario. |

**Civil engineering (NACE code 42)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Sector** | **2023** | **2024** | **2025** | **2026** | **2027** | **Notes** |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘A’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 14.3% | 14.8% | 15.3% | -\* | -\* | The expected increase of not more than 0.5 per cent each year, with a maximum growth rate of 10 per cent. |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘B’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 53.0% | 52.5% | 52.0% | -\*\* | -\*\* | The expected reduction of not more than 0.5 per cent each year, with the rate of reduction not exceeding 10 per cent. |
| Share of employees with income exceeding EUR 1000 in the total number of employees in the sector (monthly average), % | 63.1% | 64.3% | 65.4% | 66.4% | 67.3% | Forecast with autoregression, pessimistic scenario. |
| Share of workplaces with income exceeding EUR 1000 in the total number of workplaces in the sector (monthly average), % | 61.1% | 62.3% | 63.3% | 64.3% | 65.1% | Forecast with autoregression, pessimistic scenario. |

**Specialised construction activities (NACE code 43)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Sector** | **2023** | **2024** | **2025** | **2026** | **2027** | **Notes** |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘A’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 7.9% | 8.4% | 8.9% | -\* | -\* | The expected increase of not more than 0.5 per cent each year, with a maximum growth rate of 10 per cent. |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘B’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 51.1% | 50.6% | 50.1% | -\*\* | -\*\* | The expected reduction of not more than 0.5 per cent each year, with the rate of reduction not exceeding 10 per cent. |
| Share of employees with income exceeding EUR 1000 in the total number of employees in the sector (monthly average), % | 34.5% | 36.2% | 37.7% | 39.0% | 40.3% | Forecast with autoregression, pessimistic scenario. |
| Share of workplaces with income exceeding EUR 1000 in the total number of workplaces in the sector (monthly average), % | 32.3% | 33.9% | 35.3% | 36.6% | 37.8% | Forecast with autoregression, pessimistic scenario. |

**Wholesale trade, except of motor vehicles and motorcycles (NACE code 46)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Sector** | **2023** | **2024** | **2025** | **2026** | **2027** | **Notes** |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘A’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 14.2% | 14.7% | 15.2% | -\* | -\* | The expected increase of not more than 0.5 per cent each year, with a maximum growth rate of 10 per cent. |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘B’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 49.9% | 49.4% | 48.9% | -\*\* | -\*\* | The expected reduction of not more than 0.5 per cent each year, with the rate of reduction not exceeding 10 per cent. |
| Share of employees with income exceeding EUR 1000 in the total number of employees in the sector (monthly average), % | 53.0% | 54.0% | 56.0% | 57.8% | 59.3% | Forecast with autoregression, pessimistic scenario. |
| Share of workplaces with income exceeding EUR 1000 in the total number of workplaces in the sector (monthly average), % | 51.0% | 52.0% | 53.8% | 55.4% | 56.8% | Forecast with autoregression, pessimistic scenario. |

**Retail trade, except of motor vehicles and motorcycles (NACE code 47)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Sector** | **2023** | **2024** | **2025** | **2026** | **2027** | **Notes** |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘A’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 9.6% | 10.1% | 10.6% | -\* | -\* | The expected increase of not more than 0.5 per cent each year, with a maximum growth rate of 10 per cent. |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘B’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 49.6% | 49.1% | 48.6% | -\*\* | -\*\* | The expected reduction of not more than 0.5 per cent each year, with the rate of reduction not exceeding 10 per cent. |
| Share of employees with income exceeding EUR 1000 in the total number of employees in the sector (monthly average), % | 28.9% | 29.5% | 31.1% | 32.8% | 34.3% | Forecast with autoregression, pessimistic scenario. |
| Share of workplaces with income exceeding EUR 1000 in the total number of workplaces in the sector (monthly average), % | 27.8% | 28.5% | 30.1% | 31.7% | 33.2% | Forecast with autoregression, pessimistic scenario. |

**Human health activities (NACE code 86)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Sector** | **2023** | **2024** | **2025** | **2026** | **2027** | **Notes** |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘A’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 30.9% | 31.4% | 31.9% | -\* | -\* | The expected increase of not more than 0.5 per cent each year, with a maximum growth rate of 10 per cent. |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘B’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 51.6% | 51.1% | 50.6% | -\*\* | -\*\* | The expected reduction of not more than 0.5 per cent each year, with the rate of reduction not exceeding 10 per cent. |
| Share of employees with income exceeding EUR 1000 in the total number of employees in the sector (monthly average), % | 64.0% | 68.0% | 70.0% | 73.0% | 75.2% | Forecast with autoregression, pessimistic scenario. |
| Share of workplaces with income exceeding EUR 1000 in the total number of workplaces in the sector (monthly average), % | 55.0% | 58.0% | 60.0% | 63.0% | 65.3% | Forecast with autoregression, pessimistic scenario. |

**Hairdressing and other beauty treatment (NACE code 96.02)**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Sector** | **2023** | **2024** | **2025** | **2026** | **2027** | **Notes** |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘A’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 4.9% | 5.3% | 5.7% | -\* | -\* | The expected increase of not more than 0.5 per cent each year, with a maximum growth rate of 10 per cent. |
| Share of taxpayers that are legal entities without significant tax compliance risks (‘B’ class rating) in the total number of segmented taxpayers that are legal entities at the beginning of the year, % | 49.9% | 49.5% | 49.1% | -\*\* | -\*\* | The expected reduction of not more than 0.5 per cent each year, with the rate of reduction not exceeding 10 per cent. |
| Share of employees with income exceeding EUR 1000 in the total number of employees in the sector (monthly average), % | 6.4% | 7.0% | 7.6% | 8.1% | 8.4% | Forecast with autoregression, pessimistic scenario. |
| Share of workplaces with income exceeding EUR 1000 in the total number of workplaces in the sector (monthly average), % | 5.6% | 6.1% | 6.6% | 7.0% | 7.3% | Forecast with autoregression, pessimistic scenario. |

The sectoral wage indicators are projected on the basis of autoregressive models. The projected values essentially represent a pessimistic scenario for sectoral wage developments.

The indicators for the distribution of taxpayers in the sector by tax compliance will be revised as necessary.

\* The value of the indicator cannot be predicted, but an upward trend is expected.

\*\* The value of the indicator cannot be predicted, but a downward trend is expected.

Summary of State and municipality budget funding required to implement the measures included in the plan

EUR

|  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Task** | **Measure** | **Budget programme (sub-**  **programme) code and name** | **Funding planned in the Medium-term Budget Framework Law** | | | **Additional funding required** | | | | | **Year of implementation of the measure (if the implementation of the measure is time-limited)2** |
| **2024** | **2025** | **2026** | **2024** | **2025** | **2026** | **in the following period until the completion of the measure (if the implementation of the measure is time-limited)** | **annually thereafter (if the implementation of the measure is not time-limited)** |
| Total funding for the implementation of the plan, including: | Amendments have been made to the regulatory framework in respect of the introduction of general annual personal income declaration, envisaging that the population must declare all income earned during the tax year, including income that they do not currently declare, including: | 33.00.00 “Provision of State Revenue and Customs Policy” | 413 995 | 331 400 | 31 400 |  |  |  |  | 31 400 |  |
|  | * introduction of the necessary changes to the SRS information systems |  | 313 995 | 31 400 | 31 400 |  |  |  |  | 31 400 |  |
|  | * organisation of a communication campaign on general declaration |  | 100 000 | 300 000 | - |  |  |  |  | - |  |
|  | Implementation of the electronic circulation system for supporting documents (e-invoices) | 74.06.00 “Projects and Measures under the Recovery and Resilience Mechanism Plan” | - | - | - | 633 923 | 1 398 877 | - |  | - | 2025 |
|  |  | 33.00.00 “Provision of State Revenue and Customs Policy” | - | - | - |  |  | 933 754 |  | 349 368 |  |

The responsible and participating ministries will ensure the implementation of the measures included in the plan within the existing funding by requesting from the programme 80.00.00 “Undivided Financing for the Implementation of Projects and Measures Co-financed from European Union Policy Instruments and Other Foreign Financial Assistance” of the budget unit “74. Funding to be Reallocated in the Process of Implementation of the Annual State Budget” or, where necessary, through fiscally neutral proposals during the preparation of the current annual budget.

Summary of estimated tax revenue from the measures included in the plan

*mln. EUR*

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Course of action of the plan** | **Total** | **Projected revenue** | | | |
| **2024** | **2025** | **2026** | **2027** |
| **Course of Action 1 Horizontal measures and reduction of cash in circulation.** | **55.00** | **6.00** | **22.00** | **46.00** | **55.00** |
| * 1. Strengthening of public-private partnerships: use of ratings in public procurements and public procedures. | 15.00 | - | 4.31 | 10.00 | 15.00 |
| * 1. Restrictions on the circulation of cash. | 18.00 | 4.00 | 9.00 | 18.00 | 18.00 |
| * 1. Conceptual solution for the general principle of declaring personal income is identified. | 7.00 | - | 0.69 | 7.00 | 7.00 |
| * 1. Promoting the use of non-cash transactions. | 15.00 | 2.00 | 8.00 | 11.00 | 15.00 |
| **Course of Action 2 Information and data exchange.** | **1.00** | **0.00** | **0.30** | **0.75** | **1.00** |
| 2.1. Introduction of e-receipts. | 0.30 | - | - | 0.25 | 0.30 |
| 2.2. Interinstitutional information exchange and disclosure. | 0.70 | - | 0.30 | 0.50 | 0.70 |
| **Course of Action 3 Measures in the construction sector.** | **16.00** | **5.00** | **11.00** | **13.50** | **16.00** |
| * 1. Strengthening of the EDLUS, VEDLUDB, CIS data analytics. | 7.00 | 2.00 | 5.00 | 6.00 | 7.00 |
| * 1. Requirements for private individuals in the construction process. | 2.00 | - | 1.00 | 1.50 | 2.00 |
| * 1. Strengthening of the public-private partnership in the construction sector. | 7.00 | 3.00 | 5.00 | 6.00 | 7.00 |
| **Course of Action 4 Measures in the health sector.** | **7.00** | **0.50** | **2.30** | **4.75** | **7.00** |
| 4.1. Strengthening of data analytics in the health sector. | 2.00 | 0.50 | 1.00 | 1.50 | 2.00 |
| 4.2. Definition of a clear legal framework in the health sector. | 0.25 | - | 0.15 | 0.20 | 0.25 |
| 4.3. Strengthening of the public-private partnership in the health sector. | 3.00 | - | 1.00 | 2.00 | 3.00 |
| 4.4. Provision of information and public education measures in the health sector. | 0.50 | - | - | 0.35 | 0.50 |
| 4.5. Definition of a clear legal framework in the beauty care sector. | 0.25 | - | 0.15 | 0.20 | 0.25 |
| 4.6. Strengthening of data exchange and analytics in the beauty care sector. | 1.00 | - | - | 0.50 | 1.00 |
| **Course of Action 5 Other measures to improve business competitiveness.** | **41.00** | **0.50** | **4.40** | **15.00** | **41.00** |
| * 1. Reduction of the number of companies with long-term negative equity. | 8.00 | - | - | 5.00 | 8.00 |
| * 1. Reduction of the circulation of illegal excisable goods. | 33.00 | 0.50 | 4.40 | 10.00 | 33.00 |
| **Total** | **120.00** | **12.00** | **40.00** | **80.00** | **120.00** |

Total projected tax revenues from the implementation of the measures in 2027 amount to EUR 120 million, including: PIT revenue in the amount of EUR 17.20 million, followed by MSSIC revenue in the amount of EUR 33.40 million, VAT revenue in the amount of EUR 36.41 million and excise duty revenue in the amount of EUR 33.3 million.

**Assessment of the Administrative Burden**

Administrative burden is the obligation imposed on a natural or legal person to comply with the legal framework by receiving, processing, providing (transmitting) or storing information (e.g. collecting and recording of data, reporting, updating of data upon request of an authority) that the person would not have done unless required by the legal framework. In view of the above, it is not possible to accurately determine or forecast the potential administrative costs at the stage of drafting the plan. Much depends on the aspects that will be revealed when drafting the laws and regulations during the implementation of the measures of the plan, including the range of persons affected. Thus, the administrative burden for the measures included in the plan is descriptive, using a logical-constructive approach.

**1.2.2. Imposing the obligation on employers to inform the SRS of the fact that an employee’s wage is paid in cash.**

**Time** – given that employees and employers do not often change the method of the payment of wages, changes on the employers’ declaration will only be required if the method of the payment of wages in the previous month was different from the method of the payment of wages in the current month. In the first month when this obligation enters into force, a non-cash payment of the wage will be recorded automatically that will be required to be changed accordingly in the case of the payment of the wage in cash. The time taken depends on the proportion of employees in the company who choose the payment of the wage in cash. The relevant data are currently unknown.

**Frequency** – the tax return will be submitted on a monthly basis.

**Number of persons involved** – the number of persons involved corresponds to the number of legal entities with workplaces. At the same time, changes to the report of employer will only be required if the method of the payment of wages in the previous month was different from the method of the payment of wages in the current month. It is assumed that the administrative burden is likely to be minimal as it concerns a small number of employees and the information is intended to be received through the report of employer, making an additional note in the appropriate field on the employee in the report that the wages have been paid in cash. The target audience of the measure could be employers employing up to five employees. According to the submitted reports of employers, 76.9 per cent or 63 463 employers have up to five employees in August 2023 (77.5 per cent in 2022, an increase of 1.2 percentage points compared to 2021). Significant risks of ‘envelope wages’ have been identified to 55.0 per cent of the abovementioned employers. Provision of information to the SRS on the payment of wages in cash will not impose a high administrative burden on employers of small companies, although they represent the majority of employers.

**Costs** – at this stage, it is not possible to estimate the administrative costs for legal entities as the frequency of reporting and the number of persons involved may vary.

The measure does not create an administrative burden as the non-cash wage payment will be automatically recorded in the reports of employers that will be required to be changed accordingly if the payment of wages will be made in cash and if such information differs from the information provided previously (the previous option will be maintained, subsequently reducing the administrative burden).

**1.2.3. Introduction of threshold declarations for cash deposits and withdrawals (reporting of cash deposits and withdrawals in ATMs).**

**Time** – reporting on cash deposits will be ensured automatically.

**Frequency** – the tax return will be submitted on a quarterly basis.

**Number of persons involved** – legal entities operating a network of ATMs in the territory of Latvia.

**Costs –** at this stage, it is not possible to estimate precisely the administrative costs for legal entities as they depend on the current reporting algorithm. A transitional period will be provided for the implementation of the regulation to allow commercial banks to make the necessary changes to their reporting algorithms as part of the planned improvements.

**1.3.1. Assessment of whether the existing personal income declaration procedures needs to be supplemented in order to reduce the shadow economy, promote a tax-paying culture, and at the same time not increase the administrative and bureaucratic burdens. This includes identification of a conceptual solution for the phasing-in of the general principle of declaring personal income, identifying the necessary exceptions.**

**Time** – the measure does not currently represent a burden. In the future, when developing the general personal income declaration concept, it is envisaged that the tax return will be generated automatically. Thus, a person will only be required to provide additional data if the tax return does not reflect all the information at his or her disposal. The latter will not create a new tax liability for the person. At the same time, the information available to the State about a person’s income will be used to help prevent situations where the tax obligation is not complied with for whatever reason. Deliberate or unintentional non-compliance with tax obligations leads to late payment penalties (possibly, fines). Consequently the person will require less time to get an idea of the information available to the State on income earned and taxes paid, thus minimising the risks of non-payment of taxes and the corresponding negative consequences.

**Frequency** – currently the measure does not impose a burden. In the future, when developing the general personal income declaration concept, it is envisaged that the tax return will be submitted once a year.

**Number of persons concerned** – currently the measure does not impose a burden. In the future, when developing the general personal income declaration concept, it is envisaged that the tax return will be submitted by the population over 18 years of age, taking into account the relevant statutory exceptions (population of 1.5 million in 2022 from 18 years of age) The administrative burden will only be borne by those persons who need to enter additional data, the number of which cannot be determined at the moment.

**Costs** – there will be a negative effect, but given that the obligation to update data depends on the actions and activities of each person, it is not possible to provide specific estimates at this stage. The positive effect is that the person will be provided with a statement that will allow him or her to fulfil the statutory obligation to declare his or her income on time and pay taxes (i.e. compliance with the requirements already laid down in the legislation). The positive effect is to reduce the risk of deliberate or unintentional failure by a person to comply with the tax obligations, leading to the accrual of late payment penalties (possibly, fines).

A solution will be sought within the scope of the implementation of the measure to ensure convenient and automated personal income declaration, including organisation of discussions and identification of the SRS data for qualitative analytics. The basic principles of equality, certainty, convenience, efficiency will be complied with. At present, the measure does not impose any additional administrative burden.

**1.3.2. In conjunction with measure 1.3.1, assessment of the need to require the manager of portfolio investments and similar financial instruments to withhold tax at source and report the amount of taxable income to the SRS.**

**Time** – the measure does not currently represent a burden. In the future, when developing the general personal income declaration concept, it is envisaged that data will be provided by financial instrument managers and financial institutions. The time required to prepare the information is not determinable.

**Frequency** – information will be provided on a regular basis.

**Number of persons involved** – according to the information included in the statements on amounts paid to natural persons (with income type code 1019 ‘Interest’ and payer NACE Rev. 2 code 64 ‘Financial service activities, except insurance and pension funding’), 181 337 natural persons received interest income disbursed by 106 financial service providers in the first nine months of 2023.

**Costs** – at this stage, it is not possible to estimate precisely the administrative costs as the amount of withholdings from the management of investment portfolios and similar financial instruments is unknown.

* + 1. **Implementation of the electronic circulation system for supporting documents (e-invoices).**

**Time** – the introduction of e-invoices will reduce manual work, reduce the risk of invoice errors and ensure that invoices reach the accounting and tax administrations more quickly. Consequently, the implementation of the measure is expected to have a positive effect in terms of reducing the administrative burden (savings in time) that cannot be quantified precisely at present as it depends on the technical details of the solution to be developed.

**Frequency** – depending on the number of concluded transactions that is currently undefinable.

**Number of persons involved** – all companies and economic operators concluding transactions (B2B, B2G).

**Costs** – possible costs will be specified during the introduction of e-invoices. Costs are expected to decrease due to abandonment of the use of paper format invoices and transition to digital invoices and also the reduction of the risk of invoice errors and faster arrival of invoices in accounting and tax administration, alongside reduction in labour costs.

The concept of e-invoices is currently at an early stage of preparation and the interinstitutional working group is deciding on detailed solutions, so the administrative burden is not quantifiable at this stage.

**1.4.2. Obligation for businesses with an annual turnover exceeding EUR 50 000 to allow customers to pay also using non-cash payments.**

**Time** – the introduction of non-cash payments will ensure savings on drawing up of payment documents.

**Frequency** – regularly, when a transaction takes place.

**Number of persons involved** – entrepreneurs with a turnover of more than EUR 50 000 per year without any non-cash payment solution. According to the SRS, 779 taxpayers could be affected by this regulation, whereof 177 taxpayers are active in the trade sector (NACE 46 and NACE 47).

**Costs** – will increase for businesses when introducing the non-cash payment solution and settling payments for business transactions. Based on a calculation of commercial costs, non-cash payment solution pays off at an annual turnover above EUR 35 000. At the same time, the administrative burden will be reduced for customers who do not have cash at the time of purchase and are currently forced to withdraw cash from an ATM to make the transaction. It is not possible to make specific calculations of the administrative burden because information on active traders and the number of transactions is constantly changing, making it difficult to calculate the administrative burden accurately.

There are a wide variety of technological POS solutions for non-cash payments, e.g. stationary, mobile, embedded, portable, phone terminals, mini terminals, etc. The total terminal fee is comprised of two items: the terminal subscription fee and a per-transaction fee. The subscription fee per terminal ranges from EUR 14 to EUR 25 per month, depending on the type of equipment. Fixed terminals are the cheapest, while mobile terminals cost from EUR 18 to EUR 25 per month. Additional costs may be incurred if there is no internet connection at the point of sale.[[37]](#footnote-38) Given that there is a wide variety of technological solutions for POS terminals and that their costs are influenced not only by the type of terminal but also by the number of transactions and the type of payment card, the administrative burden cannot be accurately determined.

**3.1.1. Lowering of the threshold for the EDLUS implementation (from EUR 350 000 to EUR 170 000).**

**Time** – the implementation of the system is a one-off event and requires special IT equipment for day-to-day functionality. The time will be fixed automatically, whereas administrative supervision is ensured by a company employee. It is not possible to calculate the exact time, as the actual time depends on the size of the site and the number of employees on site.

**Frequency** – the system will be used on site during construction work.

**Number of persons involved** – all merchants with a construction site value from EUR 170 000 to EUR 350 000. According to the IUB data, 88 construction work procurements with a value of EUR 170 to EUR 350 thousand were announced by 24 October 2023. Assuming that public procurements account for about half of the construction works contracts, we can estimate that measure 3.1.1 of the plan will cover approximately 200 construction projects. The exact number of the affected entities cannot be determined at this stage.

**Costs** – estimated costs of setting up the IT system, provision of the necessary technical solutions on the construction site could vary from EUR 200 to EUR 300 per month per construction site.

There are several solutions on the Latvian market that offer the installation and functionality of the EDLUS on construction sites. The EDLUS is the most effective tool for monitoring the presence of workers on construction site and therefore it helps to identify the number of hours worked on site.

**3.1.2. Inclusion of the obligation in laws and regulations for the initiator of a construction plan to submit to the CIS information on the price of the construction contract, the planned price of the construction works in the case of the constructor, and also to provide for the possibility to make a selection of the costs of implementation of construction plans (price of construction works) by type of use of the structures.**

**Time** – no additional time required (up to a few minutes for completing an additional column). The measure is planned as a technical solution in the CIS functionality. This proposal concerns a preliminary assessment of construction costs and does not provide for the submission of additional documents.

**Frequency** – information on the price of the planned construction worksduring the construction process shall be submitted once in the CIS.

**Number of persons** **involved** – legal and natural persons starting the construction process.

**Costs –** the measure will not cause any additional costs for legal and natural persons and will not increase the administrative burden.

The SCCB will make the necessary improvements to the CIS functionality to enable the selection of the costs (price of construction works) for construction projects by type of use. This measure will improve the analytics of the CIS data and will be implemented through improvements to the CIS functionality. The possibility to select the CIS data by type of use of structures will allow a better analysis of the situation in the sector and to keep track of changes in construction costs.

**3.2.2. Obligation for a private individual to provide information to the CIS on the origin of the funds intended to be used for the works.**

**Time** – no additional time required (up to a few minutes for completing an additional column). The measure is planned as a technical solution in the CIS functionality where a private individual, when starting the construction, will indicate the source of the planned funding, e.g. a loan, savings, ticking a box in the CIS structured data that would confirm the veracity of that statement and the submission of additional documents is not required.

**Frequency** – information on the origin of the funding planned for the construction works is provided once during the construction process.

**Number of persons involved** – natural persons starting the construction process.

**Costs** – the measure will not cause any additional costs for natural persons and will not increase the administrative burden.

**Financial institutions have the obligation to report the balance of the current debt and borrowed funds (regardless of their legal form) exceeding 20 minimum wages.**

Also, as part of the measures to restrict the shadow economy, the Amendments to the Law on the Credit Register entered into force on 16 November 2023, thus clarifying and supplementing the right of the SRS under Section 19 of the Law on the Credit Register to receive information from the Credit Register on liabilities of natural persons (residents) that meet a certain limit of the balance of liabilities.

The Law is designed to **reduce the administrative burden** for taxpayers and aims to provide the SRS with the information necessary but currently lacking for data analysis, tax administration activities and tax administration inspections, and also for inspections of tax returns submitted by public officials.

Law:

- clarifies the existing regulatory framework by stipulating that the SRS has the right to receive information from the Credit Register on the basis of a separate request for the purpose of assessing and carrying out an examination of the usefulness of tax administration activities and tax administration if during the tax administration process there are grounds to believe that the expenses of a natural person (resident) could exceed his or her income;

- the right of the SRS to receive information from the Credit Register without a separate request is supplemented by stipulating that the Credit Register will inform the SRS once a year of the liabilities of natural persons (residents) with a total balance of at least 20 minimum monthly wages;

- supplements the right of the SRS to obtain information from the Credit Register for the purpose of verifying the tax returns submitted by public officials.

The amount of information to be included in the Credit Register will be analogous to the amount that the SRS is already entitled to receive from the Credit Register on the basis of an individual request for the purpose of analysing the necessity of a tax audit if, prior to the commencement of the tax audit, the SRS has grounds to believe that the expenses of a natural person (resident) could exceed his or her income.

According to Section 22.3 of the law On Taxes and Fees, credit institutions and payment service providers submit information to the SRS only on the turnover of accounts, while the Credit Register is supposed to provide information on the amount of liabilities, thus the new legal provision will provide additional information for the assessment of the received data.

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| |  |  |  | | --- | --- | --- | | Minister for Finance | (signature\*\*) | A. Ašeradens |   \*\* The document is signed using the electronic signature tool of the DLA portal. |

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