

# Latvia's three tier pension system and taxation of pensions (2/22/18)

This article provides a summary of information on Latvia's three-tier pension system and the taxation of pensions.

A three-tier pension system has operated in Latvia since 2001.

## Tier 1: the national mandatory non-funded pension scheme

This tier covers all social insurance contributors (including employers, employees, self-employed persons, EU citizens employed by a foreign employer in Latvia, foreign nationals employed by a foreign employer in Latvia, and persons that have voluntarily joined the social insurance system), with their contributions being used to pay old-age pensions to the existing generation of pensioners.

Under government rules<sup>1</sup> the rate of Tier 1 pension insurance is 20% of the income subject to contributions as specified by the National Social Insurance Act and the Solidarity Tax Act, unless the socially insured person is a member of Tier 2, when the rate is 14%.

In this tier the contributor accrues their pension capital, which will be used for calculating state old-age pension once they reach the statutory pensionable age (63 years and three months on 29 May 2018).

Old-age pensions over €250 a month attract personal income tax (PIT).

## Tier 2: the state-funded pension scheme

Social insurance contributions paid by members of this tier are invested on the financial market through their chosen asset manager and accrued towards the contributor's pension.

Tier 2 contributions are not payable separately, as they are sourced from mandatory insurance contributions actually paid in Tier 1.

Since 2016 the rate of Tier 2 contributions has been 6% of the relevant income (6% = 20% - 14%).

Under current law a person cannot begin to use their Tier 2 capital until they reach pensionable age. And the government does not intend to pay out the pensioner's accrued Tier 2 capital all at once.

Using Tier 2 means –

- adding the accrued Tier 2 capital to the pension capital accrued in Tier 1, or
- buying a life insurance policy (life annuity) from an insurance company.

According to the [National Social Insurance Agency's website](#) there are four insurance companies in Latvia that offer a life annuity (with a minimum of €3,000 accrued in Tier 2): SEB Life Insurance AAS, ERGO Life Insurance SE Latvian branch, Compensa Life Vienna Insurance Group SE Latvian branch, and CBL Life AAS.

For example, a person who reached pensionable age in May 2018 and chose to use their accrued Tier 2 capital (€3,000) for a life policy would be receiving a life annuity of €13.68 a month on top of their Tier 1 pension.

A life annuity is awarded for the person's lifetime and paid over the period of the life annuity contract. The life policy can designate a beneficiary to receive the life annuity over the guaranteed period if the annuitant dies during the insurance period.

In general, income from life annuity contracts (with accrued funded pension capital) are exempt from PIT under section 9(4)(b) of the PIT Act.

On 22 May 2018 the Parliamentary Budget and Finance (Taxation) Commission supported an initiative that provides for the option of inheriting any capital accrued within the state-funded pension scheme on the death of a scheme member. This initiative has been supported by the Ministry of Finance, the Ministry of Justice, the Latvian Association of Commercial Banks, the Bank of Latvia, and the Latvian Confederation of Employers. Legislative amendments are not, however, expected too soon because there are so many things to do.

### Tier 3: the private voluntary pension scheme

Each person is free to make additional savings towards their retirement in private pension funds.

Any PIT overpaid on contributions to private pension funds is recoverable, subject to meeting statutory criteria, while income from investing those contributions attracts PIT.

### Details of your pension capital and old-age pension

You can find this information on the website [www.latvija.lv](http://www.latvija.lv) after obtaining authorisation through your bank, entering "pension capital" in the search box and selecting the section –

1. "Information on the insured person's pension capital" and
2. "Information on the expected amount of old-age pension."

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<sup>1</sup> The Cabinet of Ministers' Regulation No. 785 on allocating the rate of national social insurance contributions to types of national social insurance, paragraphs 21.1 and 21.2