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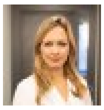
PwC’s Startup Business Survey 2022 1/42/22



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General overview

Several EU member states are taking the taxation of employee share ownership plans in startup companies a step further. Their national rules make share plans far more attractive to startup employees and provide a more founder-friendly environment. While the rules aim to ensure startups give their employees a stake in the company, there are many solutions countries can use to achieve this goal.

PwC firms have conducted a study that provides an overview of the different tax regimes for granting share options to startup employees in EU member states and some other countries where these types of plans are typically significant (the UK, Switzerland and Norway). A total of 30 countries, including Latvia, took part in the study.

The study highlights the existence of specific rules for startups and compares the personal tax treatment of share-related benefits, taking into account the different classifications of such income, the timing of its taxation, the applicable tax rates, and the existence of an exit tax. It also addresses the social insurance liability for such benefits where this is the case. The study shows that the tax and social insurance treatment of such benefits varies significantly from country to country.

Topics covered

The participating countries were asked to answer a list of questions.

Only 11 out of the 30 participants have rules in place prescribing a special regime for the taxation of benefits from employee share ownership plans in startups, while 17 countries (including Latvia) have a beneficial regime for share option plans that are not restricted to startups.

Most of the countries treat income from share plans as employment income, triggering income tax and social insurance contributions. The tax point occurs when a capital gain arises on the subsequent sale of shares.

The national law in 22 out of the 30 countries does not contain an exit tax provision or a time limit on taxation. This means individuals can hold shares in those countries indefinitely.

The study also compares the maximum rate of tax on labour income and capital gains, with Estonia and Sweden each having the highest potentially applicable tax.

Latvian rules

Income arising on the grant of employee share options is exempt if the following conditions are met:

- The holding period is at least 12 months from grant to vesting.
- The person is employed by the company or a related party during this period.
- The employer has notified the tax authority of the plan's terms within two months of the grant.

A Latvian company distributing a dividend based on the employee's share ownership is required to withhold Latvian corporate income tax (CIT) at an effective rate of 25%. No further income tax or social insurance obligations apply. Dividends a foreign company pays to a Latvian tax resident are exempt from Latvian personal income tax (PIT) if the company resides in an EU/EEA country or a country that has an effective double tax treaty with Latvia, and if foreign PIT or CIT has been paid on those dividends. All other dividends (including those from tax havens) are taxed through the individual's annual PIT return. Capital gains arising on the sale of shares are taxable.

In summary, the Latvian legislation is a truly beneficial one, as it allows shares to be issued with little or no tax burden on the company or the individual. The administrative procedure is simple, and the relevant provisions detailed. So we encourage newly formed companies to set up a share option plan and take advantage of the available tax benefits. The rules even extend to companies that do not fall under the definition of startups. Share option plans are successfully launched in companies that have been operating in Latvia for a long time with large numbers of employees in various positions. Please reach out to PwC Latvia if you need help in setting up a share option plan or any advice on related issues.