

# Claiming self-employed expenses 3/46/22



Director, Tax, and Head of Pan-Baltic  
People and Organisation Practice, PwC  
Latvia

Irena Arbidane

To measure the taxable income of businesses and individuals correctly, we need to assess whether self-employed expenses are associated with the conduct of business. In applying personal income tax (PIT), self-employed persons should follow the rules of the PIT Act and the Corporate Income Tax (CIT) Act, which in certain cases may cause disagreement with the State Revenue Service (SRS). This article explores some of the self-employed expenses the SRS may challenge if they are deducted as business expenses.

## Representation expenses

The tax treatment of self-employed representation expenses (e.g. lunch with an existing or potential client, a token gift for a client, organising events for clients, or maintaining your reputation as a service provider) is governed by the PIT Act and the CIT Act, whether the self-employed uses single- or double-entry bookkeeping.

Sections 11(4) and 11.1(3) of the PIT Act state that business expenses exclude any expenses which the CIT Act treats as non-business expenses. Specifically, the CIT Act states that non-business expenses include any representation expenses that together with staff sustainability event expenses for the financial year exceed 5% of the total gross pay on which national social insurance (NSI) contributions have been paid for the previous financial year. So, if a self-employed person has at least one employee, their representation expenses will be deductible business costs up to 5% of the employee's remuneration charged to NSI. However, for a self-employed with no staff these costs will not be treated as business expenses and are therefore fully non-deductible for PIT purposes.

## Beauty care expenses

Under section 11(3) of the PIT Act, self-employed expenses include expenses that are associated with business and necessary to carry it on. This means that a self-employed person who carries on a business is allowed to include in costs associated with the gaining of business income any expenses that are essentially related to the person's business and necessary to conduct or develop it. Thus, business expenses vary from business to business.

If the sort of business a self-employed person carries on requires them to maintain a specific public image (e.g. a vlogger or an influencer), then we believe business expenses can also include stylist and hairdresser services, clothing purchases necessary for the programme or for filming commercials etc.

It's important here to separate expenses that are needed to do some work from representation expenses (e.g. building a public image, except for expenses incurred in building a personal brand, which are fully deductible for tax purposes) and private expenses. This split might be difficult to prove and might lead to in-depth discussions with the SRS.

## Home office expenses

Many self-employed persons carry on a business from their home, with a room often serving as an office, as well as using various private assets, such as a mobile phone, an internet connection and other facilities that help them do business. In reality, these costs can rarely be attributed to business expenses in full, so we need to understand to what extent we can deduct such costs as business expenses and how this can be measured.

Section 11.5(5) of the PIT Act states that if a taxpayer uses for business purposes any space or assets they also use for their private consumption, the taxpayer may add to business costs only the proportion of expenses incurred in using the space or assets that is related to business if such a proportion can be measured and documented at all. The proportion can be based on, for example, the apartment plan showing the business area. However, if there is no way to accurately measure those costs and resources used, the self-employed is to include in their business expenses 70% of the relevant business costs.

If a self-employed person uses some part of their apartment for business, this should be notified to the SRS and the address should be registered with the SRS as a place of business.

A similar approach can be taken when attributing home internet and mobile phone costs to business expenses. In practice it's difficult to determine the business-related part of costs, so we need to bear in mind that the law allows us to allocate up to 70% of the invoice amount, without accounting for calls made and minutes spent for business purposes.