

Tax treatment of employee stock options in Latvia

Timing of taxation

At vesting unless eligible for tax favoured treatment

Taxable amount

Fair market value of shares on the vesting date

Income tax withholding rate

Progressive 20%, 23% or 31% depending on income threshold

Social tax withholding rate

10.5% for employee

Social tax employer rate

23.59%

Social tax cap

EUR 62,800. Any excess is charged to solidarity tax at the same rate so eventually there is no cap.



Payroll tax reporting requirements

- If a stock option awarded to an employee does not meet the criteria for the tax favoured treatment and is consequently taxable at vesting, the Latvian employer is liable to report the award for personal income tax (PIT) and national social insurance contributions (NSIC) purposes and ensure taxes are paid.
- Under the cost recharge model, payroll tax reporting in most cases switches to the Latvian employer.



Income from awarded shares

- A Latvian company paying a dividend based on the employee's shareholding must withhold a 25% effective Latvian corporate income tax (CIT) and no additional PIT or NSIC obligations apply.
- A dividend paid by a foreign company attracts no Latvian PIT if (1) it is established in the EU/EEA or (2) in a country that has an effective double tax treaty with Latvia, and (3) PIT or CIT has been paid on the dividend in that country. All other dividends (including from microbusiness taxpayers or tax havens) attract a 20% PIT through the individual's annual income tax return.
- Capital gains arising on the sale of shares will attract a 20% tax.



Tax favoured treatment

Rules before 12 January 2021

- The awards are not taxed at vesting if -
 - (1) the employee stock option plan imposes a minimum **3 year** holding period from granting to vesting;
 - (2) the employee has an employment relationship with the company or its related party throughout that period; and
 - (3) the employer has notified the tax authority about the terms of the plan within two months after the grant date.
- Notifying the tax authority within two months after employees become eligible for the plan is a must since the tax authority will deny an exemption unless reporting is done.

Rules from 12 January 2021

- The tax favoured treatment applies if the holding period is at least **12 months**. The continued employment requirement and the plan notification requirement remain unchanged.
- The amended PIT Act permits shares in any company, including a Latvian private limited company (SIA), to be awarded under an employee stock option plan. The old rules restricted this to shares in a Latvian public limited company (AS) or a similar foreign corporation.
- The amended PIT Act also permits leavers to benefit from the tax favoured treatment if vesting takes place no later than six months after the end of employment. They still have to meet the continued employment requirement for a holding period of at least one year. It is currently unclear whether this regime extends to any leavers that were added to the plan under the old rules before 12 January 2021.
- The tax favoured treatment is not available to an employee with a loan from the employer or its related party that is not repaid before vesting.
- Obligation to notify tax authorities within two months has remained unchanged.



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