



FOREIGN INVESTORS' COUNCIL IN LATVIA

# POSITION PAPER on ECONOMIC DEVELOPMENT OF LATVIA FOR ALL

Position Paper No. 1



IFICIL

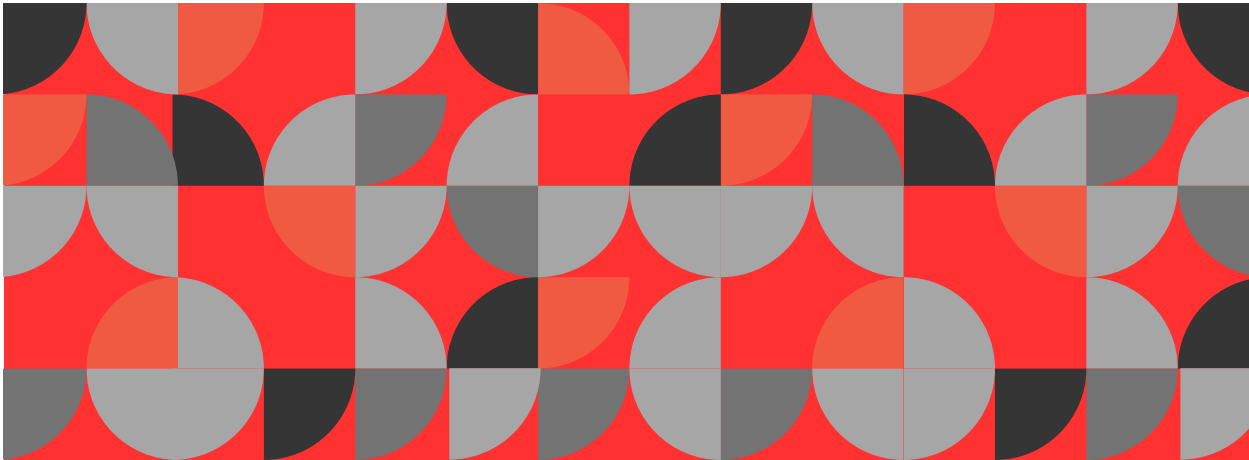
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# TABLE OF CONTENTS

Introduction	3
Human Capital	4
Future Public Administration	5
Investment Protection	6
Sustainable For the Future	7
Combatting Shadow Economy	8



# INTRODUCTION

Latvia is facing serious challenges that are holding us back. We rank low in key areas that drive economic development: our startup ecosystem is less dynamic than in the neighbouring countries,<sup>1</sup> we are underperforming in innovation,<sup>2</sup> our levels of productivity are below the EU average,<sup>3</sup> our universities are not listed in TOP-1000 universities of the world,<sup>4</sup> and it is projected that our population will continue declining in the future.<sup>5</sup> Moreover, in the next five years around 44% of workers' skills will be disrupted globally,<sup>6</sup> while upskilling and reskilling in Latvia remains at low levels and insufficient attention is being paid to the human capital development.<sup>7</sup>

More troubling is a lack of action to tackle above-listed challenges and to reverse negative trends. For years, investors have been calling the government to introduce necessary reforms, formulate ambitious long-term goals and take responsibility to realise them. While Estonia and Lithuania are getting international recognition for improving their business environments and striving for an EU-wide leadership in IT, digitalisation<sup>8</sup> and fintech,<sup>9</sup> Latvia continues to hide its potential, as if the current state of affairs is satisfactory.

In this year's position papers, FICIL recommends focusing on reducing the **administrative burden**, as it would stimulate entrepreneurship, boosting economic growth and innovation. The **modernisation of the public sector** should result in an efficient, result-oriented, transparent and

accountable system that serves needs of the society and of the economy. People are the foundation of any economy, therefore investments in human capital are essential, especially for small and developing countries like Latvia. To ensure a fair market competition, it is crucial to foster **investment protection**, by creating adequate legislation and improving court efficiency, and to **combat the shadow economy**. By embracing the **green transition**, Latvia will be able to position itself not only as a country that cares about its future, but also as the one that utilises new business opportunities.

The key message of FICIL is clear and concise – **the government should act now!** Our challenges will not be solved in a day; therefore, no time should be wasted, and no opportunities should be missed. The path forward must be characterised by well-thought through strategies, collaboration and synergies, continuous learning, dedication, responsibility, bravery and ambition, openness to innovation, result and goal-orientation. With the above, Latvia's potential will convert into Latvia's success, prosperity and safety for current and future generations!

**FICIL has created detailed recommendations regarding the above-mentioned topics, below you will find key recommendations, while complete position papers are available [here](#).**

1 In the Startup Ecosystem Report 2024, Lithuania ranks 16th, while Estonia 12th. Latvia ranks only 47th ([link](#))

2 In the European Innovation Scoreboard 2024, Latvia is almost at the bottom, ranked as "emerging innovator", while Estonia is a "strong innovator" and Lithuania "moderate innovator" ([link](#)). Latvia does not surpass its neighbours in any of the individual categories

3 Eurostat "Labour productivity per person employed and hour worked" up to year 2023 ([link](#))

4 World University Ranking 2024 ([link](#))

5 Eurostat "Population projection in the EU" ([link](#))

6 WEF (2023) "Future of Jobs Report 2023" ([link](#))

7 In year 2023, only 11% of persons aged 25 to 64 were engaged in adult education, in comparison to 23% in Estonia and 13% of EU average. Report "On Medium and Long-Term Labor Market Forecasts Until 2040", page 45 ([link](#))

8 "E-stonia: How the Baltic minnow became a tech powerhouse" ([link](#))

9 "How Lithuania became a fintech hub in Europe" ([link](#))



# HUMAN CAPITAL

The skills of a population, their willingness to engage in continuous education/training, work culture and the availability of a labour force are critical factors in determining the competitiveness of an economy. Undoubtedly, the availability of a skilled labour force is the key consideration for investors and entrepreneurs when deciding where to commence business activities.

FICIL advocates for a dual approach to address labour force challenges, which focuses on both immediate and near-future human capital scarcity, and on implementing more long-term and comprehensive policies that are expected to enhance the skills of the entire labour force. In times of labour force shortages, it is critical that the government ensures the high quality of the healthcare system, but also provides an effective sick leave administration system to prevent abusive practices. In case the latter is not successful, significant costs will be incurred by employers and the government.



*FICIL recommends focusing on three key areas related to human capital policy:*

## REFINE GOVERNANCE

- | Ensure effective implementation of the "Human Capital Development Strategy 2024-2027" and assign the responsibility for driving its implementation to the Human Capital Development Council.
- | Allocate a sufficient budget for the Human Capital Development Strategy.
- | Address the fragmented governance in adult education and the requalification policy.

## FOSTER UPSKILLING AND REQUALIFICATION OF HUMAN CAPITAL

- | Establish a regular review process for the higher education reform that adjusts policies, if necessary, and monitors whether the set goals are being achieved.
- | Align national strategic priorities with that of professional education to ensure the availability of a skilled labour force that matches labour market needs in the mid- to long-term. Collaborate closely with the private sector to identify solutions related to the quality of teaching, teacher availability and compensation.

## ENHANCE THE AVAILABILITY OF LABOUR

- | Improve the availability of labour by amending the Labour Law and make the employment arrangements more flexible.
- | Develop a strategy for attracting foreign labour and adjust relevant regulations to streamline their integration into the labour market.

# FUTURE PUBLIC ADMINISTRATION

To support transformation of the Latvia's public sector, it is essential to embrace a forward-thinking mindset that is characterised by flexibility, agility, innovation, responsibility and responsiveness to any future challenges. It is critical to assess where transformation is needed and break ineffective, inefficient and rigid systems that prevent achievement of set goals.

One way to achieve the above is by involving more voices in the decision-making process. Engaging with businesses, civil society, and everyday citizens on a regular basis can help make public policies more practical and grounded in reality. This is not just about ticking boxes for consultation—it is about working together to create effective solutions. At the same time, there needs to be a fresh approach to managing the public sector workforce. Investing in skills development and promoting leadership that is adaptable to a change will go a long way in creating a more dynamic and effective public service. There needs to be further work to ensure rotation at all levels within the civil service and an effective employee review system.

*FICIL recommends focusing on two key elements to modernise the public sector:*

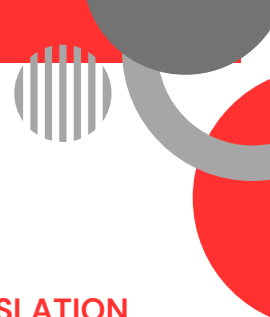
## IMPROVE EFFICIENCY THROUGH DIGITALISATION

- | Establish a high-level CIO with a clear mandate to implement centralised digital transformation of the public sector.
- | Improve data management and standardisation across the public sector and introduce a “one-stop-shop” for all businesses when submitting data to the public sector.
- | Find opportunities for close collaboration with the private sector in the field of artificial intelligence (AI), and build a strong governance model for AI.

## MODERNISE PUBLIC ADMINISTRATION

- | Continue to introduce Performance-Based Budgeting (PBB) by 2028, with the option of conducting pilot projects in several ministries. Moreover, increase the accountability of the public sector representatives for actions and results by introducing measurable KPIs, and defining consequences for failure to achieve them.
- | Improve transparency of the implementation of the State Audit Office's recommendations by requesting entities to submit regular (annual) and more elaborate explanations on concrete implementation steps.
- | Boost productivity of civil servants by introducing rotation mechanisms and setting a higher threshold for granting the status of “civil servant”.
- | Ensure that the documents published by the public sector institutions correspond to the planning document framework, thereby the category of the documents reflects its purpose and content. The State Chancellery should create an interactive tool to enable the monitoring of progress of the policy planning document implementation, thereby promoting transparency and accountability. This tool should provide a comprehensive overview of goals, key performance indicators (KPIs), and progress of achievement of aims, described in various policy documents.





# INVESTMENT PROTECTION

Investment protection is crucial to ensure long-term economic growth and to create a favourable business environment. FICIL has long emphasised the need for a transparent and reliable legal framework that protects both domestic and international investors. However, frequent changes in legislation and concerns about the quality of legislation create uncertainty among entrepreneurs. Data published by the European Commission shows that almost half of company directors in Latvia doubt whether the law and the courts will be able to protect their investments should problems arise.<sup>10</sup>

In order to address this situation and alleviate concerns, there is a need for not only incremental reforms, but also for a strategic approach to reforming the legislative process in order to promote stability, consistency and transparency.

*FICIL recommends focusing on four key categories to improve the overall business environment and assure businesses can trust that their investments are being protected:*



## IMPROVING THE QUALITY OF LEGISLATION

- | Use data more effectively in policy-making, including by informing stakeholders.
- | Strengthen the legislative process by giving stakeholders sufficient time to provide comments.
- | Set a new amount for legal land use fees and develop a specific framework for critical infrastructure.

## REGARDING STATE-OWNED ENTERPRISES

- | Review and extend the scope of Article 88 of the State Administration Structure Law.

## IMPROVING THE CAPACITY AND EFFICIENCY OF THE JUDICIARY

- | Establish an appellate court for the Economic Affairs Court.
- | Continue the digitalisation of the courts.
- | Strengthen the competence of judges, in particular in the matters concerning the private sector and business.
- | State administration should become engaged in the development of an appropriate investment protection model at the EU level.

## IMPROVING THE PUBLIC PROCUREMENT PROCESS

- | Work towards building a results-oriented public procurement policy.
- | Promote cost-efficient public procurement. Implement the recommendations which were outlined by FICIL to improve the public procurement process in order to involve more foreign businesses in tenders.
- | Improve the management of procurement contracts and make it more balanced.

<sup>10</sup> European Commission (2024) "Perceived independence of the national justice systems among companies" ([link](#))



# SUSTAINABLE FOR THE FUTURE

In today's rapidly evolving landscape, sustainability has become more than just a buzzword—it is imperative for businesses worldwide. Embracing sustainable practices is essential, not only for the health of our planet and society, but also for the longevity and success of businesses themselves. Companies that prioritise sustainability are better positioned to innovate, adapt to changing regulations, and meet the growing consumer demand for environmentally responsible products and services.

*FICIL recommends focusing on four key categories to achieve a more sustainable environment for businesses and society:*

## MANAGEMENT OF NATURAL RESOURCE AND NATURAL RESOURCE TAX

- | Negotiate industry-specific agreements to facilitate practical shifts toward decarbonization and sustainability, considering technical, economic, environmental, and social factors. Incorporate these into the National Energy and Climate Plan and other policy documents.
- | Create a catalogue of natural resources and construction materials, indicating their CO2 emissions and availability status (*plentiful, sufficient, depleting, scarce and similar*). A sectoral approach should be used to gradually develop such catalogue.
- | Conduct a thorough review of Latvia's natural resource taxation policy. Use taxation, public procurement, and financing to discourage the use of depleted and scarce resources. Enhance how the natural resource tax is applied, calculated, and paid, including better data management. Introduce regulatory requirements in financing, public procurement, and natural resource taxation to motivate the private sector's transition to sustainable practices and the “new normal”.

## HEATING AND WATER

- | Electrification of the district heating should be explored with a clear technical, economic and financial rationale, while other improvements should not be overlooked.
- | Scale up successful pilot projects for building cooling and ventilation, using public funds aimed at enhancing energy efficiency.
- | Significantly improve water supply and sewage systems to ensure quality services and functionality during extreme conditions.

## SUSTAINABILITY AND GREENWASHING

- | Government should increase efforts to prepare small and medium-sized businesses for upcoming changes. Help them remain in larger companies' supply chains by meeting ESG and sustainability standards. Implement laws to protect against misleading environmental claims. Hold accountable those who engage in or benefit from greenwashing, safeguarding consumers and the broader public.

## ENVIRONMENT IMPACT ASSESSMENT AND TERRITORIAL PLANNING

- | Make environmental impact assessments more efficient by limiting retroactive revisions and eliminating redundant activities. Continuously improve local territorial planning to support stable development across society and all economic sectors. Make environmental and climate issues integral parts of territorial planning and impact assessments.



# COMBATTING SHADOW ECONOMY

The shadow economy in Latvia remains a significant challenge, with estimates suggesting that uncollected taxes from this sector could amount to between 2 and 3.6 billion euros.<sup>11</sup> Despite efforts being made,<sup>12</sup> shadow economy levels have risen since 2016, with its first slight decrease last year.<sup>13</sup> The recently approved "Shadow Economy Reduction Plan for 2024-2027" marks a bolder and more comprehensive approach, setting a concrete aim. However, the success of this plan hinges on effective implementation, strong cross-sectoral cooperation, and the involvement of key stakeholders.

In order to combat the shadow economy more effectively, it is crucial to reduce the feeling of impunity for tax violations, by strengthening enforcement, ensuring efficient cooperation of the authorities, re-evaluating the effectiveness of penalties, and expanding the means of evidence. Additionally, improving the analytical capabilities and communication strategies of the State Revenue Service (SRS), through advanced data analytics and greater transparency, would improve the identification of compliance risks and encourage voluntary conformity. These combined efforts should not only reduce the shadow economy levels, but foster fair competition.

*FICIL recommends focusing on these key areas to reduce shadow economy levels:*

- | Ensure effective implementation of the "Shadow Economy Reduction Plan for 2024 - 2027", while granting the appropriate mandate and tools to the Ministry of Finance to ensure the plan is implemented, in order to achieve results. Strengthen the cross-sectoral (horizontal) cooperation among state institutions – key stakeholders in reducing the shadow economy level.
- | Reduce the feeling of impunity by ensuring efficient cooperation of the authorities, re-evaluating the effectiveness of penalties for violations, giving more powers to the SRS and beginning discussions on expanding the means of evidence.
- | Ensure that the SRS publishes their "risk markers" to increase taxpayers' self-compliance.
- | Implement a transparent, simple, and fair tax system with clearly communicated reforms that extend beyond budgetary goals. Ensuring predictability and continuity across successive governments is crucial for long-term business planning and sustainable economic development.
- | Enhance the SRS's analytical capabilities and communication strategy, and improve the quality of its services to encourage and motivate taxpayers.
- | Ensure a more appropriate segmentation of the SRS rating system to better reflect the current situation.



<sup>11</sup> "Shadow Economy Reduction Plan for years 2024 – 2027" ([link](#))

<sup>12</sup> Two plans. One for years 2016–2020, and the other – for 2021–2022. "Action Plan of State Institutions for Limiting the Shadow Economy for 2016–2020" ([link](#)). Informative Report "On the Implementation of Measures of the Shadow Economy Limitation Plan for 2021/2022" ([link](#))

<sup>13</sup> SSE Riga "Shadow Economy Index for the Baltic Countries" ([link](#))



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