

State Aid for Self-Employed Persons in Latvia and Other European Union Member States

Alona Irmeja¹, Mg.oec., PhD student; **Inguna Leibus**², Dr.oec., associate professor
Department of Accounting and Finance, Latvia University of Agriculture

Abstract. National competitiveness is based on competitive operators whose successful operation is dependent on favourable business environment. Such an assurance is the mission of the public administration. Regulatory environment, in which an entrepreneur operates, is as important as a relevant infrastructure and possible support for the business start-ups. Self-employment is a form of employment associable with a person's greater freedom of choice as well as increased risk chance. Even though self-employment is usually considered a part of employment policy, in a diverse sense, it can be regarded to as a first step towards forming a business. There is a wide range of labour market policies and measures, which support self-employment in the countries covered by the European Employment Observatory (EEO), such as financial support, subsidies, loans or microfinance, and advice; measures to reduce administrative burdens etc. The aim of the research is to explore the Latvian government and other European Union (EU) Member States support measures for self-employed persons. The authors conclude that almost all EEO countries have policies to support self-employment. Public support plays a major role in each country's aid policy and it is important for self-employed persons.

Key words: self-employment, state aid, European Union Member States, business.

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Introduction

The search of solution to the unemployment problem and economic growth problem at the present time is the major for governments around the world, particularly in Europe. One of the ways to improve the economic situation in the country is supporting the small business sector including self-employment with different types of aid instruments. The **aim of the research** is to explore support measures for self-employed persons applied in Latvia and other EU Member States. Tasks: 1) to find out national documents which prescribe the support for self-employed persons; and 2) to evaluate measures that exist for self-employment in Latvia and other EU Member States.

The study is based on the monographic method used to assess knowledge on self-employment, the development of a theoretical discussion on support measures and interpretation of the study results, graphical method as well as an abstract - logical method is used to separate the facts for drawing general conclusions.

Research results and discussion

Almost all countries have policies in place to support self-employment. Although, in some countries (e.g. Hungary, Turkey), it is not said to have been an important part of the political agenda (Self-employment in Europe, 2010).

One of the main long-term economic priorities of Latvia set as the government declaration is a favourable environment for business and investment. Latvia has made an important comprehensive document, which sets a target for the government of Latvia to ensure growth and outlines the main lines of action. This is the Latvian National Development Plan for 2007 - 2013. The

plan aims to promote balanced and sustainable national development and to improve the competitiveness of Latvia among other countries in the short-term period. Section 2 of the Plan refers to a company's technological excellence and flexibility, which includes subdivision "Creation of a New Competitive Company." The main challenges related to starting up a business plan are as follows: first, to promote public, particularly young people, interest to become entrepreneurs and set up their own business; to improve business prestige and reputation as well as to implement business start-up incentive programmes, training and advice; second, to provide a unified and effective support for business start-ups (mentor advice, financial support mechanisms etc.) (LR Regionālas attīstības..., 2006).

The newly proposed Europe 2020 strategy calls on the Member States to remove measures that discourage self-employment but, at the same time, urges countries not to promote involuntary or precarious self-employment. It also refers to self-employment and business in terms of access to education systems and mobility programmes promoting business and innovation among young people.

There is a wide range of labour market policies and measures, which support self-employment in the countries covered by the European Employment Observatory (EEO). The measures are categorised in this executive summary according to the following headings and are described in more detail below:

- 1) financial support, such as subsidies, loans, or microfinance;
- 2) specific support services for people wishing to set up a business including one stop shops;
- 3) the provision of training, mentoring, and advice (including consultancy);

¹ E-mail address: alona.irmeja@gmail.com

² E-mail address: inguna.leibus@llu.lv

- 4) measures to reduce bureaucracy/administrative burdens;
- 5) existing favourable conditions for the self-employed or changes to tax/social security regimes;
- 6) measures to increase motivation towards self-employment (Self-employment in Europe, 2010).

1. Measures offering financial support

The importance of providing start-up finance to enable people to access credit in order to set up a business has been recognised through the creation of the aforementioned European Progress Micro-finance Facility. This EUR 100 million fund is intended to support people at risk of losing or those who have already lost their jobs to obtain credit in order to set up a business.

In the **Czech Republic**, there are regular low-scale measures supporting business indirectly provided by the Czech-Moravian Guarantee and Development Bank, and the Export Guarantee and Insurance Corporation. Furthermore, retraining courses provided by labour offices enable start-up entrepreneurs to seek low interest rate loans from the START programme operated by the Enterprise and Innovation Operational Programme.

Enterprise **Estonia** offers start-up grants of approximately EUR 6 400 to those wishing to start a business in specific sectors, with a requirement of 20% own financing by the entrepreneur.

In **Spain**, it is possible to receive unemployment benefits as a lump sum payment, in order to start a new business. The unemployed may receive up to 60% of their total unemployment benefits in one single payment, in order to support them in their business creation process. Certain groups can get a higher proportion of the benefits: men under 30 years of age and women aged less than 35 years may receive 80% of the unemployment benefits that they are entitled to, in one lump sum payment.

In **Austria**, there are a number of measures to help with access to finance. One strand consists of state guarantees, through which companies can double their equity. For example, guarantees are granted by the Austrian Economic Service for 'innovative projects', which are no older than five years. In addition, the *Gründerbonus* (Start-up Bonus) consists of a one-off benefit for start-ups (Self-employment in Europe, 2010).

Among the measures to support self-employment and business in **Latvia**, businesses that are less than a year old will each be eligible for up to LVL 54 000 (EUR 76 205) in loans and up to LVL 5 000 (EUR 7 056) in grants for the starting of business and the repayment of loan. In Latvia, this task is committed to the state joint-stock company "Latvian Mortgage and Land Bank". These Regulations prescribe the procedure for start-ups, which use the support of the European Social Fund, the National Mortgage Bank from the amount of LVL 23 million (LVL 14 million financed by the ESF and the state, LVL 9 million - Mortgage Bank). These activities within the "Latvian Mortgage and Land Bank" are developed in six different support programmes, one of which supports a programme enhancing business start-ups. The Mortgage Bank offers new entrepreneurs a special support programme "Support for Self-employment and Business Start-up" or the Start programme. The programme aims to increase economic activity in the country, business start-ups developing knowledge and

skills as well as providing the necessary financial support for the economic activities. The programme is open to Latvian residents aged 18 years including the unemployed who have expressed a desire to start a business or self-employment as well as newly established businesses. It is also relevant to experienced entrepreneurs who want to start a new business activity (launch of an entirely new product or service) and consequently a new company. The programme supports projects up to LVL 60 000 with the client's participation in at least 10%. Participation is not required if the loan amount does not exceed LVL 5000.

Within the period from 1 September 2010 to 31 October 2011, the "Start programme" has provided financial support to 524 companies, of which 85% - Ltd, 11% - IC, and 4% - self-employed persons.

Most of the companies (all 524 of the project subjects), which participated in the "Start programme", represented the following industries: restaurants and catering services, tax consultancy, automotive maintenance and repair, clothing retail, and logging. On the contrary, IC and self-employed persons were registered in such sectors as hairdressing and beauty services, maintenance and repair, logging, retail sale of clothing and joiners, and leather goods.

2. Specific support services for people wishing to set up a business

Many of the national articles report that support services targeted at people who wish to start up a business have been or are in the process of being set up. These support services can take the form of one stop shops (as in Malta, Poland, Slovakia, the United Kingdom, or the Republic of Macedonia) or business incubators (for example, in Bulgaria, Latvia, Lithuania, Slovakia). In Ireland and Latvia, a regional approach has been used to provide support.

In **Bulgaria**, the Job Opportunities through Business Support project, which ran from 2000 to 2009, aimed to encourage employment by assisting the development of micro and medium-sized enterprises in small agricultural municipalities with high unemployment rates. One of the approaches used was to stimulate self-employment and small business development. All beneficiaries received direct services for facilitating the initial stages of their business development via a network of business centres and business incubators. The package of services provided included consultations, office and informational services, vocational training in small businesses, drafting a business plan and organising marketing surveys; leasing equipment to micro and mini companies; access to the Internet etc.

In **Ireland**, there are 35 County and City Enterprise Boards, located throughout the country. Their role is to develop indigenous enterprise potential and to stimulate economic activity on local level by assisting micro-enterprises (defined as having 10 or fewer employees). Each County and City Enterprise Board includes representatives from the social partners, state agencies, and local voluntary groups as well as elected local public representatives.

One-stop shops were introduced in **Slovakia** in 2007 to simplify access to the market for entrepreneurs by integrating all necessary administration related to

Table 1

Business incubators by region and area of activity in Latvia

Region	Name of incubator	Area of activity	Number of companies
Riga	General partnership "Rigas regiona attistibas inkubators"	Tukums, Limbazi, Ogre	53
	Creative industries business incubator Andrejsala	Andrejsala, Riga	69
Kurzeme	Foundation "Ventspils Augsto tehnologiju parks"	Ventspils, Talsi	49
	Ltd "Kurzemes biznesa inkubators"	Liepaja, Kuldiga, Saldus	52
Latgale	Society "Latgales aparatbuves tehnologiskais centrs"	Rezekne, Balvi, Daugavpils, Livani, Ludza	42
Vidzeme	Society "Biznesa inkubators Cesis"	Cesis, Madona, Aluksne	42
	"VBII" Ltd	Valmiera, Gulbene, Valka	40
Zemgale	General partnership "JIC Biznesa inkubators"	Jelgava, Dobeles, Jekabpils, Aizkraukle	82

Source: authors' calculations based on *Biznesa inkubatori, 2011*

business start-up and operation into one place in a time and cost-efficient manner. Apart from administering the registration in the trade and/or commercial register and issuing a trade licence, one stop shops enable persons at business start-up to complete income tax registration or registration for the purpose of compulsory health insurance, and provide for an electronic copy of a 'defaulter sheet'. Slovakia has also 16 entrepreneurial and technological incubators supporting new start-ups.

The **United Kingdom** has an established single service approach for providing support to new business start-ups, and the existing small and medium-sized businesses. Known as Business Link (in England), Business Gateway (in Scotland), and Flexible Support for Business (in Wales), these organisations offer an array of advice and guidance that includes help with developing a business plan (essential if start-up capital is required) and training courses for before and after a business is underway (Self-employment in Europe, 2010).

Eight business incubators are to be set up in **Latvia** in all regions with financial support from the European Regional Development Fund. These business incubators will provide discounted consulting and business services as well as the use of premises and facilities in the early years of business development (Table 1).

Activities are aimed at promoting the formation of new, viable and competitive businesses in the regions of Latvia, providing them with the necessary premises and advisory services. Business incubation is a unique and flexible business development process - a combination of infrastructure and personnel, designed to help develop new and small businesses by supporting the early stage of development with daily consultations based on business development issues.

According to the Appendix 2.3.2.1 Activity "Business Incubators" of the Cabinet Regulations No. 835 "Rules for the Operational Programme Entrepreneurship and Innovation" as well as the Ministry of Economics decision of 10 February 2009, Latvian Investment and Development Agency is the recipient of funding under this programme.

The project was launched on 27 February 2009 and it is scheduled to be completed by 31 December 2014. Total project costs are LVL 20,208,601, of which the European Regional Development Fund funding - LVL 17,179,419 or 85% of eligible costs and state budget financing - LVL 3,029,182 or 15% of eligible costs (*Biznesa inkubatori, 2011*). Eight business incubators were created in various regions of Latvia. Since January 2009, totally 429 companies have already used the Business Incubator services. Most companies are from Zemgale (Table 1).

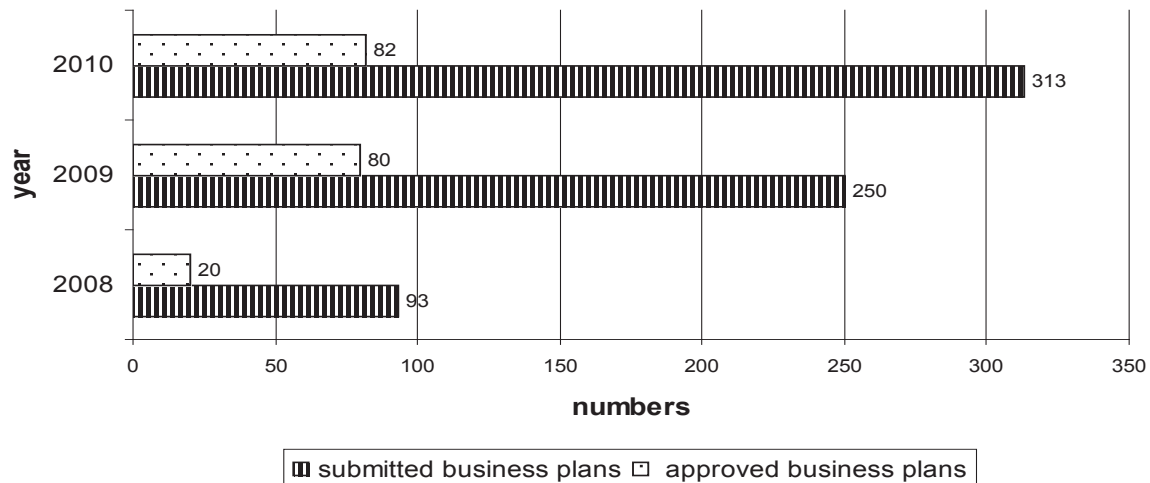
3. The provision of training, mentoring and advice

Several countries (Latvia, Lithuania, Luxembourg, Austria, Slovakia, Croatia, and Iceland) provide training, mentoring and/or advice services including consultancy support, either to people who have recently become self-employed or to those who might be thinking about setting up a business.

The **Lithuanian** Labour Exchange similarly provides information on the conditions for starting up a business, its development, the employment of employees, opportunities for pursuing activities under a business certificate; and organises basic business training for jobseekers.

In **Luxembourg** and **Croatia**, it is the social partners, which provide training and advice to the self-employed. In Luxembourg, self-employed workers need to be registered members of one of the sector-specific Professional associations (e.g. Chamber of Trade, Chamber of Agriculture). These associations offer guidance and expertise directly to members, and advise on the design and implementation of projects on self-employment. The Croatian Chamber of Trades and Crafts organises and helps with the education and improving the skills of new self-employed and the lifelong education and learning of the self-employed.

Austria and **Iceland** have introduced more targeted advice/training programmes. The Impra Unit of the Innovation Centre Iceland promotes innovation and new technology by assisting inventors and entrepreneurs with



Source: authors' calculations based on Pasakumi komercdarbības vai..., 2011

Fig.1 Submitted to and approved business plans by the State Employment Agency in Latvia, 2008 - 2010

advice and support, while in Austria, the AplusB initiative supports the start-up of new businesses stemming from the academic sector. The support offered consists of professional consultancy services for these potential future entrepreneurs (Self-employment in Europe, 2010).

The search of solutions to the unemployment problem at the present time is the major issue for governments around the world, particularly in Europe. In that sense, much of the discussion on finding solutions to the unemployment problem has focused on the pivotal role to foster business as a way to reduce unemployment, i.e. as an instrument of active labour market policy (Pfeiffer, Reize, 2000).

In Latvia, the State Employment Agency and the Ministry of Welfare provide support in the form of consultancy and financing to a small number of unemployed people who wish to start their businesses or transition into employment, with the recipients of support being those with the best business plans. The objective of activity "Measures of Business or Self-employment" is to provide advisory and financial support measures to help the unemployed with prior training and guidance for conducting business and business start-ups or self-employment and function successfully in a selected area for not less than two years.

The State Employment Agency offers help to registered unemployed persons. The unemployed receive the necessary help and support for business or self-employment:

- consulting business plan preparation and development (20 consultations within 6 weeks);
- If the agency's designated expert has given a positive opinion on the viability of a business plan and required by the State Employment Agency:
 - advice business plan of implementation in the first year (20 consultations);
 - business grants for business plan implementation - not more than LVL 2000 according to the approved business plan estimates;
 - monthly grant to support the implementation of activities at an early stage (the first six

months) - the minimum wage (Pasakumi komercdarbības vai..., 2011).

This programme becomes more urgent with each year passing among Latvian unemployed. If 93 business plans were submitted in 2008, then in 2010, the number increased three times (Figure 1).

An often-applied labour market policy to combat unemployment is to stimulate unemployed individuals to start their own businesses. Such policy may at least, temporarily lead to increases in self-employment. These policies may be called successful when the formerly unemployed individuals remain in employment for a longer period either as self-employed or as paid-employed worker and also when they become employers they contribute to reduce unemployment not only by creating their own jobs but also by hiring new employees (Congregado, Golpe, 2010).

4. Measures to reduce administrative burdens

As indicated above, one of the key areas for action identified in the 2005 Commission Communication on a modern policy for growth and employment was "red tape". A number of the national articles (Greece, France, Latvia, Malta, Austria, Portugal, Slovakia) show that steps are being taken on the national level to reduce bureaucracy and/or the administrative burdens and costs encountered when setting up and running a business. Some examples are listed below.

Greece has put the reduction of administrative burdens high on the political agenda. This is manifested, inter alia, by the recent bill on the simplification of procedures for the establishment of enterprises, which was submitted to the Parliament for discussion on 17 May 2010. The proposed legislative act foresees great reductions in costs (Self-employment in Europe, 2010).

The **Latvian** Government's plan for the support of micro-enterprises aims to decrease the costs of starting micro-enterprises by reducing the minimum capital requirements and simplifying the bureaucratic

requirements. An entrepreneur can establish a limited liability company with reduced share-capital less than LVL 2 000. From 1 May 2010 to 1 May 2011 in Latvia, totally 15,240 new limited liability companies were registered, of which 9508 (62.4%) were with reduced share-capital. Most companies with reduced share-capital were registered with a LVL 1 large capital (47.5%), while 26.6% - with a capital ranging from LVL 2 to 10 (No gada laika registretajam SIA..., 2011).

In **Slovakia**, recovery measures have been introduced, which simplify and reduce administration related to business operation. These include a shortened period for VAT reclaim (from 60 to 30 days), simplified fuel records (introduction of lump sum expenditures in the sum of 80% of fuel costs), simplified tax records and bookkeeping for entrepreneurs with an annual turnover below EUR 170,000. Another important measure to reduce the administrative burden of doing business was the launching of electronic communication with the commercial register (registration, statements, changes, de-registration, 50% lower fees for electronic communication rather than paper etc.). These are mainly legal entities, which benefit from this policy; though, natural entities/self-employed conducting business based on the commercial code may also gain.

In **Portugal**, the SIMPLEX programme is thought to have contributed to business creation by reducing bureaucracy and simplifying procedures associated with setting up a business (Self-employment in Europe, 2010).

5. Favourable tax or social security conditions for the self-employed

A number of countries have favourable conditions for the self-employed in terms of tax or social security contributions, or changes have been, or will be made in this area, sometimes in response to the economic crisis (as in Romania, Sweden, and the United Kingdom).

Taxes play a major role in the business environment. Robson and Wren (1998) find a negative relationship between the self-employment rate and marginal tax rates but a positive relationship between the average tax rates and the self-employment rate. Blau (1987) and Paker (1996) find that higher marginal tax rates lead to increases in the self-employment rate.

In **Slovakia** also, the current setting of the tax and social security system favours the self-employed compared with salaried employees. Calculations show that in a situation of equal labour costs and expected retirement pensions, the net income of a sole trader is 39% higher than that of an employee. The self-employed pay contributions from a lower assessment base (half of income attained in the previous year). They can also lower their tax base by lump sum expenses at 40% (and in some cases 60%) of income. The tax and contributions scheme allows various speculative base adjustments, by which entrepreneurs can decrease their tax and non-wage burden. Although, this is by no means a business-promoting policy, it acts as a key motive in the decision to start a business.

In **Romania**, the most significant measure has been the favourable income tax rate applied to micro-enterprises since 2007. Set at 2% in 2007, the rate gradually increased to 2.5 and 3% in 2009 but has been wholly eliminated by the government in 2010 within its crisis budgetary consolidation plan.

In **Sweden**, in response to the economic crisis, employers were given a respite from paying social security contributions and preliminary taxes for their employees for two months during 2009. The recent emergency budget in the **United Kingdom** has also brought about more favourable conditions for business start-ups. This includes an extension of the 10% relief rate for entrepreneurial activities; enlargement of finance for start-ups with the extension of the Enterprise Finance Guarantee; a reduction in corporate tax for small businesses; and exemptions from National Insurance contributions for new employees in areas outside the South East England (Self-employment in Europe, 2010).

From 1 January 2010 in **Latvia**, a natural entity performing economic activities in certain professions or activities may choose to pay patent fees. Patent fee is a fixed tax, covering income tax and state social insurance contributions for individuals of economic activities in the profession. Within 10 months (January 2011 – October 2011), the State Revenue Service has recorded 267 persons who wanted to pay patent fees: in Riga - 129, in Vidzeme - 75, in Zemgale - 28, in Kurzeme - 24, and in Latgale - 11. Most patents are issued to persons who collect the bounty of forests and meadows (Informativais ziņojums ..., 2011).

The Micro-enterprise Tax Law was adopted on 1 September 2010. Micro-enterprise – an individual merchant, an individual undertaking, a farm or fishing enterprise as well as a natural entity is registered as a performer of economic activity by the State Revenue Service. The micro-enterprise tax rate shall be 9%. Micro-enterprise tax includes mandatory state social insurance contributions, personal income tax, state fee of the business risk for micro-enterprise employees, and corporate income tax (Micro-enterprise Tax Law, 2010). On 1 July 2011, totally 12,575 micro-enterprise taxpayers were registered, while by 31 July this number had risen to 13,354 taxpayers.

6. Measures to increase motivation towards self-employment

Some people may argue that trying to become self-employed is not the most interesting entrepreneurial behaviour. Business is ultimately about wealth creation, not about the creation of a job for the founder. However, starting a business and entering into self-employment is in most cases the first step of an entrepreneurial career. To learn really about business, it is not sufficient to study success stories, one also needs knowledge on the process entrepreneurs go through on their way to success or failure. To demonstrate that a specific competence is central for entrepreneurial progress, the authors should incorporate them in business education and training programmes (Kolvereid, L, Isaksen, E. 2006).

In **Germany**, the Foundation Country Germany initiative, introduced by the Federal Ministry of Economics and Technology, focuses on young people, as it attempts to build motivation for self-employment through better information and promotion work at schools and universities.

In **Latvia**, the scope is broader; The Motivation programme was approved in December 2008 aiming to encourage as many people as possible to start their own businesses, to raise the overall prestige of business, and

to inform the society about the potential of innovation. It was introduced to support activities that improve the capacity of teaching personnel to motivate young people, activities that spread the best practices in starting businesses and developing innovation and marketing activities for innovation and businesses. More than LVL 2 million (EUR 2.8 million) of financing has been allocated to this activity, of which 85% is provided by the European Regional Development Fund. Finally, in **Luxembourg**, the Ministry of the Economy and Foreign Trade and the Ministry of Medium-sized Companies ran the *Trau dech – maach dech selbststänneg* (Have the heart to take part – become self-employed) campaign in 2004 to encourage the population to create new companies (Self-employment in Europe, 2010).

Conclusions, proposals, recommendations

1. Self-employment is an important driver in business and job creation, and thus, contributes to the European Union's goals of more growth and better jobs.
2. Almost all European Employment Observatory countries have policies in place to support self-employment. Exploring the European Employment Observatory public support for self-employment, the authors conclude that it has a major role in each country's aid policy, and it is important for self-employed persons. Improving the business environment is a focus of policy in some countries (Austria). Some countries have implemented education and awareness-raising activities to increase understanding of the opportunities offered by self-employment (Sweden), while other countries focus on supporting businesses to grow, or develop (Finland).
3. There is a wide range of labour market policies and measures, which support self-employment. The measures are categorised in this executive summary according to the following headings: Measures offering financial support; Specific support services for people wishing to set up a business, including one stop shops; Provision of training, mentoring and advice; Measures to reduce administrative burdens; Favourable tax or social security conditions for the self-employed; and Measures to increase motivation towards self-employment.
4. Turning unemployment into self-employment has become a major focus of the EU countries active labour market policy. In Latvia, the State Employment Agency and the Ministry of Welfare provide support in the form of consultancy and financing to a small number of unemployed people who wish to start their businesses or transition into unemployment. Policy makers should be careful about what to do with their stimuli, since in the context of a highly regulated labour market, these types of incentives could not generate desired effects on paid-employees who switch to dependent self-employment.
5. Recommendation for future research: it should investigate effectiveness of each support measure to find out if the national support programme

objectives have been achieved and what their results are. Future research should investigate the support for the unemployed people to start businesses and engage in self-employment, which could be a good tool in the fight against the unemployment. One of the solutions how to generate jobs and reduce unemployment would be focusing public opinion more on innovative and high-growth businesses than forcing the unemployed into engaging into self-employment.

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