



Mutual Learning Programme

DG Employment, Social Affairs and Inclusion

Peer Country Comments Paper - Latvia

Ten years informally, one year formally. How are social enterprises doing in Latvia?

Peer Review on "Social economy and social enterprises in legislation and practice"

Slovakia, 20-21 June 2019

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1 Introduction

This paper has been prepared for the Peer Review on "Social economy and social enterprises in legislation and practice" within the framework of the Mutual Learning Programme. It provides a comparative assessment of the host country and the situation in Latvia. For information on the host country policy example, please refer to the Host Country Discussion Paper.

2 Overview of key trends

2.1 Brief history of social entrepreneurship in Latvia

The concept of *social entrepreneurship* was introduced in Latvia in 2008, when the first social enterprises were created. These enterprises used business instruments to solve social problems, thereby creating sustainable financial resources for activities with a positive social impact. They were set up with the financial support of the Soros Foundation programme 'The Brigade', and a few of them are still in operation today. For example, the social enterprise 'Mammu', created to support young mothers by offering job opportunities while they are still at home with their children, and the charity shop 'Otra Elpa' ('Second Breath') providing grants for social projects and social enterprises (to support their activities or projects) from the revenue of their second-hand shops.

The first social enterprises used different legal forms – associations, foundations or regular business companies (Lesinska, 2014)¹. The turning point in the development of the social enterprise concept in Latvia was in 2014, when the government adopted a policy document 'Promoting development of social entrepreneurship in Latvia' (*Par sociālās uzņēmējdarbības ieviešanas iespējām Latvijā*)². This document recognized social enterprises as a legitimate instrument to solve different societal problems. In 2015 the Social Entrepreneurship Association of Latvia was created and played a key role in the drafting of the Social Enterprise Law.

2.2 The Social Enterprise Law and main policy options

On 1 April 2018, the Social Enterprise Law came into force and stipulated that social enterprise is a limited liability company which has obtained the social enterprise status and fulfils certain criteria. The working group established by the Committee on Social and Labour Affairs at the Parliament agreed that the most appropriate legal form for social enterprise will be the limited liability company because it is easy to establish and monitor its operation. Experts agreed that social enterprises should be private entities to ensure their independence and self-sustainability.

Criteria describing social enterprises in Latvia mirror the majority of criteria defined by the Social Business Initiative. To obtain the social enterprise status in Latvia:

1. an organisation has to have a positive social objective as the main purpose of the company;
2. all owners have agreed to obtain the status of social enterprise for their company;
3. there is a restriction on profit distribution to company owners – profits must be either reinvested in the company or invested to reach a social objective;
4. the company has to have paid staff – at least one employee with an employment contract;

¹ Lešinska A. (2014) Sociālie uzņēmumi - nevalstiskās organizācijas Latvijā (Social enterprises – non governmental institutions in Latvia). Available at:<http://providus.lv/article/socialie-uznemumi-nevalstiskas-organizacijas-latvija>

² Cabinet of Ministers (2014) *Par koncepciju "Par sociālās uzņēmējdarbības ieviešanas iespējām Latvijā"* (Policy document "Promoting development of social entrepreneurship in Latvia"). Available at: <https://likumi.lv/doc.php?id=269885>

5. there has to be a representative body in the company which consists of members of the target group or a relevant expert group (e.g. the executive body or supervisory body)³.

Target groups for social enterprises are socially vulnerable groups and are defined by the Cabinet of Ministers. Currently, 11 categories of vulnerable persons are included in the Cabinet Regulations⁴.

2.3 The registration process

To obtain the social enterprise status, an organisation must submit documents to the Ministry of Welfare, which is responsible for the support and promotion of the social entrepreneurship in Latvia. The Register of Social Enterprises is maintained and published on the website of the Ministry of Welfare⁵. According to most recent data (as of 3 May 2019), there are 58 organisations that have obtained the social enterprise status⁶. There are also about 200 organisations in Latvia that could be considered as social enterprises (Licite, 2018)⁷ using different legal forms – NGO or business legal forms, but due to fact that till 2018 there was no legal definition and official registry of social enterprises, a precise number of other organisations which can be considered as social enterprises is unknown. There is no research carried out on reasons why these organizations did not apply for social enterprise status. Potential reasons could be: their economic activities cannot be separated from NGO activities; they are not the main activities but supplementary activities of the NGO or the organizations are self-sustainable and do not see the benefits of registering. Social enterprises in Latvia are active in various fields – providing social and health services by running day care centres; providing catering services by creating a work place for persons with special needs or socially excluded persons (people with disabilities, refugees, ex-offenders); providing online services to support nursing homes and social care centres; providing bookkeeping services by creating a work place for the long-term unemployed and single parents; producing health care equipment for persons with disabilities; producing eco-friendly packaging, etc.

3 National policies and measures

3.1 Brief overview of support for social enterprises in Latvia

The main non-financial support instrument for economically active organisations with a social mission is the legal status that can be obtained, if the organisation fulfils the criteria defined in the Social Enterprise Law. The social enterprise status allows to receive financial support (tax deductions, in-kind support from state or local government), engage volunteers in their work and participate in specific public procurement procedures (e.g. public procurement with social clauses or privileged public agreements). The other driving force for social entrepreneurship activities in Latvia is

³ Saeima (2017) *Sociālā uzņēmuma likums* (The Social Enterprise Law). Adoption: 12.10.2017. Entry into force: 01.04.2018. Publication: "Latvijas Vēstnesis", 212 (6039), 25.10.2017.

⁴ Persons with disabilities, people with an intellectual impairments; members of the family recognized as needy; unemployed persons with one or more dependents, or is older than 54 or long term unemployed persons; Roma people; imprisoned persons and persons released from imprisonment; persons addicted to alcohol, drugs, toxic or other intoxicating substances and gambling; homeless persons; victims of human trafficking; refugee or a person who has been granted alternative status or a stateless person; orphans and children left without parental care aged 15 and over, and adults belonging to this group till they reach the age of 24 (including).

⁵ Information from the Ministry Of Welfare (2019), available at: <http://lm.gov.lv/eng/aktuali/aktuali-list/91030-nosaukums-social-enterprise-law-came-into-force-on-1-april-2018>

⁶ Register of social enterprises (2019), available at: <http://lm.gov.lv/lv/es-finansejums/lm-istenotie-projekti/aktualie-projekti/esf-projekts-atbalsts-socialajai-uznemejdarbibai/socialo-uznemumu-registrs>

⁷ Licite L. (2018) *Social enterprises and their ecosystems in Europe | Country report* available at: <https://sua.lv/wp-content/uploads/2018/12/Social-enterprises-and-their-ecosystems-in-Europe.-Country-report-Latvia.pdf>

the grant program 'Support for Social Entrepreneurship under the European Social Fund (ESF) run by the Ministry of Welfare.

3.2 Support mechanisms for social enterprises with special status

According to the Social Enterprise Law, local governments can grant a lower tax rate for the immovable property owned by a social enterprise and launch specific grant schemes for social enterprises to support their work. State institutions and local municipalities can transfer movable property into the ownership of a social enterprise without remuneration. In order to achieve the objectives defined within the Law, social enterprises can also engage volunteers.

A social enterprise can benefit from enterprise income tax relief – they are allowed to exclude the following expenses from the taxable base: 1) ensuring recreational and social inclusion measures to employees of the social enterprise belonging to the target group⁸; 2) integration of persons belonging to the target group in the labour market and improvement of their quality of life; 3) purchase of assets⁹ that serve for the purpose of attaining the objectives defined in the articles of association of the social enterprise; 4) ensuring social integration measures to persons belonging to the target group; 5) donations to a public benefit organisation for such purposes that conform to the objectives defined in the articles of association of the social enterprise, if by the end of the reporting year the recipient of the donation has submitted information to the donor on the utilisation of the donation.

3.3 Non-financial aid: Public procurement as a tool to support social enterprises

The Public Procurement Law grants certain direct support measures for social enterprises and enterprises with social impact (e.g. those employing persons with disabilities). According to the law, public institutions (local and/or regional) have right to:

1. issue public procurement procedures for organisations which employ persons with disabilities (at least 30% of the employees of the organisation)¹⁰;
2. reserve the right to participate in public procurement procedures to organisations that have a social enterprise status, but only for certain social services¹¹.

Public Procurement Law allows public institutions to use social clauses in public procurement procedures to choose the most socially responsible bidder.

Despite the fact that this regulation has been in force for more than one year, there are no examples where privileged agreements or social clauses in public procurement procedures were used. Some organisations working with social care issues are very successful in the public procurement procedures and have been working in this field for more than 20 years, but the public procurer always issued *ordinary* public procurement procedure (with lowest price as the main criteria).

3.4 Financial aid: Grant programme to support social enterprises

The main financial instrument to support social enterprises in Latvia is the ESF co-funded grant programme 'Support for Social Entrepreneurship', administered by the Ministry of Welfare. The purpose of the programme is to support social enterprises by providing non-repayable grants for both newly established enterprises and companies that are already operating and would like to expand their operation. The organization shall finance at least 10% of the total project costs. Until 1 April 2018, when the Social Enterprise Law came into force, the grant programme was available also for non-

⁸ Categories of target group are specified in the Cabinet Regulations No.173 "Regulations on socially vulnerable groups and on the procedure for awarding the status of social enterprise and registering and monitoring social enterprises")

⁹ For example, purchase of sewing machine or kitchen equipment, or a specially equipped car, etc

¹⁰ Public Procurement Law, Paragraph 1, Article 16.

¹¹ Public Procurement Law, Paragraph 2, Article 16.

governmental organisations or conventional business organisations dealing with societal problems. Since 1 April 2018, the grant programme was restricted only to organisations with the social enterprise status. The number of grant agreements signed with organisations without social enterprise status is thirty grant agreements (for the total amount of EUR 2 381 000, 82)¹² as well as twelve grant agreements signed with organisations with social enterprise status (for the total amount of EUR 506 234,82)¹³.

The grant programme is operated by a state-owned development finance institution ALTUM. The size of a grant ranges from EUR 5,000 to EUR 200,000. The funding can be used for capital expenses (except for land, real estate and infrastructure), wage subsidies, trainings and consultations and other working capital expenses. The total grant amount cannot exceed 90% of eligible costs. This program can be considered as the main financial support instrument for social enterprises in Latvia.

3.5 Compensatory aid: State aid to support organizations promoting integration through employment

There are two main instruments to support organisations promoting integration through employment – one is available just for social enterprises (the grant programme 'Support for Social Entrepreneurship' allows to receive funding for wages) and the other is available for all kinds of organisations providing work places for unemployed or persons with disabilities. This is a programme administered by the State Employment Agency, which provides several forms of *compensatory* aid – mostly 1) wage subsidies, 2) social insurance payments and 3) administrative/supportive assistance. Support instruments can be combined, but double financing must be avoided.

3.6 Indirect support instruments

There are several indirect support instruments for social entrepreneurship organisations (with or without legal status) in Latvia. In 2015 the Social Entrepreneurship Association of Latvia was established by five active NGOs - the Foundation for Open Society DOTS, the Policy Research Center PROVIDUS, the Latvian Samaritan Association, the charity shop 'Otra Elpa' ('Second Breath') and the social business accelerator 'New Door'. The association has more than 100 members - companies, organisations and people who believe that social entrepreneurship in Latvia has potential and who participate in co-creating and strengthening the sector. The association advocates interests on local, regional and national levels and provides capacity-building activities for its members. The association provides individual consulting services to help finding the right solution for outstanding challenges as well as to understand further steps in the development of a social enterprise or a social entrepreneurship idea.

To build the capacity of social entrepreneurship organisations (with or without legal status) two support organisations were established. In 2013, the accelerator programme 'New Door' was launched in Latvia. It is an international social entrepreneurship accelerator¹⁴ helping new companies to transform their social initiatives into sustainable social businesses by providing relevant knowledge and expertise. In 2014, the incubator 'Reach for Change' was created. It is an international social entrepreneurship incubator that aims to improve children's lives by providing support to like-minded social entrepreneurs.

¹² The first grant agreement was signed on January, 2018, the last – on May, 2019, Register of social enterprises (2019), available at: <http://lm.gov.lv/lv/es-finansejums/lm-istenotie-projekti/aktualie-projekti/esf-projekts-atbalsts-socialajai-uznemejdarbibai/socialo-uznemumu-registrs>

¹³ The first grant agreement was signed on December, 2018, the last on May, 2019 - Register of social enterprises (2019), available at: <http://lm.gov.lv/lv/es-finansejums/lm-istenotie-projekti/aktualie-projekti/esf-projekts-atbalsts-socialajai-uznemejdarbibai/socialo-uznemumu-registrs>

¹⁴ Organization has international donors and they provide consultations, mentoring and other non-financial support instruments for social enterprises

3.7 Impact measurement

According to the Social Enterprise Law, organisations that have obtained the social enterprise status will have to show the impact of their activities annually. The Ministry of Welfare is currently collecting information from social enterprises which obtained status in 2018. Due to fact that the law has been in force for just one year, it is not yet possible to evaluate the impact measurement tool and its effectiveness yet. According to the law, social enterprises have to submit an activity report to the Ministry of Welfare annually, identifying specific plans for the next year and showing results of the previous year. It is planned that organisations will provide quantitative data and qualitative information¹⁵ on the impact they have reached. There is no data collection guidance or format to report information, which can lead to a situation where the Ministry of Welfare might receive improper or incomplete data.

4 Assessment of success factors and transferability

4.1 Comparison of administrative measures for defining actors in social economy

As in Slovakia, social enterprises are regulated by a recently introduced law (Social Enterprise Law), stipulating that limited liability companies can apply for a special status granting access to various support schemes. Thus, other organisations with social impact (NGOs or businesses) are not recognized as social enterprises and are not eligible to receive state support stipulated in the Social Enterprise Law¹⁶. Those organisations can act under the Associations and Foundations Law (for NGOs) or the Commercial law (for businesses) and receive state support which is available for all organisations (e.g. wage subsidies for employing unemployed or persons with disabilities (except wage subsidies available at the grant programme 'Support for Social Entrepreneurship'), participating in public procurement procedures with social clauses (except Privileged agreements, available only for organizations with the social enterprise status) etc.). It is too early to measure the impact of the Social Enterprise Law, but the number of organisations that have obtained the social enterprise status in Latvia is higher than in Slovakia (58 organisations in Latvia (as of 3 May 2019) compared to 10 in Slovakia).

Regarding the debate in Slovakia on whether municipal social enterprises can be considered as true social enterprises, the Latvian example shows that municipalities are valuable partners for social enterprises allowing them to establish or to expand their operation by providing several support instruments. It is crucial not to influence the market and not to distort market competition but to provide adequate financial and non-financial aid. There are no social enterprises in Latvia established by local governments and state institutions, because they are allowed to establish businesses (or engage in business activities) in restricted cases only, as defined in the State Administration Structure Law. At the same time, there are several local authorities that have granted lower immovable property tax rate and/or organised grant competitions for social enterprises.

In both countries the registration process for receiving the social enterprise status is similar. However, in Slovakia, an umbrella organisation can make a binding recommendation to include an organisation in the register. The system to register a social enterprise in Latvia is a 'one-stop-shop' approach, a system easy to understand and apply. The dual system created in Slovakia has some advantages and some challenges. To ensure the quality of the decision taken by the umbrella organisation and

¹⁵ For example, organisations can use "Story telling method" or "Social Costs Benefit Analysis" to show the impact of activities.

¹⁶ For example, business without social enterprise status cannot receive a lower tax rate for the immovable property, or involve volunteers or apply for the grant program. NGOs cannot apply for the grant program. par.

to exclude any potential conflict of interest, it is very important to ensure this organisation's financial stability and independence. There is no information on how this is ensured in the Host Country Report. The main advantage of this dual system could be accessibility, if the umbrella organisation were located regionally, thus allowing social enterprises to submit all necessary documents in their place of operation instead of the capital, where the ministry is located as it is in Latvia.

To review documents submitted by organisations in Latvia, the Ministry of Welfare established the Commission for Social Enterprises, The Commission that meets once or twice a month, consists of representatives of other ministries and representatives of the social enterprise sector (e.g. NGO, universities, regional organisations, etc.). The participation of representatives from the social enterprise sector in the work of the Commission is remunerated. According to the law, the Ministry of Welfare has to take a decision (grant or reject a social enterprise status) within one month after the organization submitted all the documents. In practice, the decision-making process can take several months, often due to mistakes in the submission of documents by participants – e.g. submission of incomplete or wrongly completed documents. There has never been a case the Commissions' meeting was not held due to insufficient attendance of its members (absence of a quorum). The Commission grants objectivity of decision (due to multiple experiences of its members), neutrality (there is a restriction to participate in the decision-making process if there is any risk of conflict of interest) and high quality of the decision (each applicant participates in the commission's meetings, ensuring thorough review).

Latvia's Social Enterprise Law stipulates that social enterprises cannot distribute its profit to shareholders, the property and financial assets can be used only for the objectives defined in the statute of the organisation, while in Slovakia only a part of organisation's profit should be invested in achieving the objective of the organisation. Thus, in Latvia the system excludes shareholders from gaining any profit from the organisation, but organisations can get several state support instruments that are not available for social enterprises in Slovakia (e.g. local municipalities can grant lower immovable property tax rate for the immovable property, transfer movable property into ownership of a social enterprise without remuneration, etc).

The Host Country Report did not identify any obstacles in the administrative procedures that should be changed. To ensure that all enterprises registered social enterprise follow the criteria described in the Act 112/2018, it is very important to ensure the independence of the umbrella organisation.

4.2 Comparison of support instruments

In Slovakia, investment aid (loan and non-repayable) for social enterprises is not available yet (May, 2019), but can be considered as the main financial support instrument for social enterprises and enterprises with a social impact. In Latvia, the grant programme 'Support for Social Entrepreneurship' is available for social enterprises and helps policy makers to pilot the concept of social enterprise (e.g. legal regulations and restrictions (e.g. restriction to distribute profit), impact of existing support mechanisms, etc), by highlighting the strongest points and helping to identify the challenges to work with. This grant programme allowed to open a zero-waste café and a café providing work place for people with mental disabilities; to expand the production of medical care devices; in other words, the programme helped establishing social enterprises with low financial return but with high starting expenses.

In comparison to Slovakia, there are no service vouchers to support the work of social enterprises in Latvia. There is a similar system for social care services in Latvia – if several social care services are available, clients can choose where to receive it, but this differs from the system described in the Host Country Report.

Similar to Slovakia, public procurement procedures with the social aspect (with social clauses or privileged agreements) are very important tools to support organisations with

social impact in Latvia. However, these public procurement procedures are not used because the number of organisations with social enterprise status is not high, most social enterprises are small, with no capacity to prepare bidding documents and public organisations are not experienced in using these procedures.

In both countries there are support instruments for organisations that provide work places for the unemployed or persons with disabilities.

The Host Country Report showed that only some financial instruments are currently available. It is important to note, that the most interesting and useful instruments are not yet available, e.g. service vouchers and investment aid. The available instruments are in a form of wage subsidies, thus are interesting just for organisations promoting integration through employment. Therefore, one can conclude that the existing state support mechanisms in Slovakia are more favourable for social enterprises promoting integration through employment than for other social enterprises and are not helping to rise the number of registered social enterprises.

5 Questions

- Please share the 'lessons learned' from the case of the misuse of public funds that caused the negative connotation of the term 'social enterprise'.
- What considerations or facts were used when proposing the quota system for public procurement procedures with social clauses (or social aspects)?
- What are the main differences in registering a social enterprise by submitting documents to (1) the Ministry of Labour, Social affairs and Family and (2) the umbrella organisation? Are there any differences in documents that must be submitted or in the time frame for reviewing the application?

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Annex 1 Summary table

The main points covered by the paper are summarised below.

Situation in the peer country

- The Social Enterprise Law came into force in 1 April 2018. As of 3 May 2019, 58 organisations received the social enterprise status.
- The social enterprise status allows to get financial support (tax deductions, in-kind support from state or local government), engage volunteers in their operation and participate in specific public procurement procedures (e.g. public procurement with social clauses or privileged public agreements).
- The main financial instrument to support social enterprises in Latvia is the ESF co-funded grant programme 'Support for Social Entrepreneurship', administered by the Ministry of Welfare.
- There are two main instruments to support work integration organisations. First, is available for social enterprises (the grant programme 'Support for Social Entrepreneurship' allows to receive funding for wages). Second, is available for all kind of organisations providing work places for the unemployed or persons with disabilities.
- The Public Procurement Law grants some direct support for social enterprises and enterprises with social impact (e.g. employing persons with disabilities).

Assessment of the policy measure

- The Social Enterprise Law has been in force for just one year, therefore it is too early to measure the impact of the policy measures.
- The grant program can be considered as the main financial support instrument for social enterprises in Latvia. There is an uncertainty on which financial instrument that will replace if after 2022.
- Despite of supportive legal regulations, state institutions and public procurement do not use instruments stipulated in the Public Procurement Law. There is a lack of understanding and knowledge how to use the privileged agreements or social clauses in the evaluation process.

Assessment of success factors and transferability

- There are no social enterprises in Latvia established by local governments and state institutions. It is crucial not to influence the market and distort the economic competition, but provide adequate financial and non-financial aid. State institutions and local governments in Latvia can grant lower immovable property tax rate and/or organise grant competitions for social enterprises or use options stipulated in the Public Procurement Law.
- The registration process for receiving the social enterprise status is similar in both countries. To review documents submitted by organisations in Latvia, the Ministry of Welfare established the Commission for Social Enterprises. This body consists of representatives from other ministries and representatives of the social enterprise sector. Representatives from the social enterprise sector who participate in the Commission are remunerated.

Questions

- Please share the 'lessons learned' from the case of the misuse of public funds that caused the negative connotation of the term 'social enterprise'.
- What considerations or facts were used when proposing the quota system for public procurement procedures with social clauses (or social aspects)?
- What are the main differences in registering a social enterprise by submitting documents to (1) the Ministry of Labour, Social affairs and Family and (2) the umbrella organisation? Are there any differences in documents that must be submitted or in time frame for reviewing the application?

Annex 2 Example of relevant practice

Name of the practice:	The Social Enterprise Law – the policy instrument to define social enterprises and stipulate state support instruments
Year of implementation:	The law is in force from 1 April 2018
Coordinating authority:	The Ministry of Welfare
Objectives:	The purpose of the law is to improve the quality of life and to promote employment for target groups, through creation of an economic environment supportive to social enterprises. The Law creates the legal framework by providing both the criteria for obtaining the status of a social enterprise and the procedure for state support.
Main activities:	<p>The law defines criteria describing social enterprises and sets out the procedure to obtain the status of the social enterprise.</p> <p>To obtain the social enterprise status in Latvia, organisation has to have a positive social objective as the main purpose of the company; all owners have agreed to obtain the status of social enterprise for their company; there is a restriction on profit distribution to company owners – profits must be either reinvested in the company or invested to reach a social objective; the company has to have paid staff – at least one employee with an employment contract; there has to be a representative body in the company which consists of members of the target group or a relevant expert group (e.g. the executive body or supervisory body) .</p> <p>The law stipulates provisions of the state support and describes the control mechanisms.</p>
Results so far:	<p>As of 3 May 2019, 58 organisations received the social enterprise status.</p> <p>The Commission for Social Enterprises are meeting once or twice a month to review documents submitted by organizations.</p> <p>The Social Enterprise Law is in force just one year, therefore it is too early to measure the impact of provided solutions and policy measures.</p>

