**MICROENTERPRISE TAXATION, EMPLOYMENT, AND EARNINGS**

**MIKROUZŅĒMUMU NODOKĻIS, NODARBINĀTĪBA UN DARBA IENĀKUMI**

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The microenetrprise tax (MET) regime in Latvia was introduced at the end of 2010 as a tool to foster job creation in a country hardly hit by the crisis. During the last year the MET regime was in the spotlight of policy debate; recent and further projected changes in MET remain a focal point of the dialog between the government and social partners. This paper employs full-coverage administrative data to look at the evolution of the MET regime from two angles - sector-specific and worker-specific. First, we identify sector-specific factors which determine the share of MET workers in private employment reached in 2015, as well as the change in tax burden, labour cost, and labour productivity between 2010 and 2014. It appears that, other things equal, the share of microenterprise workers increases with pre-MET burden of labor taxes and profit taxes (each measured as a share of turnover); there is also evidence that firms in sectors with wide-spread wage manipulation practices were more likely to use the MET regime. However, while reduction of the tax burden was a strong (and in many case the only) incentive to enter the MET regime, and sectors with larger shares of MET-only workers indeed have seen larger cuts (or smaller increases) in the burden of main taxes, the share of mixed workers (those having earnings at both MET and the general tax regime) has an opposite effect.

The expansion of the MET regime had an economic impact beyond purely fiscal effects: other things equal, sectors with higher shares of microenterprise workers in 2014 feature smaller growth (or larger decrease) of real labour productivity, as well as larger growth of nominal unit labour costs. However, expectedly, the effect of the MET share in employment on labour cost per full-time equivalent worker is negative.

At the individual level, we analyze worker flows and identify large inflows to the MET regime from the general tax regime but also substantial inflows from non-employment or informal employment. Finally, we classify microenterprise workers into four groups and compare their earnings history over 2008-2015 with that of employees without microenterprise earnings.

**Key words:** *Earnings, informal employment, labor taxation, microenterprise tax, productivity*