

KĀRLIS KETNERS

Directions in the evolution of Latvia's public finance legislation

Latvijas publisko finanšu regulējuma attīstības virzieni

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Introduction

The foundation of the public finance law system in the Republic of Latvia is the Constitution (*Satversme*), which contains only a few provisions addressing financial law issues. Article 66 states that

“annually, before the commencement of each financial year, the Saeima shall determine the State Revenues and Expenditures Budget, the draft of which shall be submitted to the Saeima by the Cabinet. If the Saeima makes a decision that involves expenditures not included in the Budget, then this decision must also allocate funds to cover such expenditures. After the end of the budgetary year, the Cabinet shall submit an accounting of budgetary expenditures for the approval of the Saeima”.

Article 73 specifies that the Budget and laws concerning loans, taxes, customs duties, railroad tariffs, military conscription, declaration and commencement of war, peace treaties, declaration of a state of emergency and its termination, mobilisation and demobilisation, and agreements with other nations may not be submitted to national referendum¹.

¹ Latvijas Republikas Satversme [The Constitution of the Republic of Latvia]. (15.02.1922). Available at: <https://www.likumi.lv> [last viewed 15.10.2025].

Budget and tax laws regulate the Latvian public finance system². The Latvian tax system and its legislation have a relatively short history, having been introduced in 1990. The current tax legislation is primarily based on the continuation of the tax policy established since the tax reform of 1995. Initially, tax policy was not aimed at relatively high profit and property taxes, combined with penalties and high interest rates on overdue tax debt, but instead shifted its focus to indirect taxation, influenced by the country's accession to the EU and EU tax regulations. The tax and fees system in Latvia consists of state taxes, the object and rate of which are set by the *Saeima*; state fees applicable according to the Law "On Taxes and Fees", specific other laws, and regulations of the Cabinet of Ministers; local government fees applicable according to the Law "On Taxes and Fees" and binding regulations issued by the local government council; and directly applicable taxes and other obligatory payments set in European Union regulatory enactments. Other researchers have noted that the Latvian tax system is quite young; however, Latvia has succeeded in creating a viable and effective tax system in a comparatively short period, balancing the main fiscal aims (ensuring state budget revenue) with the use of taxes as an instrument of economic policy³. Latvia has succeeded in doing so because, during the reorganisation of the tax system in the mid-1990s, new tax laws were developed based on the experiences of developed democratic countries and in consideration of advice from experts representing various international organisations. From this perspective, it could be argued that Latvia, in creating its tax system from the ground up, has had certain advantages over "old" tax systems. The current Latvian tax policy is primarily based on the continuation of the tax policy implemented since the 1995 tax reform⁴. Generally, the system's goal has been to ensure capital inflow and promote capital market activities, thereby increasing foreign direct investment and fostering national economic development. Recent developments in the tax system have primarily focused on abolishing discriminatory and restrictive provisions by extending relevant exemptions, as well as addressing the impact of the COVID-19 crisis on public finance and tax laws⁵. As for social insurance laws, the Soviet understanding of social

2 *Lazdiņš, J.* (red.) *Latvijas tiesību avoti. Valsts dibināšana – neatkarības atjaunošana* [Legal sources of the Latvian state. Documents and commentaries]. Dokumenti un komentāri. Rīga: Tiesu Namu Aģentūra, 2015.

3 *Robežniece, D., Jurušs, M.* Tax policy in Latvia on the Eve of enlargement. *Baltic Journal of Economics*, 2003, 4.1: 116–120, p. 117.

4 *Lazdiņš, J.* Tendencies in the Development of Laws in the Republic of Latvia after the Renewal of Independence in 1990–1991. *Journal of the University of Latvia. Law / Latvijas Universitātes žurnāls. Juridiskā Zinātne*, 8, 2015.

5 *Ketners, K., Jarockis, A., Petersone, M.* State budget system improvement for informed decision-making in Latvia. *Scientific Bulletin of Mukachevo State University. Series Economics*, 11(3), 2024, pp. 86–99.

insurance law was abandoned immediately after the de facto restoration of the Republic of Latvia's independence, culminating in the enactment of the Second Social Insurance Law, which personified social insurance contributions and introduced the principle of "actual contributions". Latvia's public finance management system has developed in line with political and administrative changes from a socialist planned economy, the dismantling of which was the most important task in restoring Latvia's independence.

1. Development of the Budget Law from the 1990s to the 2020s

The Latvian budgetary process law is represented by the Law on Budget and Financial Management (hereafter also – LBFM)⁶. Before 1994, within the framework of total planning in the USSR, the budget was thoroughly planned, accurately forecasting annual revenues and expenditures, as well as the amount of taxes to be collected. The budget was drawn up according to the principle of administrative classification, ensuring complete control of expenditure at all levels. The budget was planned for a five-year period, with income and expenditure amounts specified for each year. The Supreme Council of the USSR approved the budget law. As previously mentioned, the budget of the Latvian SSR was essentially part of the USSR budget, and the integration of the Latvian budget into the USSR budget was as close as the political and socio-economic integration of the Latvian SSR into the USSR. The budget of the Latvian SSR consisted of two parts: the republican budget and local budgets (the budgets of large cities and municipalities–districts). The republican budget was used to make various mutual settlements with the USSR budget and received subsidies from the USSR budget and made payments to it. Notably, during the period of USSR occupation, several areas were directly subordinate to the USSR and were outside the jurisdiction of the local (Latvian SSR) government on Latvian territory. These areas were financed directly from the USSR budget, without the intermediation of the Latvian SSR budget. Ministries and their subordinate institutions were able to calculate norms without difficulty when planning their expenditure for planned measures. Enterprises were divided into wage groups based on sector-specific economic indicators. The Latvian SSR budget law was usually no longer than 2–3 pages. For example, the 1988 Latvian SSR state budget law consisted of nine articles, which specified the republic's revenues and expenditures, which in Latvia were less than revenues. The remaining articles separately specified expenditures for financing the national economy and allocations for social and cultural events, as well as for the maintenance of state power and state administration bodies, expressed in a single figure format, without providing any insight into the economic classification of the budget.

⁶ Law "On Budget and Financial Management" [Likums par budžetu un finanšu vadību] (24.03.1994.). *Latvijas Vēstnesis*, 41, 06.04.1994. Available at: <https://likumi.lv/ta/id/58057> [last viewed 15.10.2025].

According to the budgetary administrative division, the approximate expenditure and revenue for each district were specified, along with the percentage of tax deductions. The changes were marked by the proclamation of economic sovereignty and the formation of a new legal framework. Thus, the Supreme Council of the Republic of Latvia adopted the Law on the Budgetary Rights of the Republic of Latvia⁷. The law stipulates that the budget system of the Republic of Latvia consists of the state budget, the state social insurance budget, and local council budgets (local budgets) as separate, independent parts. The state budget, the state social insurance budget, and local budgets were to include convertible currency budgets as independent components. The specifics of applying individual articles of this Law to convertible currency budgets were determined by the Supreme Council of the Republic of Latvia. Local budgets refer to the budgets of districts, cities, city districts, and other municipalities. Budgets were interrelated within the framework established by law. The distribution of budget revenues and expenditures between the state budget and local budgets shall be determined by the Supreme Council of the Republic of Latvia. Budgets are approved for one year, from 1 January to 31 December, inclusive. If necessary, the Supreme Council of the Republic of Latvia may determine that the budget be drawn up for a shorter financial period. This option was used in 1992 and 1993 because of hyperinflationary conditions. In accordance with the regulations of the state budget of the Republic of Latvia, the Law defines the structure of the Republic of Latvia's state budget revenue, stipulating that the state budget of the Republic of Latvia combine funds for the financing of programmes of national and international importance, as well as other expenditures provided for in this Law. The Law also stipulated that, if necessary, bank loans, state borrowings, loans from other countries' budgets, and local budget funds may be used to cover the state budget deficit or specific budget expenditures, subject to repayment or other conditions, without being included in the budget revenue section. Loans, humanitarian aid, targeted programmes, and other types of financial resources must be presented in a separate annexe to the state budget, indicating repayment and any additional conditions. If these funds are received during the budget execution period, they shall be included in the annexe to the budget, as specified in the Law on amendments to the state budget. The famous "one-twelfth rule" is also found in the Law on budgetary affairs, e.g.

"If budgets have not been approved by the beginning of the planned budget year, then, until their approval, monthly financing for the planned financial period shall be carried out in the amount of one month's share of the budget for the previous financial period."

7 On the Budgetary Rights of the Republic of Latvia. [Par Latvijas Republikas budžeta tiesībām]. (27.06.1990.). Gazette of the Supreme Council and Government of the Republic of Latvia, 29, 19.07.1990. Available at: <https://likumi.lv/ta/id/76213-par-latvijas-republikas-budzeta-tiesibam> [last viewed 31.10.2025].

It can be concluded that in the first years after the restoration of independence, the previous budget structure remained largely unchanged, but the budget became more extensive. Expenditures were distributed among institutions, with the gradual introduction of a classification system by function. The reserve fund, currency fund, and extra-budgetary funds were separated as distinct components of the budget. Thus, the 1991 budget introduced classifications of revenue by tax type and of expenditure by institution. Two state functions were reflected separately: health care and education. In the 1994 state budget, ministries were coded for the first time, making the budget law more transparent. Each ministry is also shown the distribution of budget funds by function, although the budget expenditure items remain the same as before: state investments, the budgetary institutions' wage fund, and institutional maintenance expenses. It must be admitted that in the early years, budget items for all ministries were not unified. If a ministry had special requirements, specific items would appear in its budget, such as a scholarship fund, a service payment fund, and others, making the budget difficult to review.

A systematic approach to public finance management was initiated in 1994 when the *Saeima* adopted the Law on Budget and Financial Management, which, with annual amendments, remains in force today⁸. The LBFM determines the procedures for the formulation, approval, and implementation of the State budget and local government budgets, as well as the stakeholder's responsibilities in the budget process. Financial management, as defined in this Law, applies to the funds of the State budget and local government budgets. In the mid-1990s, Latvia widely adopted foreign experience in improving public administration models and financial management systems. This move sparked interest in enhancing the financial accounting and budget execution processes, making them more transparent and revealing the actual financial situation of central government institutions. To achieve this objective, the state budget had to reflect the revenues generated by ministries and their subordinate institutions through providing services to the population. These revenues had not previously been included in the budget. As a result, in 1995, the state budget was divided into a basic budget and a special budget. The transition to including the ministries' own revenues in the basic budget began, with a portion remaining in the ministries' special budgets. These changes were met with resistance from the ministries, who could not accept changes that restricted their right to reallocate financial resources without objection⁹. The Law "On local govern-

⁸ Ketners, K. Budget Process and Fiscal Rules: Analysis of Past Progress and Future Development. Proceeding of International Scientific Conference "Whither Our Economies-2014", Vilnius: MRU Publishing House, 2014, pp 46-54.

⁹ Ketners, K., Titova, S. Nodokļu politika Eiropas Savienības vidē [Tax Policy in the European Union Environment]. Rīga: Banku augstskola, Biznesa un finanšu pētniecības centrs, 2009, 244. lpp.

ments' budgets"¹⁰ determines specific procedures for local government budget approval and execution. According to OECD research, Latvia's budget process is transparent and institutionally sound but suffers from short-termism, frequent political instability, and weak medium-term fiscal planning.¹¹ Programme-based budgeting and a system of performance indicators were introduced in 1997 to ensure budget transparency. The reform did not resolve the problems of budget formulation, as budget programmes were created according to administrative divisions and institutions' investments, rather than by analysing policy objectives and achievable results. This innovation, although improving the structure and transparency of the budget, still did not ensure the essence of the budget transparency principle – providing accurate information on how taxpayers' money is being spent.¹² Programme-based budgeting system was consistently improved in 2000s and last amendments to LBFV were done in 2024. Until 2012 the approach to budget planning involved a pattern of in-year adjustments with at least one supplementary budget and additional (incremental) expenditures each year. In contrast, a series of substantial expenditure cuts had to be made to the 2009 budget to adjust to the unfolding crisis and to maintain external financial support. During the fiscal adjustment process, the regular budget formulation schedule was suspended, and budgeting lost its annual character. The budget preparation process was reformed in 2007 by introducing a formal medium-term budget framework. According to the LBFM, the medium term is three years, formed by the financial year for which the state budget is planned and the subsequent two financial years. Amendments to the LBFM, which entered into force on 1 January 2012, provided that the Framework, approved by the Cabinet of Ministers, shall be developed in the form of a law as the Medium Term Budget Framework Law, to be approved by the *Saeima*, thus ensuring that financial indicators included in the Framework Law and to be achieved are legally binding. The financial indicators should underpin the annual state budget law. The first Framework Law was prepared in 2012 and submitted to the *Saeima* as part of a single legislative package with the State Budget Law for 2013. The Framework Law is linked to development planning documents, thus ensuring the allocation of available financial resources in accordance with government policy priorities for the medium term. From 2023 budget year, annual budget law and the Framework law are merged in single state budget law. In the field of

10 On Local Government Budget [Par pašvaldību budžetiem]. Available at: <https://likumi.lv/ta/en/en/id/34703-on-local-government-budgets> [last viewed 15.10.2025].

11 Kraan, D. J., Wehner, J., Sheppard, J., Kostyleva, V., Duzler, B. Budgeting in Latvia. OECD Journal on Budgeting, OECD Publishing, 9(3), 2010, pp. 185–227. <https://doi.org/10.1787/budget-9-5kmh6dmr9zvkk>

12 Ketners, K. Developing potential budget reform for Latvia: Shifting from conventional to contemporary budgeting. Social and Legal Studios 2.7., 2024.

budget-regulatory legislation, Latvia also adopted the Fiscal Discipline Law¹³ in January 2013, which formulates national numerical fiscal rules, provides principles for linking the annual budget to medium-term budgetary plans, allows for justified escape clauses, and foresees long-term stabilisation mechanisms for budget balance. The purpose of the Fiscal Discipline Law is to prescribe fiscal policy principles and conditions that ensure a balanced budget throughout an economic cycle, thereby facilitating sustainable state development and macroeconomic stability, while reducing the negative impact of external factors on the national economy. The Fiscal Discipline Law also provided for the creation of a Fiscal Discipline Council as an independent, collegial body established to monitor compliance with the rules of fiscal discipline. This Council, as an independent fiscal policy supervision institution, has been functioning since 1 January 2014, and its main task is to monitor compliance with set fiscal rules, provide evaluations of budgetary elements at different stages of the budget process, and warn respective institutions in case of non-compliance. Since 2016, the spending review of individual programmes has been carried out by working groups established by the Ministry of Finance, following a proposal by the Ministry and a decision by the Cabinet of Ministers. Various partner organisations have also been involved in this process. However, experience has shown that in most cases, the review of expenditure by ministries is seen as an opportunity to request additional funding rather than an opportunity to assess the effectiveness of the use of allocated budget funds. The failure of budget programme reviews to date stems from the way the process was organised – sufficient time and resources were never allocated for a serious analysis of functions and programmes. Attempts to fit the spending reviews into the regular budget planning cycle resulted in a superficial review that quickly concluded that optimisation was not possible. Notably, in all countries that have successfully reduced their budget base, programme reviews are carried out by specially established audit or analysis institutions, which are given more than a few weeks to develop optimisation proposals.

Overall, the changes to budget planning introduced in the 1990s can be seen as an attempt to adopt new management methods and results-oriented budget planning. However, no significant changes were achieved during this first period of reform. The reforms were implemented only partially, often through formal measures that had been successful in other countries. However, Latvia did not achieve such results. One of the main reasons why the reforms were not effective enough was that all the changes were implemented separately. No reform policy was developed, no goals were set, and no achievable results were defined. No specific action was planned, and the purpose of the reforms remained unclear – the innovations proposed by the ministries were

13 Fiscal Discipline Law [Fiskālās disciplīnas likums]. (31.01.2013.). Available at: <https://likumi.lv/ta/en/en/id/254896-fiscal-discipline-law> [last viewed 15.10.2025].

often perceived as additional, burdensome formal procedures that did nothing to improve their work. The overall lack of policy planning is also evident in the planning of budget reforms (or rather the lack thereof). As in other countries, budget reform in Latvia is a long-term process. At each stage of development, understanding the causes of failure and implementing the necessary changes in the public administration model are crucial. Although the reforms introduced in the 1990s were designed to achieve results-oriented budget planning, the reforms did not ensure that the objective was achieved.

Based on the review of the development of legal regulation of public finance in the Republic of Latvia, specifically related to budget and tax affairs. The study identifies and elaborates on the substantive characteristics of modern budgetary principles in Latvia, as well as their trends:

- *Principle of Complexity.* The principle of complexity stipulates that the budget system must be viewed as an integrated whole, encompassing interrelated components of revenue, expenditure, and financial management. The principle ensures that the regulation of public finance considers the systemic interactions between various fiscal instruments and institutional mechanisms.
- *Principle of Timeliness.* The principle of timeliness requires that all stages of the budget process – preparation, approval, execution, and reporting – occur within legally defined timeframes. Adherence to this principle promotes fiscal discipline, predictability, and the efficient allocation of public resources.
- *Principle of Historical Sequence.* The principle of historical sequence emphasises the importance of continuity in budgetary policy. The principle requires that the formulation of new budgets take into account the financial outcomes, obligations, and experiences of previous fiscal periods, ensuring the progressive development of fiscal governance.
- *Principle of Annuality.* The principle of annuality establishes that the budget shall be approved and implemented for a fixed fiscal year. This temporal limitation ensures periodic review of fiscal policies, promotes accountability, and enables adaptation to changing economic and social conditions.
- *Principle of Strategic Approach.* The principle of strategic approach asserts that budgetary planning must be aligned with the state's long-term development objectives, fiscal sustainability strategies, and policy priorities. The principle reinforces the role of the budget as a key instrument of strategic governance and public policy implementation.
- *Principle of Consistency.* The principle of consistency requires coherence and stability in fiscal policy, legislation, and administrative practice. The principle ensures that budgetary decisions are predictable, logically aligned, and sustained over time, thereby fostering trust in public financial management.

2. Budget regulation and institutional framework

Article 66 of the Constitution regulates the division of competencies between parliament and the government. This article reveals the principle of separation of powers, according to which the specific competencies of the executive and legislative authorities are separated in the field of drawing up and reviewing the State budget. The executive branch drafts a budget for the state's revenues and expenditures for the financial year, which is submitted to the Cabinet of Ministers. However, the *Saeima* must approve the budget. Thus, only the Cabinet has the right to initiate the draft State Budget Law, and the Cabinet is responsible for establishing the proposal of the state budget plan¹⁴.

The leading actors in the annual budget planning process are the Cabinet of Ministers, the Ministry of Finance, and line ministries. The Bank of Latvia has an advisory role in the process. The aforementioned constitutional provision for the submission of the draft budget law to parliament is elaborated in the Law on Budget and Financial Management. The provision requires that the Cabinet submit the draft budget law to the *Saeima* no later than 1 October (Article 21 of the LBFM). During the economic crisis, external actors – particularly the IMF and the European Commission – also exerted substantial influence on budgetary decisions. If the *Saeima* rejects the annual draft budget submitted by the Cabinet at the first or second reading, the rejection is regarded as a vote of no confidence in the Cabinet (Article 30 of the Rules of Parliamentary Procedure). Since 1991, the government has had to resign for this reason only once. The *Saeima* is authorised to amend the draft budget proposed by the Cabinet.

However, the Constitution restricts the amendment powers of parliament by the following provision:

“If the Saeima makes a decision that involves expenditures not included in the budget, then this decision must also allocate funds to cover such expenditures.”

The restriction is further elaborated in Article 10¹ of the Law on Budget and Financial Management:

“In the decisions of the Saeima, the adoption of which relates to expenditures not provided for by the budget, provision shall also be made for funds by which such expenditures shall be covered. In cases provided for by law, the Minister of Finance shall submit an opinion concerning submitted draft laws no later than two weeks from the date of receipt of the relevant draft law.”

In practice, an amendment increasing expenditures can be achieved by either correcting the revenue estimation or adjusting the tax rate for specific taxes. Both are

¹⁴ Latvijas Republikas Satversmes komentāri. V nodaļa. Likumdošana. Rīga: Latvijas Vēstnesis, 2019, 59. lpp.

difficult to realise; thus, the total amendment power of parliament remains limited. The budget adopted by parliament takes effect at the beginning of the budget year. However, if an annual state budget has not been enacted on time, the Minister of Finance approves the state budgetary expenditures, provided that the monthly expenditures do not exceed one-twelfth of the appropriations from the previous year. (The deadline is usually respected, but delays have occurred in some parliamentary election years.) The separation of powers is also ensured by the *Saeima's* financial independence. After the budget request of the *Saeima* has been examined by the committees and approved by the Praesidium, the request is submitted to the Minister of Finance, who incorporates it without any amendments into the draft budget law. The Praesidium decides issues related to the financial management of the parliament. Bookkeeping records, the legitimacy and usefulness of expenditures, and the annual report of the parliament are audited by the Public Expenditure and Audit Committee (Chapter VII of the Rules of Parliamentary Procedure). The LBFM enumerates a set of documents that must be submitted in conjunction with the annual budget bill: proposals for amendments to substantive laws that conform to the draft budget law (referred to as “budget-related draft laws”) and explanations of the draft budget law.

A few judgments of the Constitutional Court have been landmarks, including the judgment of 29 October 2020 (Case No. 2019-29-01). The Constitutional Court affirmed its complete competence to review the compliance of budgetary laws with the Constitution, even though budget laws are politically sensitive. The Court emphasised that Article 66 of the *Satversme* reflects the principle of separation of powers, distinguishing between the executive’s role in drafting and the legislature’s role in approving the budget. The Cabinet of Ministers retains the exclusive initiative in preparing the draft state budget, constrained by legally established obligations but not by fixed budgetary allocations set in other laws. The Court held that the Law on Higher Education Institutions, which prescribed a binding link between GDP and higher education funding, unconstitutionally restricted the Cabinet’s competence to develop a balanced, economically sound budget. By effectively transferring part of the budget-drafting authority from the executive to the legislature, the norm violated Articles 1 and 66 of the Constitution. Consequently, the Court reaffirmed that pre-allocating portions of the budget through substantive legislation undermines fiscal transparency, executive responsibility, and the coherence of the state budget. In the Judgment of 7 May 2021 (Case No. 2020-40-01) on the compliance of the Law on the State Budget for 2020 with the Constitution, regarding funding for health-care workers’ remuneration under the Health Care Financing Law, the Court emphasised the constitutional link between annual budgets and medium-term budgetary frameworks, which serve the principle of sustainable fiscal governance. The Health Care Financing Law identified remuneration increases for health-care workers as a medium-term priority for 2019–2021. The Cabinet, however, retained discretion in balancing this priority against other fiscal obligations

and macroeconomic realities when preparing the 2020–2022 medium-term framework. The Constitutional Court concluded that both the Cabinet and the *Saeima* had complied with the Health Care Financing Law's intent, as the contested allocations were developed within the approved medium-term budget framework and reflected the state's financial capacity. Thus, the 2020 Budget Law did not breach Articles 1 and 66 of the Constitution. These decisions articulate a coherent doctrine regarding constitutional limits on budgetary legislation in Latvia. The Court reaffirmed that the executive branch must retain sufficient discretion to prepare a balanced and realistic state budget, guided by principles of economy and sustainability. The legislature cannot pre-determine binding expenditure obligations in substantive laws that undermine the annual budget process. Medium-term budget frameworks provide a constitutional mechanism to reconcile political priorities with fiscal discipline. The rule of law requires genuine, financially backed commitments in budgetary decisions; promises without fiscal feasibility would endanger democratic governance. In essence, the Court's jurisprudence delineates the constitutional equilibrium between parliamentary control and executive autonomy in fiscal matters, thereby strengthening the integrity, transparency, and sustainability of Latvia's public finance system.

Appropriation is the permit approved by the *Saeima* in the annual state budget law, allowing state budget institutions to use funds for specific positions and purposes. The annual budget law authorises appropriations in ministries' budget programmes for items such as "remuneration", "goods and services", "subsidies and grants", "fixed capital formation", "transfers" and others. The annual budget law itself is very detailed. Appendix 4 of the Law contains appropriations for revenue and expenditure for all ministries and other central state institutions, which comprise around 30 budget units. The expenditures are divided into about 500 budget programmes and sub-programmes. Each programme/sub-programme consists of budget line items (classification codes), which show expenditure at a detailed level. The line items themselves are divided into four different levels, with about 1,100 items at the lowest and most detailed levels. Within the execution of the budget law, even in economic classification, changes related to procedures and those resulting from external factors are made. Changes in subsidies and donations in 2023, for example, reflect the increase in European funds and other investments channelled to the commercial sector of the economy and various projects. Changes in social benefits in 2021 reflected subsidies to private individuals due to the impact of the COVID-19 pandemic. The aforementioned shows that a detailed line-item budgeting system is very burdensome for line ministries and the Minister of Finance, who approves changes in appropriations. The link between resources granted to the budget units and results can be lost without supplementary amendments to the annual budget law. When the 1997 budget was prepared, the first attempts were made to introduce the principle of flexibility in the allocation of funds within the framework of economic classification codes not approved by the budget law (for example, to

transfer various current expenditures among accounts, except for remuneration). This possibility still exists today and has been refined over the years. Different institutions (Finance Minister, Cabinet of Ministers, *Saeima*) are involved in deciding on changes in appropriations depending on the amount and significance of the allocations to be made. The legislator has delegated exclusive rights to the Minister for Finance regarding the final modification of appropriations for budget execution. As for previous years, there were 199 orders from the Minister of Finance regarding amendments to appropriations in 2019, 389 in 2020, 665 in 2021, 650 in 2022, 345 in 2023, and 400 in 2024. A significant impact on the number of amendments to the appropriation occurred during the COVID-19 pandemic.¹⁵ The plan is to delegate financial flexibility within the programme to sectoral ministers, starting in 2027, but the functioning of this flexibility remains a matter of debate. At a time when most public institutions plan their activities within the framework of investment utilisation without setting achievable outcomes, the reporting system is primarily focused on controlling the lawful use of investments. Greater freedom of action can be given to institutions only after greater accountability has been established. Increased flexibility in the allocation of financial resources to ministries was implemented in conjunction with a review of all ministries' expenditure by budget item. It could be recommended to improve the efficiency of in-year budget execution, by introducing a structured in-year reallocation (*virement*) regime, based on a supplementary budget towards the end of the year rather than the existing practice of bi-weekly reallocations. A process with greater flexibility should specifically regard the authority of the *Saeima* when approving the Budget. The system of *virement* applies when a line ministry or agency uses savings on one or more line items from within its overall budget allocation to meet an expenditure overrun on another line item during the course of the year. This system does not require specific parliamentary approval. In Latvia, the basis for *Saeima* approval should be changed from the existing line-item basis to a higher level of total expenditures. When selecting a higher level to vote on appropriations, Latvia should use the overall level of individual institutions (budget units) and the programme total level, where applicable, to maintain consistency with the recommendation to use indicators more selectively, encouraging a greater focus on performance. The higher level chosen would lead to greater flexibility and free up human resources for more analytical work. The application of savings on a line item to offset an excess in another would not be approved unless the Ministry of Finance is satisfied that the savings are actual and not merely the postponement of expenditure to

15 Ketners, K. Improvement of re-allocation tool for budget planning and execution for COVID-19 health care system financing in Latvia. International Virtual Academic Conference Education and Social Sciences. Business and Economics. 9 December 2020 ISBN 978-608-4881-16-2. <https://doi.org/10.13140/RG.2.2.18438.40008>.

a subsequent year. Additionally, funding excess spending on staffing and administrative costs, including salaries and allowances, is not permissible.

It can be concluded that the *Saeima* (Parliament) has a central role in exercising financial competence – the right and obligation to plan state revenues and expenditures and to determine state property obligations, as derived from the Constitution. Adopting the state budget is one of the core constitutional powers, ensuring the principle of separation of powers. The executive branch is responsible for implementing the decisions made by the *Saeima*, and the Government is constitutionally obliged to submit the draft state budget to Parliament. The *Satversme*, while not prescribing the structure, level of detail, or accounting method of the state budget (cash or accrual-based), requires the budget to be comprehensive (“covering all income and expenses”) and annual (“for each year”). A balance must be maintained between a sufficient level of detail – enabling parliamentary financial oversight – and the avoidance of excessive specificity, which could hinder budget execution. A key focus is budget flexibility, referring to the extent to which ministries and constitutional institutions may modify the state budget approved by the *Saeima*. The flexibility is constitutionally acceptable as long as it does not diminish the *Saeima*'s substantive budgetary authority and remains legally grounded. The proposed framework allows ministers and constitutional institutions to adjust the detailed economic breakdown of expenditures within their total allocated ceilings, while also requiring notification to the *Saeima* Finance Committee about such changes. This mechanism strengthens parliamentary oversight while maintaining the Government's necessary decision-making freedom.

Thus, it can be concluded that within the legal and institutional framework of the Latvian state budget, the Cabinet's dominant role in decision-making and restoring priority activities suggests that the budget formula is primarily focused on the annual budget. Within the annual budget law, a detailed economic classification and numerous detailed, legally binding line-item appropriations largely prevent the flexible use of resources. This exactness has led to growing dissatisfaction within public administration.

Conclusions and further developments

The budget in Latvia has been established based on programmes/sub-programmes since 1997. Principles for the establishment of budget programmes (sub-programmes) shall be applied by budget units (ministries and other central state institutions) when creating the structure of budget programmes (sub-programmes) intended for the State basic budget for the implementation of the basic functions of the state. For example, if the operational strategy of the institution has been approved for the ministry, the structure of the budget programmes shall be determined by the operational (action) directions defined in the operational strategy of the institution. In case of the ministry lacking an approved operational strategy for the institution, the structure of the budget programmes shall

be based on the functions specified for the ministry in other legal acts. Budgetary programmes must ensure the achievement of the objectives set out in the development programming documents, the planned results, and their performance indicators. Budget law explanations provide information regarding the State budget as an instrument for implementing policy; the budget unit shall indicate in the budget explanations the areas of activity under the responsibility of the unit in which a particular policy or activity direction is implemented. The current Latvian budget performance information framework is overly complex, determined, and not extensively utilised in budget negotiations and planning. Politics heavily influence the budget preparation process, leaving little room for the Ministry of Finance to conduct thorough technical analysis and significantly influence budget allocations. The medium-term perspective for budgeting is not binding at the programme and measure levels, which creates planning problems for both the Ministry of Finance and the line ministries (budget units). The focus of budgeting has prevailed on inputs and neglected performance results. Therefore, budget administration within the Ministry of Finance clearly has room to develop reform ideas to counter these problems. Budget planning reform should involve shifting from a conventional line-item budgeting system to one that emphasises the results and outcomes achieved through the use of public funds. Improvements can be achieved by enacting an organic budget law that clearly defines the roles and responsibilities of different actors in the budget process, ensures compliance between the policy programme and the medium-term budget financing framework (fiscal rules). To ensure increased autonomy for line ministries, the line minister shall approve the policy programme and control the allocation of resources in accordance with the planned goals. If several ministries contribute to the achievement of the programme objective, the line ministers shall approve the whole programme, or the programme shall be divided into sub-programmes to be approved by the ministers. The Ministry of Finance should be granted greater authority and autonomy to conduct technical analyses and provide recommendations on budget allocations.

Latvia has made significant progress in adopting international best practices for budgetary governance. However, areas still need improvement to address future fiscal challenges:

- Enhancing the budget planning process by linking policy documents to the medium-term budget framework to incentivise realistic budget planning.
- Addressing inefficient in-year budget execution and the inflexibility of the current system for budget reallocations. Changes can be achieved by introducing a virement regime and increasing the budget flexibility of the line ministry, which would reduce administrative complexity and the need for frequent re-allocations.
- Aligning budget request volumes with available fiscal space and setting limits on medium-term budgetary expenditure growth through policy strategies. Line ministers should also be held responsible for current budget appropriations to reduce incremental budget planning.

- Implementing necessary legislative amendments to support critical reforms in state budget planning processes in Latvia.

SUMMARY

Latvia's budget system has evolved from Soviet central planning to a transparent, EU-aligned framework based on the Law on Budget and Financial Management (1994) and the Fiscal Discipline Law (2013). The process follows principles of complexity, timeliness, annuality, and strategic coherence. Despite legal progress and clear division of powers between the *Saeima* and the Cabinet, budgeting remains overly detailed, rigid, and politically influenced. Reforms aim to link budgets to policy goals, strengthen medium-term planning, increase flexibility, and enhance performance-based management to ensure sustainable and efficient public finance. The research findings were also used to formulate proposals for amending current legislation regulating public finances. The author has proposed the following theses in relation to this matter:

1. Budget regulation was initially introduced in early 1990 with the "Law on Budgetary Rights in the Republic of Latvia" and continued with the adoption of the Latvian organic budget law – the "Law on Budget and Financial Management". All budgetary affairs are organised based on this law and in accordance with the *Satversme*. Between 2010 and 2013, the organic budget law was reformed to align with EU fiscal regulations.
2. In developing legal acts, Latvia has primarily drawn on the experience from the continental European framework. Laws regulating budget revenues, including revenue collection and administration, can be classified into general administration acts and specific legal acts concerning tax and non-tax revenues. Tax laws are based on those developed following the first tax reform in 1990, subsequent expert recommendations in 1995, and laws established in accordance with EU regulations.
3. Several future challenges in public finance law should be noted. In the area of budget law, these include the creation of a new and modern Budget Management Law that would facilitate financial management in line with OECD best practices for budget formulation. In the realm of budget planning, there is a need to strengthen parliamentary oversight while simultaneously ensuring the autonomy of budgetary resources and granting greater rights in appropriation planning to achieve specific objectives and performance indicators, thereby moving towards clear performance-based budget planning.

KOPSAVILKUMS

Rakstā tiek analizēta Latvijas publisko finanšu regulējuma attīstība, īpašu uzmanību pievēršot budžeta un nodokļu jomai. Raksta mērķis ir pamatot jēdzienu "budžeta princips" un identificēt mūsdienu budžeta principu galvenās iezīmes un attīstības tendences

Latvijā. Pētījumā aplūkoti budžeta sistēmas un procesa organizatoriskie un metodoloģiskie aspekti, nošķirot budžeta sistēmas principus, budžeta procesa principus, kā arī ieņēmumu un izdevumu veidošanas pārvaldības principus.

Rakstā izcelti jauni virzieni publisko finanšu regulējumā digitālajā kontekstā, tostarp ieņēmumu avotu dažādošana, budžeta efektivitātes paaugstināšana un pārskatāmības veicināšana. Pētījumā konstatēta augšupejoša tendence nacionālajā regulējumā sekmēt budžeta informācijas atklātību, kā arī ierosināti grozījumi spēkā esošajos publisko finanšu tiesību aktos.

Autors izvirza trīs galvenās tēzes: (1) budžeta regulējums Latvijā aizsākās ar 1990. gada likumu “Par Latvijas Republikas budžeta tiesībām” un turpināja attīstīties, pieņemot Likumu par budžetu un finanšu vadību, kas 2010.–2013. gadā tika reformēts atbilstoši Eiropas Savienības fiskālajiem noteikumiem; (2) tiesiskā attīstība balstās kontinentālās Eiropas modeļos un Eiropas Savienības standartos; (3) Satversmes tiesas praksei ir centrālā nozīme fiskālās pārvaldības un tās regulējuma modernizācijā.