Tax Card 2020

Effective from 1 January 2020

The Republic of Estonia

KPMG Baltics OÜ

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CORPORATE INCOME TAX

In Estonia, corporate income tax is not levied when profit is earned but when it is distributed. In 2020, the tax rate for regularly paid dividends is 14% (calculated as 14/86 of the net distribution) and the standard rate is 20% (calculated as 20/80 of the net distribution).

Under the regulation in force from 1 January 2018, a profit distribution that is smaller than, or equal to, the past three years' average profit distribution which has been taxed in Estonia will be subject to income tax of 14% (calculated as 14/86 of the net distribution). The Income Tax Act includes certain transitional provisions:

- In 2019, the amount of profit distributions smaller than, or equal to, 1/3 of the profits distributed in 2018 was subject to corporate income tax (CIT) calculated as 14/86 of the net distribution while the tax payable on the remaining amount (if anything) is calculated as 20/80 of the net distribution.
- In 2020, the amount of profit distributions smaller than, or equal to, 1/3 of the total amount of profits distributed in 2018 and 2019 is subject to CIT calculated as 14/86 of the net distribution while the tax payable on the remaining amount is calculated as 20/80 of the net distribution.

Companies which distribute profit and pay 14% CIT on it are additionally obliged to withhold income tax of 7% from dividends paid to resident and non-resident natural persons. Tax treaties may provide lower withholding tax rates.

Exceptions

Under certain conditions, redistribution of dividends is not subject to taxation. Income tax is not charged on the dividends received from a company domiciled in an EEA Member State or

Switzerland if at least 10% of the shares or votes in that company is held by an Estonian company. The exemption applies to dividends received from a company domiciled in another country if the Estonian company holds at least 10% of the shares or votes in the company, and income tax has been withheld or paid. Also, in some cases the exemption is applied to the dividends paid out of the profit attributed to a resident company's permanent establishment. However, the exemption does not apply if dividends are received from companies in low tax jurisdictions.

Fringe benefits and expenses not related to business

Fringe benefits are subject to income tax of 20% (calculated as 20/80 of the net amount at the employer's level) and social security tax of 33% (social security tax is levied on the amount which includes both income tax and non-deductible VAT). Excluding the exceptions expressly listed in the Estonian Income Tax Act, all benefits in kind provided to employees are taxed as fringe benefits. Share option programmes may be exempt from fringe benefit taxes under certain conditions.

Expenses and payments not related to the company's business are subject to income tax of 20% (calculated as 20/80 of relevant net amounts).

Gifts, donations and entertainment costs

A resident company has to pay income tax of 20% (calculated as 20/80 of the net amount) on gifts and donations made, with certain exceptions granted to non-profit organisations. Expenses incurred while entertaining guests and business partners, i.e. expenses incurred in respect of accommodation, catering, transport and cultural events, are also subject to tax if they exceed certain tax-exempt limits.

Transfer pricing

If the value of a transaction conducted between associated persons (including transactions carried out between the head office and its permanent establishment) differs from market conditions, the difference is subject to income tax. Qualifying companies must document their transactions with associated parties to prove that the prices used are at arm's length.

Other distributions

Payments made by a resident company upon reduction of share capital or contributions, or upon redemption or return of shares or contributions, are subject to income tax at the level of the company who makes the payment. Income tax is paid only on the amount which exceeds the actual contribution made to acquire a holding. These deposits must be declared. Similarly, the portion of liquidation proceeds that exceeds the initial monetary or non-monetary contributions is subject to corporate income tax of 20% (calculated as 20/80 of the net amount).

Exit tax

Income tax is levied on the amount that is equal to the difference between the market value and carrying amount of the assets to be taken out at the time of exit of the assets from Estonia if a resident company or a non-resident company (through its permanent establishment in Estonia) takes assets to a permanent establishment in another Member State of the European Union or in a third country.

Controlled Foreign Companies

In general, if Estonian entity has at least a 50 percent holding in a controlled foreign company (CFC), or has a foreign branch, which does not carry on actual business activities, the Estonian CFC taxation rules must be applied. The portion of profits of a CFC attributable to ostensible transactions (the main purpose of which was to obtain a tax advantage) must be attributed to the resident company and taxed as profits. An exception might apply if certain thresholds in terms of the amounts of annual profit and financial income earned by the controlled foreign company is not exceeded.

Loss carried forward

Losses incurred by a company do not affect corporate taxation.

Thin capitalisation

Income tax is levied on the residual borrowing costs of a resident company, other than a financial undertaking, in excess of 3,000,000 euros and 30% of the interest, tax and profit before depreciation of a resident company, in the portion exceeding the losses of the resident company, unless:

- a resident company is not part of a consolidated group for the purposes of financial reporting and has no affiliated company or permanent establishment, or
- the loan is used to finance long-term infrastructure projects of public sector involving both the project promoter, borrowing costs, assets and income in the European Union, or
- a resident company that is a member of a consolidated group for financial reporting purposes shall choose that its excess borrowing cost is not taxed (has to comply with certain conditions)

Withholding tax on payments to non-residents

In Estonia, withholding tax is imposed on the following payments made to non-residents:

• interest	0%, 20%*
• royalties	0%, 10%**
• fees for services provided in Estonia	10%
• rental payments	20%
• dividends (if subject to CIT calculated as 14/86 of the net dividend)	7%***

* 20% rate applies to interest exceeding the market interest rate.
** In certain cases, outbound royalty payments are exempt from withholding tax provided that the recipient is an associated company of the paying company and is a resident in another EU Member State or Switzerland, or such a company's permanent establishment situated in another Member State or Switzerland.
*** Withholding obligation applies when dividends are paid to natural persons.

Withholding tax rates may be subject to reduction under Double Taxation Treaties (see the list below).

Withholding tax is paid on making the payment.

PERSONAL INCOME TAX

In Estonia, a flat rate of 20% is imposed on personal income.

Taxable income

Natural persons are subject to general income tax of 20% on income derived from

- employment (monetary payments);
- business (self-employed income);
- property/investment (rental income, royalties, interest, capital gains on disposal of business, movable and immovable property);
- other sources (certain pensions, scholarships, grants, awards, lottery prizes, insurance indemnities and payments from pension funds).

In certain cases, the income tax rate is 10%.
Fringe benefits are taxed at the employer's level.

Deductions from income

Under Estonian law, certain amounts may be deducted from personal income such as:

- basic exemption EUR 0 – 6,000 per year (see the table below);
- one resident parent who maintains two or more minor children, may deduct increased basic exemption from his/her income for a child of up to 17 years of age, starting from the second child. The amount of the increased basic exemption is

1,848 euros for the second child and 3,048 euros starting from the third child.

- additional deductions for housing loan interest, training expenses, gifts, donations, insurance premiums, acquisition of pension fund units, etc.

The total amount of additional deductions allowed is limited to EUR 1,200 (incl. EUR 300 in respect of housing loan interest); however, the amount deducted cannot exceed 50% of the taxpayer's taxable income during the period of taxation (i.e. a calendar year). In addition, amounts paid to acquire units of supplementary pension fund or as insurance premiums under an insurance contract for a supplementary funded pension can be deducted. However, the deductions are limited to 15 % of the taxpayer's annual taxable income, but not more than EUR 6,000. Natural persons have to submit the personal income tax return annually by 30 April following the year of taxation.

From January 2018, the amount of basic exemption deductible from the income of a resident natural person depends on his/her income:

Annual gross income (EUR)	**Basic exemption**
Up to 14,400	EUR 6,000 (maximum)
Between 14,400 and 25,200	Proportional reduction of basic exemption, determined using a specific formula
EUR 25,200	No entitlement to basic exemption

Social security

An employer must pay mandatory social security contributions on gross employment income. No ceiling has been set on social security contributions. The minimum social security obligation per employee per month is EUR 178,2.

For employees working in Estonia, social security and unemployment insurance contribution rates are as follows:

- the rate charged to employers: 33.8% (33% + 0.8%);
- the rate charged to employees: 1.6%.

Funded pension contributions of 2% are withheld on gross salary payments to residents if the employee has joined the funded pension system. The latter is obligatory to an Estonian tax resident born in 1983 or later.

VAT

The standard VAT rate is 20% and the reduced rate is 9%.

The following supplies are subject to VAT of 9%:

- books and certain periodicals;
- certain medicines and medical devices;
- accommodation services.

The following transactions are subject to zero-rate (0%) VAT:

- export of goods and intra-Community supplies;
- cross-border business-to-business services;
- goods placed in free zones or free warehouses;
- certain goods listed in Annex V of Council Directive 2006/112/EC that are placed in a VAT warehouse;
- export and import-related transport services, international passenger services;
- supply of aircraft used by an air carrier operating mostly on international routes;
- supply of sea-going vessels for navigation on high seas;

- provision of services on board vessels or aircraft during international transport;
- supplies of goods under diplomatic and consular arrangements;
- supplies of goods and services to institutions of the EU and NATO forces.

The following transactions are exempt from VAT:

- transactions involving securities and financial services (with an option to tax domestically);
- insurance transactions;
- transactions involving immovable property or parts thereof (with an option to tax);
- rental transactions involving immovable property or parts thereof (with an option to tax);
- universal postal services;
- lotteries and gambling;
- certain education services;
- transactions involving health and welfare.

Special arrangements

- the domestic reverse charge applies to voluntarily taxed immovable property, scrap metal, precious metal and some metal products;
- postponed import VAT payment mechanism;
- VAT grouping.

REAL ESTATE TAX AND LAND TAX

The only property tax imposed in Estonia is the land tax. As a rule, the annual tax rate is between 0.1% and 2.5% of the taxable value of the land. The owner (or, in certain cases, the user) of the land has to pay the tax. However, the land under a taxpayer's home is exempt from tax.

TAX TREATIES

As of 1 January 2020, Estonia has concluded Double Taxation Treaties with the following countries and jurisdictions:

Albania
Armenia
Azerbaijan
Austria
Bahrain
Belarus
Belgium
Bulgaria
Canada
The Czech Republic
China
Croatia
Cyprus
Denmark
Finland
France
Georgia
Germany
Greece
Hungary
Hongkong
Iceland
India
Ireland
The Isle of Man
Israel
Italy
Japan
Jersey
Kazakhstan
Kyrgyzstan
The Republic of Korea
Latvia
Lithuania
Luxembourg
Macedonia
Malta
Moldova
The Netherlands
Norway
Poland
Portugal
Romania
Serbia
Singapore
Slovakia
Slovenia
Spain
Sweden
Switzerland
Thailand
Turkey
Turkmenistan
Ukraine
The United Arab Emirates
The United Kingdom
The United Mexican States
The United States of America
Uzbekistan
Vietnam

INVESTMENT INCENTIVES

Only one investment incentive is available under the Estonian tax system – no tax is levied on retained or reinvested profits. However, profit distributions are subject to taxation.

REAL ESTATE TRANSFER DUTY

The duty is paid by the acquirer of immovable property. The rate of the duty depends on the purchase price of the property. However, if the purchase price cannot be established, the rate depends on the taxable value of the land plus the value of the building (in the case of improved immovable property).

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