Tax obligations of employment income 2008

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General Obligations

There are four tax laws, which regulate directly the obligatory withholdings and payments of taxes in relation to payments made by employers to employees (resident natural persons) for salaried work performed by the latter. These laws are:

- the income tax act,
- the social tax act,
- the act on unemployment insurance,
- the funded pensions act.

Income tax, unemployment insurance premiums (and funded pension payments for resident employees) have to be withheld and social tax and unemployment insurance premiums paid on all payments made to the employee and declared (on Form TSD) and transferred to the Tax and Customs Board (Income accounts) by the 10th of every month, following the month of payment (i.e. on payments made in January tax should be withheld and transferred and declared to the Tax and Customs Board by February 10) by employer. This deadline encompasses all withholding taxes and payments made to employees.
All of the abovementioned taxes and payments are personified.
Taxes paid or withheld from payments made to
o resident employee shall be declared on annex 1 of form TSD;
o non-resident employee shall be declared on annex 2 of form TSD.
A non-resident operating as employer in Estonia has to pay income and social tax on fringe benefits granted to resident and non-resident natural person.
The taxable income of a natural person does not include fringe benefits.

Fringe benefits have to be declared on annex 4 of form TSD to the Tax and Customs Board by the 10th of every month, following the month of granting fringe benefits by non-resident operating as employer in Estonia.
A non-resident operating in Estonia as an employer has same obligations even if the non-resident employer does not have a permanent establishment in Estonia.

A non-resident operating in Estonia as an employer

In order to declare and transfer taxes on payments made to employees to the Tax and Customs Board, a non-resident operating in Estonia as an employer has to register in the register of taxable persons.

Registration

For registration a non-resident operating in Estonia as an employer has to contact or go to:
Division of International Taxation,
Tax Department,
Northern Regional Tax and Customs Centre,
Estonian Tax and Customs Board,
Endla Street 8, 15177 Tallinn,
phone (+372) 676 1200, (+372) 676 1111
e-mail pohja@emta.ee
In order to be registered, an application setting out the following shall be submitted:
o the name of the non-resident employer;
o the postal address of the employer in the home country, if any;
o the postal address of the employer in Estonia, if any;
o the name and postal address of the person representing the employer;
o the signature of the employer or a person authorised by the employer.
The following documents shall be attached to the application:
o a copy of the articles of association or another document regulating the activities of the non-resident employer if available;
o a document certifying the authorisation of the person representing the employer;
o a specimen signature of the person which is notarised or officially certified by a tax authority;
o in case of tax representative, a written agreement between non-resident and his tax representative

Taxes to be paid and withheld by an employer

1. Income Tax

The income tax is withheld monthly by the employer at a rate of 21% of the gross salary of the employee. Certain subtractions can be made from the tax base of the income tax of resident taxpayers.
These are (the list is final):

- on a basis of employees written application, 1/12 of the annual basic exemption (27 000 EEK in 2008) - only one employer simultaneously

- alimony paid to the receiver of alimony on the basis of court's ruling or notarized agreement

• withheld unemployment insurance premiums

• withheld funded pension payment.

2. Social tax

The social tax is paid at a rate of 33% on all payments made to employees for salaried work performed. Employers pay the social tax in full. There is always a minimum obligation on social tax to be paid, which is equal to 33% of the minimum envisaged by the budget act annually. In 2008, it is 2700 EEK per month, i.e. a minimum social tax obligation of 891 EEK has to be paid monthly (even if there were no payments for salaried work) for each employee who is entitled to 1/12 of the basic exemption with this particular employer.

3. Unemployment insurance premium

An unemployment insurance premium is withheld at a rate of 0,6% of the gross salary of the employee. Pensioners are not entitled to unemployment status benefits and therefore they do not pay the unemployment insurance premium. In addition to this, employers pay the unemployment insurance premium at a rate of 0.3% of the sum of gross salaries monthly.

4. Funded pension payment

A funded pension payment is withheld at a rate of 2% for the persons under the obligation, which is envisaged by the funded pensions act. Once having joined the obligatory funded pension system, one cannot disjoin it. Also, everyone who was born after 1 January 1983 is automatically a person under obligation. In addition to the 2% withheld, the state adds 4% of the gross salary of a person under obligation at the expense of the social tax paid for that person.
Social security contributions (social tax, unemployment insurance premium and funded pension payment) will not be paid or withheld in Estonia, if the employee has a ceritificate of a posted employee (E101) issued by the authorities of an EU country, or a country with which Estonia has a social security agreement (Canada, Ukraina, Russia).

Examples of tax calculations

1. In case an employee is a non-resident

• A gross payment of 20 000 EEK is agreed upon

• An income tax of 4 200 EEK is withheld, calculated as 21% x 20 000 = 4 200

• The amount of social tax of 6600 EEK (33%) is to be paid by employer

• An unemployment insurance premium of 60 EEK is to be paid by the employer (0.3%)

• A total cost to employer is 26 660 EEK

- An unemployment insurance premium of 120 EEK is withheld (0,6%)

- A total net result received by the employee is 15 680 EEK, calculated as 20 000 – 4200 – 120 = 15 680.

2. In case an employee is a resident

- A gross payment of 20 000 EEK is agreed upon

- An unemployment insurance premium of 120 EEK is withheld (0,6%)

- A funded pension payment of 400 EEK is withheld (2%)

- An income tax of 3 618 EEK is withheld, calculated as 21% x (20 000 – 120 – 400 – 2250) = 3 618 EEK. 2250 EEK is 1/12 of the annual basic exemption 27 000 EEK

- The amount of social tax of 6600 EEK (33%) is to be paid by employer

- An unemployment insurance premium of 60 EEK is to be paid by the employer (0.3%)

- A total cost to employer is 26 660 EEK

- A total net result received by the employee is 15 862 EEK, calculated as 20 000 – 120 – 400 –3 618 = 15 862.

Obligations of employee – non-resident and resident

1. Concept of Residency

A person shall be deemed to be a resident as of the date of his or her arrival in Estonia. Thus, it is
possible, that a person shall be deemed to be resident for one part of the period of taxation and non-resident for the other part of the period of taxation.
A natural person is a resident if one of the following conditions is met:
o his or her place of residence is in Estonia;
o he or she stays in Estonia for at least 183 days over the course of a period of 12 consecutive calendar months. A person shall be deemed to be a resident as of the date of his or her arrival in Estonia;
o Estonian state public servants who are in foreign service are also Estonian residents.
If the residency prescribed on the basis of an international agreement ratified by the Riigikogu (the Estonian Parliament) differs from the residency prescribed pursuant to the Estonian Income Tax Act, the provisions of the international agreement apply.

Thus, where by reason of the provisions of agreement between two countries that have concluded a tax treaty, a person is a resident of both contracting states, his status shall be determined according to the tax treaty.
Thus, if a natural person is deemed to be a tax resident in foreign country in the sense of the tax treaty, she or he will be considered to be a non-resident according to the Estonian Income Tax Act.

2. Non-resident

Non-residents (natural and legal persons) have a limited tax liability in Estonia, only the Estonian-source income is taxed.

According to the Estonian Income Tax Act, income tax is charged on income derived by a non-resident natural person:

- from work under an employment contract or
- in public service or
- from activities engaged in on the basis of a contract for services, an authorisation agreement or a contract entered into for the provision of any other services under the law of obligations

if the non-resident performed his or her duties or provided the services in Estonia and at least one of the following conditions is fulfilled:

- the payment was made by:
    - an Estonian state or local government authority or
    - Estonian resident or
    - a non-resident operating in Estonia as an employer, or
- if the payment was made through the permanent establishment of a non-resident legal person registered in Estonia, or
- if the person has stayed in Estonia for the purpose of employment for at least 183 days over the course of a period of 12 consecutive calendar months.

If the tax treaty prescribes more favourable conditions for taxation of the income of non-residents than those provided by the Estonian legislation, the provisions of the tax treaty apply. According to the article 15 (2) of the tax treaty, remuneration derived by a resident of

a contracting state in respect of an employment exercised in the other contracting state shall be taxable only in the first-mentioned state if:
a) the recipient is present in the other state for a period or periods not exceeding in the aggregate 183 days in any twelve-month period commencing or ending in the taxable year concerned, and
b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other state, and
c) the remuneration is not borne by a permanent establishment or a fixed base which the employer has in the other state.

Obligations

In general, the withholding taxes are final taxes for non-residents, and the non-resident recipient has no obligation to file an income tax return for income so taxed. If no tax has been withheld, form A1 has to be submitted by non-resident employee. The forms of tax returns for non-residents can be found on web-site of the Estonian Tax and Customs Board (http://www.emta.ee/?id=1313) .
When the Estonian Tax and Customs Board has received your tax return, you can obtain the reference number at https://maksuamet.ma.ee/e-service/doc/a0004.xsql_necessary for the payment, if you contact the Division of International Taxation, Tax Department, the Northern Regional Tax and Customs Centre.

3. Resident

Residents have unlimited tax liability in Estonia, the foreign income is included to their taxable income.
A resident natural person is required to submit an income tax return to the regional tax centre of the Tax and Customs Board concerning the income of a period of taxation not later than by 31 March of the year following the period of taxation.
The regional tax centre of the Tax and Customs Board shall calculate any additional amount of tax due and issue a written tax notice to this effect to the taxpayer.

This guideline is to be considered as informative and should not be treated as final. In specific cases one must act according to law. In case of questions, you are welcome to turn to tax administrator.