

# Expenses related to business

## WHAT ARE EXPENSES RELATED TO BUSINESS?

Expenses are related to business if they have been incurred for the purposes of deriving income from taxable business or are necessary or appropriate for maintaining or developing such business and the relationship of the expenses with business is clearly justified, or if the expenses have been made for ensuring the occupational health and safety to the employees (in accordance with **subsection 13(1) of the Occupational Health and Safety Act**).

In order to consider the expenses as expenses related to business, these must be:

- ✓ made by taxpayers themselves;
- ✓ made during the period of taxation when the expenses are deducted from the business income;
- ✓ certified;
- ✓ related to the business activity of the taxpayer, not to the business activity of anybody else.

## EXPENSES RELATED TO BUSINESS ARE:

- ✓ acquisition of fixed assets for business activity (including any commissions and fees paid); fixed assets are assets that a sole proprietor uses in production or provision of services for a longer period than one year (for example, land, buildings or civil engineering works, machinery, equipment, animals, patents, licences, etc.);
- ✓ costs for renovation and supplementation of fixed assets;
- ✓ property which is not fixed assets;
- ✓ goods acquired (including materials, raw material, fuel, energy, semi-finished products);
- ✓ services acquired (including rental charge paid for facilities used in business);
- ✓ wages, salaries or other remuneration that sole proprietors pay to their employees;
- ✓ social tax on payments made by sole proprietors to their own employees and unemployment insurance premiums of employers;

- ✓ fringe benefits granted by sole proprietors to their own employees, after payment of income tax and social tax thereon;
- ✓ social tax paid for the sole proprietor's spouse participating in the sole proprietor's business activities;
- ✓ other state taxes related to business (land tax, value added tax, customs duty, heavy goods vehicle tax, road toll) and local taxes (taxes established by local governments within their administrative territories, for example, sales tax, advertisement tax, entertainment tax, etc.);
- ✓ financial costs, interests paid on loans related to business or on other debt obligations (except interests paid on the basis of the Taxation Act);
- ✓ interest calculated and paid on the tax arrears to be paid in instalments pursuant to the Taxation Act after approval of the payment schedule (except interest calculated on the tax liability imposed by a notice of assessment);
- ✓ in-service training and re-training costs paid by the sole proprietor for himself/herself or for the employees, if the existing professional, vocational or occupational knowledge was broadened or new skills needed in the business activities were acquired;

**Example:** A sole proprietor participated in a training course on changes in the Accounting Act and acts concerning taxes and paid for the training himself. Whereas the sole proprietor keeps his accounting himself, he enters the amount paid for the training into the business expenses.

- ✓ insurance premiums for the property used in the business activity;
- ✓ costs related to the transfer of the property used in the business activity;
- ✓ fees paid for licences, trading permits or activity licences, etc. used in business activity;
- ✓ social tax paid in a foreign state, if the sole proprietor has submitted a certificate from the tax administration of the foreign state to the Tax and Customs Board (Form A1/E101) indicating that he/she has the social insurance in the foreign state and the Estonian Social Tax Act is not applied for taxation by the social tax.

On **Form E**, sole proprietors indicate the expenses related to business together with the value added tax paid.

## WHICH EXPENSES ARE NOT RELATED TO BUSINESS?

**The expenses that are not considered business expenses and thus not deductible from business income are listed in the Income Tax Act in § 34.** Such expenses are:

- ✓ income tax paid on business income (including advance payments of income tax);
- ✓ fines and penalty payments imposed on the basis of law and paid during the period of taxation, and interests paid on the basis of the Taxation Act;

### **Example**

A sole proprietor who provides transport services was fined for over speeding. This fine cannot be entered in the expenses related to the sole proprietor's business.

- ✓ the cost of property seized from the taxpayer;

### **Example**

A sole proprietor sells at the market besides his own goods also cigarettes brought illegally into Estonia, for which he has paid to the mediator. The police confiscate the cigarettes. It is not allowed for the sole proprietor to enter the amount paid for the cigarettes in the expenses related to business.

- ✓ environmental charges at a higher rate paid pursuant to the Environmental Charges Act and for the breach of the requirements provided by this Act or for the pollution of the environment, and the compensation for damage caused to the third person;
- ✓ expenses incurred on account of benefits not subject to income tax pursuant to the Income Tax Act;
- ✓ any loss from the transfer, at a price lower than the market price, of property to a person associated with the taxpayer, unless income tax on fringe benefits has been paid on such loss;
- ✓ any loss from the transfer, at a price higher than the market price, of property purchased from a person associated with the taxpayer;
- ✓ gratuities and bribes;
- ✓ social security taxes and contributions paid in Estonia or in a foreign country, if the objective of payment was to guarantee pension, health, maternity, unemployment, accident at work or occupational disease insurance to the person, if the Estonian Social Tax Act is applied upon taxation of business income by social tax. ;
- ✓ contributions to a mandatory funded pension;
- ✓ the amount paid for services to a natural person, which is taxed on the basis of the Simplified

- ✓ Business Income Taxation Act, i.e. through a business account;
  
- ✓ expenses incurred for receiving business income exempt from income tax (the income earned through a permanent establishment located in a foreign country and taxed in the foreign country) (the income declared in Table 1 on Form E and 'exemption method' chosen);
  
- ✓ calculated sickness benefit indicated in the Social Tax Act which is exempt from social tax.