REPUBLIC OF ESTONIA
TAX AND CUSTOMS BOARD

Fringe benefits

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About fringe benefits

Fringe benefits, according to subsection 4 of § 48 of the Income Tax Act, are any goods, services, remuneration in kind or monetarily appraisable benefits which are given to a person specified in subsection 3 of § 48 of the Income Tax Act in connection with an employment or service relationship, membership in the management or controlling body of a legal person, or a long-term contractual relationship, regardless of the time at which the fringe benefit is granted. This means that fringe benefits may not always be linked to valid contracts. In summary, a fringe benefit is a part of salary or wages that is usually paid in a non-monetary form. As an exception, individual cash payments are also treated as a fringe benefit, and these cases are precisely specified in the Income Tax Act.

Section 48 of the Income Tax Act provides a sample list of fringe benefits, which is not final. Therefore, if the benefit provided by the employer meets the conditions of a fringe benefit, it is subject to taxation as a fringe benefit, even though the specific benefit is not listed by name in § 48 of the Income Tax Act.

Example 1
The employee is retired, but the former employer remembers him on his jubilee and gives him a gift. It is still considered a fringe benefit because the employer gives a gift because it was a former employee.

A benefit can be treated as a fringe benefit if the following conditions are met, i.e., it is a benefit granted by the employer to the employee due to an employment relationship and it is financially assessable for the employee.

If the benefit provided to the employee is treated as a fringe benefit, then it does not matter whether the employer has incurred expenses for the benefit provided.

Section 65 of the Act on the General Part of the Civil Code provides for the value of a property object, which is the usual value of such an object, unless otherwise prescribed by law or transaction. The usual value of an object is its average local selling price (market price).

Example 2
The employer receives free concert tickets from their contract partner and gives them to their employees. The foregoing is regarded as a fringe benefit, the taxable value of which is the market price of such concert tickets. Therefore, the price of the fringe benefit is usually determined on the basis of the market price of the goods or services granted as fringe benefit.

The services and goods purchased by employers for employees from both sole proprietors and users of the business account are considered as fringe benefit.

Example 3
The employer orders food for their employees via an app and also pays for the courier service.

Regardless of the fact that the courier is a business account user or a sole proprietor (FIE), tax liability arises on the fringe benefit, i.e., the costs of food and courier services.

Fringe benefits do not include cash payments normally considered to be wages or salaries, additional payments or similar payments on which income tax has to be withheld or which are not subject to income tax.

Last updated on 08.01.2025

Employer

According to subsection 2 of § 48 of the Income Tax Act, an employer is:

- a resident legal person
- a resident natural person
- a state or local government authority
- a non-resident who has a permanent establishment in Estonia (§ 7) or whose employees work in Estonia.

A RESIDENT LEGAL PERSON

A legal person is a resident in Estonia, according to subsection 2 of § 6 of the Income Tax Act, if it is established pursuant to Estonian law. European public limited companies (Societas Europaea, SE) and European associations (Societas Cooperativa Europaea, SCE) whose registered office is registered in Estonia are also residents.

According to § 24 of the Act on the General Part of the Civil Code, a legal person is either a private legal person or a public legal person. According to subsection 1 of § 25 of the Act on the General Part of the Civil Code, a private legal person is a legal person founded in private interests on a basis provided by the law concerning that type of legal person. A private legal person is a **general partnership, limited partnership, private limited company, public limited company, commercial association, foundation and non-profit association.**

According to subsection 2 of § 25 of the Act on the General Part of the Civil Code, a public legal person is the State, the municipality or any other legal person founded in the public interest under the law concerning the legal person in question.

A RESIDENT NATURAL PERSON

According to subsection 1 of § 6 of the Income Tax Act, a natural person is a resident if his or her place of residence is in Estonia or if he or she stays in Estonia for at least 183 days over the course of a period of 12 consecutive calendar months. A person is deemed to be a resident as of the date of his or her arrival in Estonia. Estonian diplomats who are in foreign service are also residents. A resident natural person is a taxable person on the basis of § 48 of the Income Tax Act if he or she acts as an employer (subsection 2 of § 2 of the Income Tax Act).

If the residency of a legal or natural person determined on the basis of an international agreement differs from the residency determined on the basis of law or if the international agreement prescribes more favourable conditions for taxation of income than provided by law, the international agreement will apply.

A STATE OR LOCAL GOVERNMENT AUTHORITY

According to § 38 of the Government of the Republic Act, the authorities of executive power are governmental authorities and state authorities administered by governmental authorities. Governmental authorities are ministries, the Estonian Defence Forces and the Government Office as well as executive agencies and inspectorates and their local authorities with authority to exercise executive power. Other governmental authorities may also be prescribed by law.

State authorities administered by governmental authorities are formed, reorganised and their activities are terminated pursuant to law.

Governmental authorities and state authorities administered by governmental authorities are registered in the state register of state and local governmental authorities.

Local government authorities are authorities and institutions administered by authorities.

A NON-RESIDENT WHO HAS A PERMANENT ESTABLISHMENT IN ESTONIA OR WHOSE EMPLOYEES WORK IN ESTONIA

The creation of a permanent establishment of a non-resident in Estonia is regulated by § 7 of the Income Tax Act. If an international agreement provides for more favourable conditions for the taxpayer with regard to the creation of a permanent establishment, the international agreement will apply.

If a non-resident has a permanent establishment in Estonia, fringe benefits granted to employees of the non-resident (regardless of the residence of the employees) will be taxed at the expense of the permanent establishment. Where an international agreement provides for more favourable conditions for the taxation of fringe benefits, the international agreement will apply. The benefits granted by a non-resident to its employees in Estonia are also subject to taxation as a fringe benefit.

Last updated on 08.01.2025

Employee

Employee as a beneficiary of a fringe benefit is a broader term than only within the meaning of the Employment Contracts Act. From the perspective of the fringe benefit, it is not important which law regulates employment relationships. According to subsection 3 of § 48 of the Income Tax Act, an employee is:

- ✓ a person employed under an employment contract
- ✓ an official (subsection 1 of § 13)
- ✓ a member of the management or controlling body (§ 9)
- ✓ a natural person who sells goods to an employer during a period longer than six months
- ✓ a natural person who works or provides services on the basis of a contract for services, authorisation agreement or any other contract under the law of obligations

Pursuant to subsection 6 of § 48 of the Income Tax Act, benefits which an employer grants to the spouse, cohabitee or direct blood or collateral relative of the mentioned person or which are granted by a person that belongs to the same group as the employer are also taxed as fringe benefit.

A PERSON EMPLOYED UNDER AN EMPLOYMENT CONTRACT

All persons who have entered into an employment contract with an employer will be deemed to be persons employed on the basis of an employment contract.

The workload the person employed, whether the employment contract has been suspended at the moment of granting the fringe benefit, whether the benefits are prescribed in the employment contract or collective agreement, etc., do not matter at the taxation of fringe benefits granted to a person employed on the basis of an employment contract.

AN OFFICIAL

According to the Civil Service Act, an official is a person who is in the public-law service and trust relationship with the state or local government.

The persons specified in subsection 3 of § 2 of the Civil Service Act (members of the Riigikogu, members the European Parliament, the President of the Republic, members of the Government of the Republic, judges, the Chancellor of Justice, the Auditor General, the Public Conciliator, members of local government councils, members of rural municipalities or city governments, elders of rural municipalities or city districts) are treated as officials for the purposes of the Income Tax Act (subsection 1 of § 13).

A MEMBER OF THE MANAGEMENT OR CONTROLLING BODY

Pursuant to § 9 of the Income Tax Act, a management or controlling body of a legal person is any authorised body or person who, pursuant to an Act governing the legal person, a partnership agreement, the articles of association or any other legislation regulating the activities of the legal person, has the right to participate in managing the activities of the legal person or in controlling the activities of the management body of the legal person.

Management or controlling bodies include management boards, supervisory boards, partners authorised to represent general or limited partnerships, procurators, founders until registration of the legal person, liquidators, trustees in bankruptcy, auditors, controllers and revision committees, etc. Directors of branches of foreign companies and managers of other permanent establishments of non-residents are also deemed to be management bodies (§ 9 of the Income Tax Act).

A NATURAL PERSON WHO SELLS GOODS TO AN EMPLOYER DURING A PERIOD LONGER THAN SIX MONTHS

Upon the sale of goods to an employer, a natural person is deemed to be an employee for the purposes of § 48 of the Income Tax Act if the goods are sold for a longer period than 6 months. The time criterion will be assessed on the basis of the length of the period during which the goods are sold. If the sale of goods is agreed for a period of more than 6 months, the natural person will be deemed to be an employee as of the beginning of such an agreement (regardless of the frequency of the sale of individual goods). The fringe benefit must therefore be granted to a person with whom the grantor of the fringe benefit has or has had an business relationship.

A NATURAL PERSON WHO WORKS OR PROVIDES SERVICES ON THE BASIS OF A CONTRACT FOR SERVICES, AUTHORISATION AGREEMENT OR ANY OTHER CONTRACT UNDER THE LAW OF OBLIGATIONS

A person providing services to an employer on the basis of a contract under the law of obligations is deemed to be an employee for the purposes of § 48 of the Income Tax Act regardless of the duration of the provision of such services.

In granting benefits to the mentioned natural persons, after the end of the supply of the services or goods provided by them, it is necessary to assess, in the case of those persons, whether or not the benefit was granted as a result of the contractual relationship.

The benefits granted or given by the employer to the spouse, registered cohabitee, cohabitee or direct blood or collateral relative of the employee are also taxed as a fringe benefit.

A cohabitee is an unspecified legal term and, as beneficiaries of fringe benefits, a cohabitee is granted the same meaning as a spouse and registered cohabitee, assuming a common economic interest regardless of the formal connection. Direct blood and collateral relatives are terms arising from the Family Law Act.

Direct blood relatives are parents and children (also grandparents, grandchildren) and collateral blood relatives are sisters, brothers, aunts, uncles.

Last updated on 08.01.2025

A person that belongs to the same group as the employer

A FRINGE BENEFIT GRANTED BY A PERSON THAT BELONGS TO THE SAME GROUP AS THE EMPLOYER

A benefit granted by a person belonging to the same group as the employer is considered a fringe benefit granted by the employer.

According to the Commercial Code, a parent company together with subsidiaries is considered to be a group. Thus, in the case of a group, it is necessary to distinguish between the employees of companies belonging to the group where the payer of taxes on fringe benefits is not the formal grantor but the company employing the person receiving the benefit.

We point out that branches are not groups. A branch is provided for in § 384 of the Commercial Code and the provisions of § 53 of the Income Tax Act apply to taxation.

An employee must notify the employer of the receipt of a fringe benefit from a person belonging to the same group as his or her employer. How the employee informs the employer of the benefit received from another company belonging to the group must be regulated by the employer itself, no such procedure has been established in the Income Tax Act. As a rule, companies belonging to a group communicate with each other and report within the group the benefits granted to employees of another company and the amount thereof.

In the case of a group, it is important to distinguish between three different cases when taxing fringe benefits.

a. The entire group is located in Estonia

For example, an Estonian parent company organises an information day within the group and bears the entire cost of the event. Catering is organised for the event.

The materials distributed on the information day (including pens) are not financially valuable benefits to the employee – they are necessary for work.

However, for the catering of employees (fringe benefit), taxes are paid by each employer itself, despite the fact that the parent company incurred the full cost. Thus, the parent company pays taxes on the fringe benefit granted to its employees and the subsidiary pays taxes on the fringe benefit granted to its employees and incurred by the parent company.

There are two main ways to find out the amount of the fringe benefit:

- ✓ the parent company submits an invoice to the subsidiary by reselling or making a claim for reimbursement of the costs of catering to its employee. In this case, the subsidiary has incurred both the costs and the taxes paid on it
- ✓ the parent does not invoice but notifies the subsidiary of the amount to be treated as a fringe benefit. How the information process takes place is decided by the group companies themselves. A subsidiary pays taxes on its employees' fringe benefits, even though it has not actually incurred the cost. The cost to the parent company will be treated as linked to its business and no double tax liability will arise.

b. An employee of a company belonging to a group located in Estonia receives a fringe benefit from a company belonging to the group and located in a foreign state

For example, an Estonian subsidiary sends its employee abroad to the parent company. The employee attends a reception, meeting, or other event where, among other things, there is catering, cultural service. Taxation in a foreign state is carried out pursuant to the laws of that state and if the expenses incurred by the parent company are subject to taxation in the foreign state (i.e., are included in taxable income, despite the fact that the specific expenses may be exempt to a certain extent), the Estonian subsidiary does not incur double tax obligations on such expenses. An Estonian subsidiary will incur tax on the special benefit granted to its employee only if the benefit is not included in the taxable income of the parent company in the foreign state (e.g., it would be taxable at the level of a natural person).

c. An employee of a foreign company belonging to a group who has come to Estonia receives a benefit from a company located in Estonia and belonging to the group

Section 48 of the Income Tax Act regulates the benefits granted by Estonian employers to their employees, which are treated as fringe benefits. Although it is a person belonging to the same group, the company belonging to the group is located in a foreign state and § 48 does not regulate the taxation of employees of companies belonging to a group and located in a foreign state in Estonia as a fringe benefit. According to Estonian law, this employee is treated as a guest and taxation is carried out in accordance with the provisions of § 49 of the Income Tax Act. Thus, there are no changes in taxation compared to the previous – these are costs of entertaining guests or gifts given to them.

Last updated on 08.01.2025