Republic of Estonia
Tax and Customs Board

Fringe benefits

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Employer’s car

Fringe benefit arises when the employer's car is allowed to be used for private rides. This means that it is not important to use the employer's car for private rides, but to enable the use of the car. Reimbursement of private rides when using the employer's car is also not important, because it does not change the taxation of the fringe benefit.

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Taxation procedure of fringe benefits

The price of a fringe benefit for enabling the use of an automobile in the ownership or possession of the employer for activities not related to employment or service duties or to the employer’s business is:

- 1.96 euros per month for a new car (for an engine power unit kW)
- in the case of a car older than five years, the price of a fringe benefit is 1.47 euros for an engine power unit (kW).

The motor power (kW) of a passenger car can be found in the **motor register of the Transport Administration** or in the passenger car registration certificate (technical passport).

In the case of hybrid passenger cars, the basis is the maximum power (kW) of the internal combustion engine stated in the motor register of the Transport Administration or in the technical passport.

In the case of electric and gas-powered cars, the basis is the maximum power (kW) of the internal combustion engine stated in the motor register of the Transport Administration or in the technical passport.

The price of the fringe benefit can also be calculated on a kilowatt basis for a van (category N1 vehicle) which the employer allows to use for private driving.

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Keeping driving records

It is not possible to reimburse private rides based on accounting and therefore keeping a logbook of driving records is not necessary. However, if the employer wants to prove that the car is used only for business purposes and business rides, it is possible to keep a logbook (for example, electronic GPS-driving records or the like).

If it is certified that the employer allows the car to be used only for business rides, no fringe benefit will arise. As the taxation of fringe benefits does not depend on the use of the car for private rides and private journeys cannot be compensated based on accounting, then even in the case the employer leases out the car to an employee at a preferential or market price, the tax liability on fringe benefits, nevertheless, arises on the kilowatt-based calculation.

If a car rental company or a lessor leases out a car to its employee as a customer with the rental market price, then the car rental company or the lessor will not have a tax liability on fringe benefits.

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Notifying the Transport Administration

If an employer does not enable the use of its car for private rides, the employer has to notify the Transport Administration about it.

If a company leases out a car to another company or a private person, then a notation must be made in the motor register of the Transport Administration that the car is used only for the performance of work duties. A lessor cannot guarantee that the lessee only makes business trips with the car. If the lessee allows its employees to use the car for private rides as well, regardless of the notation in the motor register of the Transport Administration, the lessee must declare and pay taxes on fringe benefits for the car.

The Transport Administration can be notified through the **e-service** and at the **Transport Administration's service bureaus**.

The Transport Administration must be notified only about the use of M1 category vehicles (passenger cars) for business rides. The use of N1 category vehicles (vans) does not need to be reported.

If, according to the Transport Administration, the company owns or uses cars with valid insurance and these are used only for the performance of work duties, please check that the persons doing the work are registered in the employment register and their wage payments are declared in Annex 1 and 2 of the Form TSD. To make business rides, the company must have registered employees.

If the Transport Administration has not been notified/there is no corresponding notification, it is considered that the employer allows employees to use the company car for private rides. Therefore, it is necessary to fill in code 4040 (“The enabling of a use of a vehicle of the employer for activities not related to employment or service duties or to the employer’s business") in Annex 4 of the form TSD and pay the tax liability.

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Declaration and tax liability

DECLARATION OF FRINGE BENEFITS

Fringe benefits are declared on Annex 4 of tax declaration Form TSD by the tenth day of the following month. Enabling the use of the employer's car is declared in Annex 4 of the Form TSD under code 4040 "The enabling of a use of a vehicle of the employer for activities not related to employment or service duties or to the employer’s business". The tax liability on fringe benefits is usually paid on the basis of Form TSD.

TAX LIABILITY ON FRINGE BENEFITS

The tax liability of the fringe benefit is calculated on the engine power of cars (1.96 euros per kW or, if the car is older than five years, 1.47 euros per kW).

Example 1
For a new 190 kW passenger car, the price of the fringe benefit is 1.96 × 190 = 372.40 euros, and taxes are calculated on it as follows:
income tax 372.40 × 22/78 = 105.04 euros
social tax (372.40 + 105.04) × 33% = 157.56 euros
total tax liability is 105.04 + 157.56 = 262.60 euros.

Example 2
For a new 90 kW passenger car, the price of the fringe benefit is 1.96 × 90 = 176.40 euros, and taxes are

calculated on it as follows:
income tax 176.40 × 22/78 = 49.75 euros
social tax (176.40 + 49.75) × 33% = 74.63 euros
total tax liability is 49.75 + 74.63 = 124.38 euros.

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Using a passenger car exclusively for business purposes

If a company wishes to deduct 100% input value added tax on the acquisition and use of a passenger car and not pay taxes on the fringe benefit, it must be ensured that the passenger car cannot be used for a non-business purpose.

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Proof of using a passenger car in business

The statement that a car is used exclusively for business purposes can also be made by the company representative only orally, and this is one of the pieces of evidence in the inspection of the circumstances related to the use of the car. However, such a statement can be considered general if it is not possible to determine how and in what way the use of the car exclusively for business purposes is specifically guaranteed. Although the law does not explain what evidence the taxpayer must use to prove that the expenditure is related to business (and taxable supply), the courts have explained that the taxpayer must organise its business activities in such a way that economic transactions are properly documented and important circumstances for determining tax liability are verifiable [1]. In addition, the court has stated that economic transactions may be certified only by invoices, but in this case they must be clear, credible and specific [2].

[1] Decision No. 3-3-1-15-13 of the Supreme Court of Estonia of 04.06.2013
[2] Decision No. 3-09-773 of the Tallinn Circuit Court of 22.10.2010

The same conditions apply to the deduction of input value added tax on the expenses related to passenger cars (including acquisition) and to proving the use of the passenger car exclusively in business – this means that the use of the passenger car during the taxation period must be verifiable and, at the request of the tax authority, certified by the taxpayer (there is a company decision, employees have been informed and the use is monitored).

The following are simplified questions to which the owner/responsible user of a passenger car used exclusively for business must **pay attention** if the tax authority wishes to check the purpose of use of the passenger car. The list of questions is not exhaustive.

- ✓ How is it ensured that the car is not used for private rides?
- ✓ What is the monthly mileage of the car?
- ✓ Where is the car kept during non-working hours?
- ✓ Who uses/can use the car?
- ✓ What is the fuel consumption of the passenger car (in a situation where the company has several vehicles, it is important to understand the fuel consumption of each passenger car)?
- ✓ Which rides have been made with the car – how is the mileage related to business?
- ✓ Has (have) the driver(s) of the car been fined during the inspection period (traffic fines, parking fines)?
- ✓ If there are more vehicles than employees, there must be a reasonable explanation.

The fact that it is not a car used exclusively in business is indicated by the following circumstances:

- ✓ persons not related to the company are indicated in the passenger car's technical passport;
- ✓ non-business-related equipment is installed in the car (ski box, bike rack for cars, safety seat, etc.);
- ✓ the company has more cars than users, and it cannot be reliably explained that the cars were acquired based on business rather than following the interests of related parties;
- ✓ in a company with only one board member (who can be the sole shareholder at the same time) and

- ✓ no employees, the board member or his or her family does not have another vehicle with which to make private rides.

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Keeping records

KEEPING RECORDS OF CARS USED EXCLUSIVELY IN BUSINESS

To make it easier for an entrepreneur to prove the use of a passenger car only in business, the following calculation may help. This is not the only option, and the company may use another credible way to prove it.

- ※ The entrepreneur decides whether private rides can be made with the cars he or she owns or not. Employees must also be informed of the decision.

- ※ The entrepreneur establishes rules for using cars exclusively in business. This is an internal document of the company, in which the topic related to passenger cars is clearly fixed, and the company must submit it immediately during an inspection.
  The rules of using cars establish:
  - ✓ that personal rides are not permitted;

  - ✓ the location where the car is kept when it is not used for business rides, and if the location is different from the company's place of business, then an economic justification is provided as to why it is expedient to store the vehicle in the specified location;

  - ✓ the users of the car, and whether and how the use is organised (e.g., whether contracts have been drawn up with the employees regarding the use, where the conditions are stated; if the vehicle is used by several employees, how is the return of the keys organized, etc.).

In addition to establishing the usage regime, the actual use of the cars must also be monitored. For example, if the rules of use stipulate that company-owned cars may not be used for private rides and that they must be parked in the company's parking lot at the end of the working day, then it must be

possible for the company to check this.

To ensure verifiability, records of the passenger car can be kept, for example, based on GPS placed in the car or the following indicators:

- monthly fixation of the initial and final mileage of the odometer so that it is possible to determine the monthly mileage;
- the names and addresses of customers, cooperation partners, etc., to whom the employees drove in a month (if this information can be found elsewhere, double counting is not necessary);
- an explanation of work rides if these partly overlap with personal interests. For example, going home or parking at home (if it is a car used exclusively for business, but one night the employee needs to go home, because he or she needs to go directly to a business assignment early in the morning from home).

There are several ways to keep records, such as using automatic journey accounting systems/applications or driving logbooks, from which or with the evidence added to it, it is possible to show the connection of the rides with business (for example, the names of customers related to the purpose of the ride are indicated, the information on refuelling is included so that the number of fuel receipts and the number of refuelling can be compared).

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Emergence of fringe benefit on employer's vehicles

According to subsection 4 of § 48 of the Income Tax Act, fringe benefits are any goods, services, remuneration in kind or monetarily appraisable benefits which are given to an employee in connection with working for an employer. Among other things, the use of a vehicle of the employer free of charge or at a preferential price is considered fringe benefit.

The purpose of taxation of fringe benefits is equally to tax both monetary and non-monetary benefits given to an employee. It is important to note that the employee's monetary income is taxed as a fringe benefit, not the employer's expense. Therefore, it can sometimes happen that the employer has not (directly) made an expenditure, but a fringe benefit has still been granted and the tax liability has arisen.

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What is considered a vehicle?

An employer's vehicle is considered to be a vehicle in the employer's possession – whether it is owned by the employer, acquired on the basis of a lease agreement, rented, in use (free of charge) on the basis of a usufruct agreement, etc. It is important that while the vehicle is put at the employee's disposal, it is owned or held by the employer.

As the Income Tax Act does not specifically address what is considered to be a vehicle, the definition of a vehicle is based on the legislation in which that concept is set out. According to the Road Traffic Act, a vehicle means a device powered by a motor or in another way, designated for road traffic or driving on the road. Therefore, when a fringe benefit arises, it does not matter what type/category of vehicle is involved. Whether it is a car, truck, bus, ATV, motorcycle, tractor, etc., if the employer allows the employee to use the vehicle owned or in the possession of the employer for free or at a preferential price for the employee's private rides, a fringe benefit arises and, also, a tax liability.

For employer's passenger cars (M1 and M1G category vehicles), the legislator has established specific rules for calculating the tax liability. The reason is the fact that enabling the employee to use the employer's car is very common and calculating the tax liability according to the general rules for giving property to use would be too burdensome for the taxpayer.

In the case of the employer's van (N1 category vehicle), the legislator has given the taxpayer the opportunity to choose whether the price of the fringe benefit for private rides is calculated:

1. based on the rental market price,
2. based on the difference between the rental market price and the preferential price or
3. the calculation of the fringe benefit is based on the power of the vehicle's engine and the age of the vehicle. With new cars, the price of the fringe benefit is 1.96 euros per month for an engine power unit (kW) of the automobile as indicated in the motor register. In the case of an automobile older than five years, the price of the fringe benefit is 1.47 euros for an engine power unit (kW) of the automobile.

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Taxation procedure of fringe benefits

WHAT IS THE PROCEDURE FOR CALCULATING THE FRINGE BENEFIT FOR VEHICLES OTHER THAN PASSENGER CARS?

In order to calculate the tax liability correctly, the **procedure for determining the price of fringe benefits** established by the Minister of Finance must be followed. Pursuant to clause 1 of § 2 of the regulation, if the fringe benefit is the grant, free of charge or at a preferential price, of an asset, incl. a vehicle (except a passenger car), owned or held by the employer, for the use of work, official or service tasks or for activities not related to the employer's business, **the price of the fringe benefit is deemed to be the market price for the rent of such asset or the difference between the market price for the rent and the preferential price.** Market price is the price used by independent parties in their transactions under similar conditions, such as in the case of vehicles, the price and conditions with which vehicles are rented to their customers by vehicle rental companies. The full price of the fringe benefit is taxed.

The regulation of the Minister of Finance does not stipulate how the employer should document enabling the use or not enabling the use of vehicles owned by the employer for personal rides. General documentation requirements apply here, i.e., the employer must be able to prove with sufficient documents whether and how the rides made with this vehicle are/were related to its business or not. If there are enough documents to make sure that all rides made with the vehicle were related to business and that personal rides (free or with a preferential price) of employees were not made, then no tax liability arises.

Example
The employer owns an N1 category van with which the employee also makes personal rides. However, since the employer does not charge the employee for these rides, the employee has received a fringe benefit – the opportunity to use the car for free.
To calculate the price of the fringe benefit and the tax liability, the employer chose the market price of renting the van.
For example, if the rental conditions and the rental price for such van in vehicle rental companies is 32 euros per day for long-term rental, regardless of the actual mileage, the employer can calculate the price of the fringe benefit based on it. If the employee used the van for a whole month, i.e., 30 days, the price of the fringe benefit is 32 × 30 = 960 euros.
The income tax liability is 960 × 22/78 = 270.77 euros, and the social tax liability is (960 + 270.77) × 33% = 406.15 euros. Therefore, in the case of giving such van to an employee for free use for a month, the employer must consider the income and social tax liability of 676.92 euros.

Of course, the rental conditions and prices of the rental companies are not always the same, and to determine the market price, it must be based primarily on conditions like those of the employer itself.

Since, pursuant to the Income Tax Act and the regulation of the Minister of Finance, a fringe benefit arises from giving any employer's property to an employee for personal use free of charge or at a

preferential price, the use of employer's property that is not a vehicle in the sense of the Road Traffic Act (e.g., boats, launches, etc.) may also give rise to a fringe benefit. For the use of such assets, fringe benefit is calculated in the same way as for the use of vehicles.

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Value added tax calculation related to passenger cars

A procedure applies to passenger cars and the goods and services purchased for their use, according to which instead of taxing the self-supply of a passenger car, **the deduction of the value added tax (VAT) paid on the purchase of the passenger car** (including renting, leasing) **and the goods and services for its use is limited. The overall limit for the deduction of input VAT is 50%.**

Therefore, when **purchasing a car to use in business-related activities** or **using it based on a usage agreement** and **receiving goods and services for this car, 50% of the input VAT is generally deducted** from the calculated VAT. Essentially, 50% is considered to be the percentage of using a car in business.

The limitation of deducting input VAT applies to a vehicle of category M1 (including M1G) the gross weight which does not exceed 3,500 kilograms and which does not have more than 8 seats in addition to the driver's seat.

If a taxable person also has **supply exempt from tax or activities that are not considered business,** then these circumstances must also be taken into account when deducting input VAT.

Car-related costs are, for example, motor fuel, spare parts, maintenance, repairs, parking fees, costs for car transport (ferry tickets).

The following **are not considered as the costs** of a passenger car:

- ✓ the costs of placing advertisements on vehicles – these costs are not related to using vehicles, but to advertising;
- ✓ purchase or rent of a trailer.

If, **in addition to business rides, private rides** are made **with a passenger car purchased for a company,**

then 50% of input VAT (or less, for example, if part of the company's supply is exempt from tax) is deducted from VAT upon the purchase or use of a passenger car used for business under a contract of use and upon receipt of goods and services for it. Therefore, regardless of the extent to which the vehicle used for business is used for private consumption, the input VAT can be deducted to the extent of 50%.

The transport of employees between the place of residence and the place of work with the employer's passenger car **is not deemed to be use of a passenger car for private purposes (i.e., it is deemed to be use of a passenger car for business purposes), if the conditions provided for in subsection 5[1] of § 48 of the Income Tax Act are met.** Read more from the article „**Transport of employees to work and home pursuant to subsection 5[1] of § 48 of the Income Tax Act**".

EXAMPLES OF DEDUCTING INPUT VAT

Example 1
A passenger car is **both in business and in private consumption.** The car is used for taxable supply in the extent of 60% and for tax-exempt supply in the extent of 40%.
Motor fuel was bought at a price of 50 euros + VAT 11 euros.
3.30 euros of input VAT can be deducted (11 × 0,5 × 0,6).

Example 2
A passenger car is used **exclusively for business purposes.** The car is used for taxable supply in the extent of 60% and for tax-exempt supply in the extent of 40%.
Motor fuel was bought at a price of 50 euros + VAT 11 euros.
6.60 euros of input VAT can be deducted (11 × 0,6).

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Exceptions

Subsection 4 of § 30 of the Value-Added Tax Act provides exceptions when the deduction of VAT paid for a car and receiving goods and services for its use is not limited.

Exception applies in the following cases.

- The car is purchased for **sale** or **rental.**
  It is important that cars purchased for sale or rental are **not taken into use by themselves.**

- When a car purchased for sale is put into use for another purpose, the **input VAT deducted at the time of purchase must be adjusted.** The correction must be made in the taxable period, when the taxable person takes the car purchased for sale to its own use. If the taxable person is also involved in granting vehicles into use and, for example, a car purchased for sale is rented out, the 2-year period starts counting from the car rental.

- The passenger car is mainly used for **passenger transportation** or **driving practice for a fee.** Taxable person has the right to **deduct input VAT in full** for the vehicle used for business and the goods and services purchased for its use, even if the vehicle is mainly used for the carriage of passengers for a charge on condition that the taxable person has a **Community licence** and a **certified copy** of the Community licence or, in the case of the provision of taxi service, a **taxi licence and a licence card**.
  Private consumption is taxed as self-supply according to **subsection 7[1] of § 12 of the Value-Added Tax Act**.
  According to **subsection 7[1] of § 12 of the Value-Added Tax Act** the taxable value of self-supply for the use of these passenger cars is: the price of the fringe benefit calculated on the basis of the Income Tax Act ÷ 1.22.

  Therefore, granting your employee the use of a car that is mainly used for the provision of a paid passenger transport service or driving practice is taxed. Unlike other passenger cars, it is possible to deduct 100% of the input VAT on these vehicles even if the car is used for private consumption. It is important that the vehicle meets the conditions set out in **clauses 3 or 4 of subsection 4 of § 30 of the Value-Added Tax Act**.

  The taxable value, including VAT, of the self-supply resulting from the use of a car used mainly for passenger transport or for educational purposes and an N1 category truck (van) with a gross weight of up to 3,500 kilograms for private rides is the price of fringe benefit calculated on the basis of the Income Tax Act. According to the Value-Added Tax Act, self-supply cannot arise from the use of other passenger cars for private rides.

- The car is used **exclusively for business purposes.**
  The exception is applied only if the passenger car is directly necessary for business and this car is used exclusively for business.

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Keeping records of the use of the car

A taxable person who applies the aforementioned exceptions and has fully deducted the input VAT on the car and related expenses **must ensure** that t**he use of the passenger car in question for non-business rides is not possible** and may continue to keep records of the use of the car.

The entrepreneur decides which way to keep records – the goal is to ensure that the entrepreneur's passenger car is used only for business purposes. For example, an entrepreneur can, among other things, keep a **detailed record, i.e., a driving log,** or use a **GPS service** provided by a third party.

In general, a car used exclusively for business purposes should be **parked at the company during non-working hours.**

The company must decide:

- ✓ how a car is used,
- ✓ how such use is secured, and
- ✓ how it is possible to check the use of the car both by the management and the tax authority.

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Private use of cars

If a car used in business is also **for private use**, regardless of whether the employee reimburses the costs related to the use of the car or not, the use of such a car **is not considered to be used exclusively for business purposes.**

This procedure also applies to companies the field of activity of which is granting cars to use, and which provide **cars for their employees to use for a charge.**

To avoid double taxation, the **private use of a car is not taxed as self-supply** and granting **the use of a car for a charge** to an employee, servant or member of a management and control body of the taxable

person **is not considered supply.**

The use of a company car for personal rides is taxed with a fringe benefit based on the **vehicle's capacity.**

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