

# Tax Alert

Estonia, May 2009

AS PricewaterhouseCoopers in Estonia helps clients in finding tax efficient business solutions and managing tax risks.

We work together with our colleagues in other PricewaterhouseCoopers' offices world-wide and use our access to international know-how and long-term experience to quickly and efficiently solve tax issues that arise both locally and in foreign jurisdictions.

For more information, please see our contact details below.



## Increase of unemployment insurance contributions

In the end of 2008, the Estonian Government approved the increase of the rates of unemployment insurance contributions from 0.6% to 1% for employees and from 0.3% to 0.5% for employers from 1 July 2009.

However, on 30 April 2009 the Estonian Government decided to increase the rates already from 1 June 2009 and due to rising unemployment levels to further increase the rates of contributions. Thus, from 1 June 2009 the new rates will be 2% for employees and 1% for employers, which are the maximum rates allowed under the current Unemployment Insurance Act.

The contributions mainly apply to salaries and service fees paid to individuals. However, the unemployment insurance contributions are not due on fees paid to members of the management and supervisory board. The employee's part of unemployment insurance contributions (withheld by the employer at source) is deductible from the taxable income of the resident individual.

## Suspension of contributions to compulsory accumulative pension scheme

On 14 May 2009, the Estonian Parliament adopted the proposal of the Government which would generally suspend the contributions to the compulsory accumulative pension

scheme from 1 June 2009 to 31 December 2010.

Currently, resident employees born after 31 December 1982 are obliged to join the compulsory accumulative pension scheme and make contributions at 2% from gross salary. For resident employees born before 1983 joining the compulsory accumulative pension scheme is voluntary, but after joining, it becomes compulsory and employees may not subsequently leave the scheme. In addition to the 2% contribution made by the employee, 4 percentage points of the social security contribution payable by the employer (33%) will be transferred by the state to the employee's pension account.

Under the adopted law amendment, state contributions (4%) will be temporarily suspended for the period from 1 June 2009 to 31 December 2010. However, upon the voluntary application the employee may continue (2%) contributions from 1 January 2010 and state will continue its contributions at 2% rate from 1 January 2011. Without such an application, all contributions will be fully suspended for the period from 1 June 2009 to 31 December 2010 and in 2011 the rates of contributions will be 1% for the employee and 2% for the state. The standard system of contributions (2%+4%) is expected to be fully restored from 2012. Exceptionally, the persons born on and before 1954 are upon their application entitled to continue with the standard system of contributions also in 2010 and 2011.

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The contributions to the compulsory accumulative pension scheme mainly apply to salaries, directors' fees and service fees, but also to net business income of sole proprietorships. The contributions are withheld by the employer at source and are deductible from the taxable income of the resident individual.

### **New Gambling Tax Act adopted**

On 22 April 2009 a new Gambling Tax Act was adopted in Estonia that will enter into force as of 1 June 2009 (in respect of remote gambling as of 1 January 2010). New law was drafted as a consequence of the new Gambling Act that entered into force as of 1 January 2009 and that changed the previous regulations starting to regulate among other things also commercial lotteries organized as marketing campaigns and legalizing remote (internet) gambling. Main changes in taxation are as follows: - Tax rates for gambling machines and gambling tables will be unaffected and will remain respectively EEK 7000 (approx. EUR 447) and EEK 20000 (approx. EUR 1278) per month. However, the requirement for revenue stamps will be abolished and it will be replaced by the decision given by the tax authorities to the gambling operator that confirms the number of machines and tables in the specific gaming hall the operator has paid tax for;

- Amusement game machines (games of skill) will no longer be taxed on the basis of the turnover, but operators must pay a monthly tax of EEK 500 (approx EUR 32) per machine;
- All lotteries will be made subject of a uniform 18% tax that applies to the amount received from the sale of the tickets (previously the numerical lotteries were subject to a lower 10% tax rate);
- Commercial lotteries organized as marketing campaigns will become subject to 18% tax on the prize fund (tax is only applicable to lotteries with prize fund with EEK 10000 and more);
- Betting and remote gambling is subject to 5% tax rate on net amount (stakes minus winnings).

### **Double tax treaty concluded between Estonia and Isle of Man**

On 8 May 2009, Estonia and Isle of Man concluded a treaty for the avoidance of double taxation with respect to taxes on income. Tax treaty generally follows the wording of the OECD Model Tax Convention, which is a basis also for the rest of the Estonian tax treaties. It is noteworthy that the treaty limits withholding taxes on dividends, interest and royalties to 0%.

Provided that the income received by Estonian resident from Isle of Man has been taxed there, an exemption method is used as a double tax relief. Where an Estonian resident company derives income that is attributable to a permanent establishment in the Isle of Man and that income has not been subject to tax, exemption method is applied to the 50% of the income. Similarly, where an Estonian resident company receives dividends from Isle of Man and the underlying profits have not been subject to tax in Isle of Man, exemption method is applied to the 50% of the dividends. Treaty will enter into force after the parties have notified each other on the completion of the respective domestic procedures (e.g. ratification in Estonia).

### **Double tax treaty concluded between Estonia and Macedonia**

On 20 November 2008, Estonia and Macedonia concluded a treaty for the avoidance of double taxation with respect to taxes on income. Treaty was ratified in Estonia on 8 April 2009. Tax treaty generally follows the wording of the OECD Model Tax Convention, which is a basis also for the rest of the Estonian tax treaties. It is noteworthy that the treaty limits withholding taxes: (a) on dividends to 0% provided that the shareholder is a company holding directly 25% of the capital of the company paying the dividends and 5% in all other cases; (b) on interest to 5%; (c) on license fees to 5%. Treaty will enter into force after the parties have notified each other on the completion of the respective domestic procedures (e.g. ratification in Estonia).

### **Double tax treaty between Estonia and the Netherlands amended**

On 26 June 2008, the Netherlands and Estonia signed a third protocol to the income and capital tax treaty between Estonia and the Netherlands which provides a replacement of the exemption method for the avoidance of double taxation by the credit method for artists and sportsmen resident in Estonia. This amendment results from the fact that the Netherlands as from 1 January 2007 no longer taxes non-resident artists and sportsmen performing in the Netherlands. The purpose of the amendment is an avoidance of non-taxation by both of the contracting states. Protocol will enter into force on 22 May 2009 and amendments will be applicable as of 1 January 2010.

Text of the treaty (also in English) is available at:  
<http://www.riigiteataja.ee/ert/act.jsp?id=13163254>

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