

# **Country Profile Fact Sheet**

## **Estonia**

**Working Group  
Market Access  
in co-operation with  
EIC EE881 Tallinn  
March 2001**

## Table of contents

<a href="#">Sources</a> .....	2
<a href="#">Disclaimer</a> .....	2
<a href="#">Overall view of Estonia</a> .....	3
<a href="#">Phare situation in the country</a> .....	3
<a href="#">2000 Regular Report</a> .....	4
<a href="#">How to set up a company</a> .....	5
<a href="#">Commercial Code</a> .....	5
<a href="#">Laws and regulations</a> .....	9
<a href="#">Accounting Principles</a> .....	9
<a href="#">Auditing Standards</a> .....	9
<a href="#">Labour Legislation</a> .....	10
<a href="#">Vacation</a> .....	11
<a href="#">Maternity leave</a> .....	11
<a href="#">Sickness</a> .....	11
<a href="#">Payment for overtime</a> .....	11
<a href="#">Social security</a> .....	12
<a href="#">Trade Unions</a> .....	12
<a href="#">Inward investment incentives</a> .....	12
<a href="#">Sectoral opportunities/priorities</a> .....	12
<a href="#">Inward Investment Incentives</a> .....	13
<a href="#">Banking system</a> .....	14
<a href="#">Taxation</a> .....	14
<a href="#">Principal Taxes</a> .....	14
<a href="#">Income Tax</a> .....	15
<a href="#">Income tax incentives</a> .....	16
<a href="#">Value Added Tax</a> .....	16
<a href="#">Social Tax</a> .....	16
<a href="#">Other Taxes</a> .....	16
<a href="#">Tax treaties</a> .....	17
<a href="#">Market development, market conditions</a> .....	17
<a href="#">Environmental regulations</a> .....	18
<a href="#">Intellectual and Industrial Property Rights</a> .....	18
<a href="#">Export/import formalities</a> .....	18
<a href="#">Recommendations and hints</a> .....	19
<a href="#">Negotiations, payment</a> .....	19
<a href="#">Useful addresses</a> .....	20
<a href="#">Internet links</a> .....	21
<a href="#">Statistics</a> .....	23

## **Sources**

COM (1998) 705 Final.

Estonia Investment Agency, August 1999.

Statistical Office of Estonia 1999-08-13.

2000 Regular Report from the Commission on Estonia's Progress Towards Accession, November 2000

Market Introduction Estonia, Swedish Trade Council, March 2000

Contributions from EIC EE881, EE882.

## **Disclaimer**

This country profile is not intended to be comprehensive. Its purpose is to give an overview of the general situation in Estonia. The information herein should be treated as a guideline. Although every care has been taken to ensure accuracy, no responsibility for errors can be taken. Whenever taking a business decision, the actual laws and regulations should be consulted. More detailed information can be found by consulting the sources listed in this document.

## Overall view of Estonia

Location: Eastern part of the Baltic Sea area

Area: 45 227 km<sup>2</sup>

Time: GMT +2

Population: 1 445 100 (01/01/1999)

Capital: Tallinn

State organisation: Unicameral Riigikogu

Administrative division: 15 counties

Currency: Kroon, plur. Krooni. 1 Kroon = 100 senti, 1 EUR=15.6 EEK

Main port: Muuga (Tallinn)

Main airports: Tallinn

## Phare situation in the country

Since January 2000, there are three pre-accession instruments financed by the European community to assist the applicant countries of Central Europe in their pre-accession preparations; the Phare programme, SAPARD which provides aid for agricultural and rural development; and ISPA, which finances infrastructure projects in the fields of environment and transport. These programmes concentrate their support on the Accession Partnership priorities that help the candidate countries to fulfil the criteria for membership.

In the years 2000 – 2002 total finance assistance to Estonia will amount annually to at least 24 million euro from Phare, 12 million from SAPARD, and between 21 and 37 million from ISPA.

During the period 1990 – 1999, the Phare programme allocated 190 million to Estonia. The 2000 Phare Programme for Estonia consists of a national allocation of 24 million, concentrated on the following priorities:

- political criteria – social integration and language training for ethnic minorities (3.14 M).
- administrative capacity – financial management and financial control (1 M).
- internal market – market surveillance and master customs tariff system (3.8 M).
- employment and social affairs – labour market services (1.8 M).
- justice and home affairs – drugs, police training and crime prevention (1.9 M).
- agriculture – agricultural support systems (1.98 M).
- economic and social cohesion – business development, training and investment (10.1 M).

An additional 3 million euro has been allocated under the Cross Border Cooperation programme for investment in the infrastructure, to improve water quality, and for a small project facility to support cooperation activities in the Baltic region.

Estonia also participates and benefits from Phare funded multi-country and horizontal programmes, such as TAIEX, Justice and Home Affairs and the Small and Medium-sized Enterprise Facility. Furthermore, Estonia participates in a number of Community programmes – Multiannual Programme for Enterprises and Entrepreneurship, 5<sup>th</sup> Framework Programme on

Research and Development, Leonardo da Vinci, Raphael, Socrates, Youth for Europe, Drug Dependence and Health Promotion, Culture 2000. Estonia has expressed its interest to participate in the Culture 2000 Community programme. Following the opening of negotiations regarding Estonia's participation in the European Environment Agency, an agreement has been reached. Following ratification and entry into force of this agreement, scheduled for early 2001, Estonia will become a member of the Agency.

Since 1998 the Commission has worked with the EIB and International Financial Institutions, in particular the EBRD and the World Bank, with a view to facilitating the co-financing of projects relating to pre-accession priorities.

### *2000 Regular Report*

Economic development has resumed in Estonia from second half of 1999. A stable economic and legal environment and proper policies have supported the rapid return to relatively strong growth after the economic recession partly prompted by the Russian crisis. In particular the Government's stability-oriented macroeconomic policy has led to a restructuring and a rapid adjustment to the new conditions by enterprises and other economic actors.

Estonia's trade with the EC decreased slightly in 1999, to recover again in the first half of 2000. By June 2000, Estonia's export (except transit exports) to the EC accounted for 73% of total exports. Imports from the EC accounted to 73% of total imports. Estonia's main EC trading partners are Finland, Sweden and Germany and the main exports to the EC are machinery and electrical equipment, wood and mineral products, while the most important import products are machinery and electrical equipment, agricultural products including processed foodstuffs and transport equipment.

Estonia continues to have a very liberal external trade and payments regime. In November 1999, it joined the World Trade Organisation, WTO. On 1 January 2000 a limited number of tariffs on a selected number of agricultural products were introduced for countries with which Estonia has no free-trade agreement. Tariffs have been set at rates below the level agreed in the WTO agreement. Some of the few remaining restrictions on foreign direct investment were removed.

All SME's are privately owned, while only a very small number of large companies have yet to be privatised. More than 99% of enterprises in Estonia are SME's. The share of SME's is largest in wholesale and retail activities and in construction, while larger enterprises are dominant in industry, energy production and fishing. At the end of 1998, SME's accounted for about 47% of the total workforce, and for more than 74% of enterprise employment.

Estonia has continued to attract a high level of foreign direct investment inflows. Gross foreign direct investment inflow reached 5.96% of GDP in 1999 and 5.7% in the first half of 2000.

Except in a declining number of well-defined areas, there are no significant barriers to market entry. In fact, the number of new companies being entered in the Commercial Register increased from about 4 200 in the period 1 October 1998 – 1 June 1999 to about 5600 in the same period of 1999 – 2000.

Estonia has made progress in developing a policy towards SME's that is in line with the principles and objectives of EC enterprise policy. The main lines of Estonia's policy towards SME's revolve around internationalisation, creation of a system of regional business support and the development of innovation and technological development. Although the definition of SME's recommended by the European Commission is not officially recognised in Estonia, it is applied in practice.

## **How to set up a company**

### *Commercial Code*

The new Commercial Code was adopted on 15 February 1995 and has been effective since 1 September 1995. The law establishes the basic principles for restructuring Estonian entrepreneurship. Its main aim is to increase the responsibilities of those engaged in entrepreneurship. The Commercial Code introduces new principles and includes new legal and registration requirements for entrepreneurs.

The Commercial Code also outlines the role of the Commercial Register, which exercises legal control over the activities of entrepreneurs. Estonian law is based on the continental European model.

There are five forms of business entities:

- general partnership (täisühing or TÜ in Estonian)
- limited partnership (usaldusühing or UÜ in Estonian)
- private limited company (osäühing or OÜ in Estonian)
- public limited company (aktsiaselts or AS in Estonian)
- bransch (filiaal in Estonian).

Foreign investors can establish all forms of business entity and own them 100%. The most usual forms in which a business may be conducted are the following:

- Sole Proprietorship - Any physical person may be a sole proprietor. If a person is without legal competence, a legal representative will conclude transactions in the name of the person to the extent provisioned by law. If the legal competence of a person is restricted he or she may, under conditions provided by law, conclude transactions with the consent of a legal representative. A sole proprietor may be entered in the Commercial Register at his or her request. A sole proprietor will be entered into the commercial register if he or she is registered with the Tax Board as a taxpayer under the Value Added Tax Act. The law may provide other cases in which a sole proprietor will be entered in the commercial register.
- General Partnership - A general partnership is a commercial undertaking in which two or more partners operate under a common business name and are jointly liable for the obligations of the undertaking with all of their assets. A general partnership will operate on the basis of the partnership agreement concluded by the partners. There is no minimum capital requirement and no obligation to present the partnership agreement to the Commercial Register. Each partner will receive a portion of the distributed profit corresponding to the partner's contribution (unless the partnership agreement prescribes otherwise). After leaving the general partnership the partner is personally responsible for fulfilling the liabilities

that occurred before he left for the next five years. Similarly, when an unlimited partnership terminates, the partners are jointly responsible for its liabilities for the next five years.

- **Limited Partnership** - In a limited partnership there must be at least one general partner with unlimited liability and one or more limited partners who are liable only to the extent of their capital contributions. The limited partner is not responsible for the liabilities of the limited partnership if he has paid his deposit in full. A limited partner who has not fully paid his deposit is responsible for the liabilities of the limited partnership up to the unpaid deposit. A limited partner does not usually have the right to take part in the management unless the partnership agreement states otherwise but he is entitled to the corresponding part of its profits.
- **Private Limited Company** - A private limited company is a commercial undertaking the capital of which is divided into shares. A shareholder will not be personally liable for the obligations of the company. A private limited company is liable for the fulfilment of its obligations with all of its assets. The share capital must be a minimum of 40,000 EEK (approx. USD 2,800). The minimum nominal value of a share is 100 kroons. A share of a private limited company can be sold to the other joint owner. When selling to a third party the joint owners have the prerogative of purchasing the share. A joint owner can only own one share in a private limited company. A share of a private limited company can be divided and therefore alienation of a part of a share is possible. In that case the agreement of other joint owners is necessary. A share of a private limited company can be pledged or be of shared ownership if not fixed otherwise in the Articles of Association. A share is not heritable if the Articles of Association state so. The Management Board organises the accounting of the private limited company. A private limited company must have an auditor if the share capital of the private limited company is greater than 400,000 EEK (approx. USD 28,000) or if so stated in the Articles of Association. Shareholders whose shares represent at least one tenth of the share capital may demand a resolution on conducting of a special audit on matters regarding the financial situation of the private limited company.
- **Public Limited Company** - A public limited (stock) company is a commercial undertaking, which has a stock capital divided into stock. A stockholder is not personally liable for the obligations of the public limited company. A public limited company is liable for the fulfilment of its obligations to the full extent of its assets. Stock capital must be a minimum of EEK 400,000 (approx. USD 28,000) and the minimum par or nominal value of a share should be EEK 10. The number of shares a shareholder can own in a stock company is unlimited and shares can be freely transferred to third parties. A share cannot be divided. Shares may either be registered or bearer shares. The rights attached to registered shares belong to the person who is entered as the shareholder in the stock register. The rights attached to bearer shares are considered to belong to the person who has possession of the stock certificate unless proved on the contrary or unless otherwise provided by law. The general meeting, which specifies the procedure for the remuneration of auditors, will also specify the number of auditors.

**Formation Procedures** - One or several individuals or legal persons can establish a private limited company as well as a public limited company. For entering a company in the Commercial Register, the founders must draft a Foundation Agreement, which is terminated after the company has been entered into the Commercial Register, and Articles of Association. The Foundation Agreement must be signed by all founding members and notarised in Estonia or at the Estonian diplomatic representation in a foreign country. If there is only one founder, the Foundation Agreement is substituted by the founding resolution signed by the founder and notarised thereafter. Upon foundation, the founders shall open a bank account in the name of

the newly founded company into which monetary contributions will be paid in. The required minimum share capital requirement must be paid in before the registration of the company. Contributions may be monetary or non-monetary, but not in the means of service or work provided for the company or any activities of the founders at the foundation of the company. If the non-monetary contribution exceeds EEK 40,000 (approx. USD 2,800) or if non-monetary contributions in total exceed one half of the share capital, an evaluation is required by an auditor. An auditor must audit the valuation of a non-monetary contribution paid in to a public limited company.

The Foundation Agreement must include the following information:

- the business name, location, address and area of activity of the company
- the names and residences/locations of the founders
- the proposed amount of share capital
- the nominal value and number of shares and, upon issue of more than one class of stocks, their denotation and the rights attached to the stocks and their division among the founders
- the amount to be paid for the shares, and the time, place and procedure of payment
- if a share is paid for by a non-monetary contribution, the item of the non-monetary contribution, its valuation method and value
- the names, personal identification codes and places of residence of members of the management board, supervisory board, procurator and auditors (if appointed)
- the assumed amount of foundation expenses.

Registration Requirements - The Management Board must submit an application for the registration in the Commercial Register within six months of concluding the Foundation Agreement. The application must be signed by all members of the board and include the following information to be entered to the Commercial Register:

- the business name of the public limited company
- the area of activity, location and address of the public limited company
- the amount of stock capital
- the date of approval of the Articles of Association
- the names, personal identification codes and residences of the management board
- the members of the management board entitled to represent the public limited company differently than provided for in subsection 307 (1) of the Commercial Code
- the beginning and end of the financial year
- other information provided by law.

The following documents should be enclosed with the application:

- the foundation agreement
- the Articles of Association
- a bank notice concerning the payment of stock capital
- upon payment by a non-monetary contribution, the agreement concerning the transfer of the contribution to the public limited company, documents certifying the value of the contribution and an opinion on the valuation of the non-monetary contribution signed by the auditor
- the names, personal identification codes and dwelling of the members of the management board, the supervisory board, and the auditors
- specimen signatures of the members of the management board
- telecommunication numbers (telephone, facsimile, etc.)
- other documents provided by law.

In case the founder is a foreign company, an official certificate proving the existence of the company in the country of incorporation is required. This certificate as well as a foundation resolution must be notarised in the foreign country by a public notary, which is legalised by the Ministry of Foreign Affairs of the foreign country and the Estonian Embassy or its diplomatic representative. If there is a translator available in the Estonian Embassy, these documents may be translated in a foreign country and legalised at the Estonian Embassy. In that case, no further legalisation is required in Estonia. However, if there is no acceptable translator available in a foreign country, the documents must be legalised at the Estonian Embassy and sent to Estonia for translation and notarisation.

All documents must be submitted to the Commercial Register in Estonian or with an appended notarised translation. The Foundation Agreement must be signed by all founders or by their notarised proxy. As a rule, the registration process takes up to 2 or 3 weeks. The following stamp taxes are applicable on registration of the company:

- Sole Proprietorship EEK 500
- General / Limited Partnership EEK 500
- Branch of a foreign enterprise, depends on organisation form; Public limited company 0.2% of share capital but not less than 4 000 EEK, Private limited company 0.2 of share capital but not less than 3 000 EEK.
- Private / Public Limited Company 0.2% of (nominal) share capital (min. EEK 2 400 max. 40 000 for public and 20 000 for private limited company)

Foreign Enterprise Entities - If a foreign commercial undertaking wants to permanently offer goods or services in its own name in Estonia, it should enter its branch in the commercial register. As a branch is not a legal person, the commercial undertaking will be liable for the obligations arising from the activities of the branch. In the cases provided by law, a commercial undertaking must obtain a license in order to open a branch in Estonia. The branch of a foreign company is established after its registration in the Commercial Register. To register a branch, the application must contain the same data about the branch and the parent company as for a stock company. The application also has to state the country under whose legislation the corporation operates.

A foreign commercial undertaking should appoint a director or directors for the branch. A director must be a natural person with legal competence. The residence of at least one director must be in Estonia. A bankrupt or a person whose right to engage in economic activity has been taken away pursuant to the law cannot be a director. If the branch or company conducts banking activities in Estonia it will need a foreign investment license from the Council of the Bank of Estonia.

A foreign commercial undertaking must maintain separate accounts concerning the branch. Accounts concerning the branch must be maintained pursuant to the requirements of the Accounting Act. Implementation of the Commercial Code By 1 September 1999 all capital requirements for limited liability companies (40,000 EEK) and stock companies (400,000 EEK) must be fulfilled. Before 1 September 1999 limited liability companies with a minimum capital of 10,000 EEK and stock companies with a minimum capital of 100,000 EEK must be registered in the Commercial Register if they wish to continue business.

## **Laws and regulations**

Estonia is using the examples of the EU member states to bring its legal system up to date. Improved legislation was introduced in the field of competition industrial property rights, energy and the financial sector. To guarantee a competitive environment, the authorities will set up regulatory bodies for the relevant markets (telecommunication, energy, railways).

The overall legislative framework in Estonia is well developed. It supports and regulates most aspects of business activity. Most of this legislation is recent and follows the German and Scandinavian models. Although there have been cases in the past of inconsistent application and interpretation of the law due to lack of experience in the courts, there has been progress in clarifying the legislation and improving enforcement of civil and commercial law.

### *Accounting Principles*

The Law on Accounting (valid from 1 January 1995) regulates basic accounting functions in all business entities registered in Estonia. It does not regulate accounting for taxes, which are regulated by other laws and acts. The essence of the law is framed in compliance with International Accounting Standards (IAS). With a few exceptions, the use of IAS was acceptable prior to 1 January 1995.

Compared with International Accounting Standards the major differences are:

- no consolidation is required (equity method is used to account for subsidiaries)
- notes to financial statements are usually fewer.

In addition to the Law on Accounting there are a number of regulations issued by the Estonian Accounting Committee, which interpret and amend the law. Each business entity may also establish additional rules regulating some aspects of its own accounting and reporting.

A fiscal year is twelve months long. A business entity can choose a fiscal year ending on 31 March, 30 June, 30 September or 31 December. If a company wishes to use any other fiscal year, permission from the Ministry of Finance is required. The law also prescribes that a parent company and its subsidiary should have the same financial year, which may also be a fiscal year.

All accounting records should be maintained for seven years. Contracts, business plans and other documents, necessary for reconstructing business transactions should be maintained for ten years.

### *Auditing Standards*

All companies registered in Estonia are required to submit their audited financial statements to the authorities within 6 months of the end of the fiscal year.

An audit is not required for a private limited company if its share capital is less than EEK 400,000 and if its net sales in the previous fiscal year did not exceed four times the mandatory VAT registration limit set in the Law on Value Added Tax. This currently equals EEK1,000,000.

An audit is not required for sole proprietorships or for partnerships, provided the partners are neither public nor private limited companies nor business cooperatives.

The auditing process is regulated by Estonian Standards of Auditing. General requirements concerning auditing are regulated by the Accounting Law and the Commercial Code. Estonian Auditing Standards are sanctioned by the Estonian Auditing Committee on September 1994.

Estonian Auditing Standards are composed in accordance with generally accepted auditing standards and are based on the standards of the International Federation of Accountants (IFAC), International Standards on Auditing (ISA) as well as on the standards of the American Institute of Certified Public Accountants (AICPA).

Currently, all major international accounting firms are present in Estonia.

#### *Labour Legislation*

- The length of a working week            5 days
- The length of a working day            8 hours
- General vacation                        28 days
- Age of retirement                        63 years

Since 14 June 2000 there is a law on social defence of unemployed. Those out of work are eligible to receive an unemployment benefit (currently EEK 400) for a period of six months provided they have registered themselves with the government.

Foreign citizens must apply for a work permit. Having obtained one, they have the same rights and obligations as residents of Estonia.

The most important statutes and rules regulating the activities in the labour market are the Constitution of Estonia, Conventions of International Organisation of Labour, Law on Employment Contracts and several enactments of the Government and ministers of Estonia. These statutes and rulings are in accordance with ILO principles specifying the following main clauses:

- the right to choose freely your own field of activity, occupation and work place
- working conditions are under the supervision of the state
- the employer-employee relations are governed by the state to the extent necessary to guarantee equitable interdependence between the parties and to defend the interests of the economically weaker party, i.e. the employee
- employees' and employers' freedom of association, i.e. formation of trade unions and organisation of legal strikes and demonstrations.

Every employee, including adolescents, must enter into a labour contract personally. By law the contract is required to include some terms in the absence of which, the contract is defective. These terms should specify:

- the job and its level of difficulty

- the working hours, wage and the place of work
- the period of the contract's validity and the time for commencing the job (as a rule, a contract is concluded for an open-ended period).

Other terms such as additional cultural services and special working conditions are optional and do not affect the validity of the contract in any way. The contract is to be considered expired on the following grounds:

- agreement between the parties
- end of the contracted period
- the initiative of the employee
- the initiative of the employer
- demands of third parties and conditions not dependant on the parties involved.

The notice of contract termination by either party should be in writing unless agreed otherwise.

### *Vacation*

The main vacation is 28 calendar days. For adolescents and disabled persons as well as Government and local authority employees, the extended main vacation is 35 days. Some additional vacation of 5 to 14 days is given to workers in mines, health damaging environments and other special conditions. Both the contract and the collective agreement can provide additions to holidays.

### *Maternity leave*

To parents, additional maternity leave, adoption leave, childcare and further child vacations are granted. The official maternity leave is 70 calendar days before and 56 days after childbirth. During this period, the mother receives her last six months' average wage to the extent of 100 percent. This amount is paid at the beginning of the period. In case a child less than a year old is adopted, the adopter is granted 70 days of adoption leave and receives full pay. The right to child care vacation remains until the child is three years of age. The father or any other person who is legally taking care of the child can also use it. During this time, expulsion due to personnel reduction is prohibited.

### *Sickness*

In case of sickness, the employee can be given up to four months of paid vacation. The gross wage during this period is, 60 or 80 percent of his/her last six months' average salary depending on whether the employee is registered in a hospital or not. After the period of four months, a medical examination has to either extend the paid sick leave or confirm him/her as a disabled person.

### *Payment for overtime*

Employers are responsible for overtime payments, while maternity leave and sickness benefits are compensated from social security. Extra payment for every case of overtime work must not be less than 50 percent of the rate of hourly pay. Work during holidays could be compen-

sated either by offering time off, or by extra remuneration of at least 50 percent of the wage rate. Work on public holidays has to be compensated at a double rate. Additional pay for working in the evenings (from 6 PM to 10 PM) or at night (10 PM to 6 AM) must be remunerated with at least 10 and 20 percent, respectively, of the hourly pay of the employee.

### *Social security*

Social tax is paid by employers operating within the territory of Estonia on all payments in cash and in kind made to individuals at a rate of 33% of total payments.

### *Trade Unions*

The major trade union organisation in Estonia is the Estonian Association of Trade Unions, which represents the interests of industrial, service, trade, public and agricultural employees. The activity of trade unions has primarily occurred in three areas: participating in the drafting of laws and introducing proposals to the Parliament, trilateral negotiations with the government and employers, consulting their members. However, Estonia has managed to sustain harmonious labour relations, and labour disputes are generally resolved through direct negotiations between employers and employees.

## **Inward investment incentives**

### *Sectoral opportunities/priorities*

By the end of 1999, the cumulative stock of foreign direct investments amounted to over 38 billion kroons (approx. USD 2.44 billion). Over the last years, income has been increasingly reinvested as well as taken the form of new investments into new companies. As far as sectoral breakdown is concerned, 27 percent of FDI has been invested in manufacturing. This sector is followed by trading and financial services, with 23 and 22 percent of the total respectively. The share of financial services in the FDI stock has come up from 7.3 percent in 1996 to 23 percent in 1999. This dramatic increase can be attributed to the sale of two major Estonian banks to the Swedish SE Banken and Swedbank.

Transportation and telecommunications have attracted 10 percent of the foreign direct investment stock. Estonia's favourable geographical location, good infrastructure and major privatisation projects underway provide excellent bases for increasing foreign capital inflows into this sector. In the coming years, infrastructure and public utilities will offer good opportunities for foreign investors. Until now the sector has been subject to regulation both in terms of required licences and price controls.

The Scandinavian countries are the biggest source of foreign direct investment in Estonia. Sweden tops the list of donor countries with 40 percent of the total, followed by Finland with 30 percent. The USA, Norway and Denmark all have a 4 percent share of the foreign direct investment stock.

Estonia has no exchange controls or restrictions on foreign investment. The amount of foreign capital invested in Estonian business enterprise is unlimited and companies can be in full foreign ownership. Foreign companies enjoy equal rights with local ones. To carry out activities

in certain areas a license must be obtained notwithstanding the origin of an operator. These specific areas are: mining, public utilities, reconstruction of railways, airports, ports and dams, long-distance telecommunications, retail sales of pharmaceuticals, production of alcohol and tobacco, gambling, banking. The basic rules for licensing are included in the Regulation of the Estonian Government from May 8, 1990 on Issuing Statutory Activity Licenses.

#### *Inward Investment Incentives*

In general, there are no foreign investment specific tax holidays. It is, however, possible to get tax exemptions depending on the nature of business and region where the investment has been made.

In October 1997, the Parliament adopted a law of amendments to the income tax law allowing the Government to determine regional investments subject to tax concessions. Companies can deduct expenses made to acquire or upgrade fixed assets and equipment from taxable income. According to the Government's regulation from January 1998, the tax concession applies provided that assets were acquired or upgraded in a region other than the cities of Tallinn, Keila and Saue and the districts of Harku, Jõelähtme, Rae, Saku, Saue and Viimsi.

Estonia has investments promotion and protection agreements with the following countries:

<i>Country</i>	<i>Effective from</i>
Austria	October 1995
Belgium	December 1996
China	June 1994
Czech Republic	July 1995
Denmark	February 1993
Finland	December 1992
France	September 1995
Germany	January 1997
Greece	July 1998
Israel	May 1995
Italy	To be ratified
Latvia	May 1996
Lithuania	June 1996
Netherlands	September 1993
Norway	June 1992
Poland	August 1993
Spain	July 1998
Sweden	May 1992
Switzerland	August 1993
Turkey	To be ratified
Ukraine	July 1995
United Kingdom	December 1994
United States of America	February 1997

Double taxation avoidance treaties have been signed with the following countries:

<i>State</i>	<i>Effective from</i>
--------------	-----------------------

Canada	December 1995
Czech Republic	May 1995
Denmark	December 1993
Finland	December 1993
France	To be ratified
Germany	December 1998
Iceland	November 1995
Ireland	To be ratified
Italy	To be ratified
Latvia	December 1993
Lithuania	December 1993
Moldova	June 1998
Netherlands	November 1998
Norway	December 1993
Poland	December 1994
Russia	July 1998
Sweden	December 1993
Ukraine	December 1996
United Kingdom	December 1994
USA	To be ratified

## **Banking system**

The wide fluctuations in interest rates and the volatility on the domestic and international financial markets have affected the financial sector, but its development has not gone off course. Even the voluntary or forced closure of some of the banks does not seem to have dented the general confidence in the financial sector. Deposits by residents briefly fell at the end of 1997, but then continued to grow. Also, the consolidation of the financial sector has led to the emergence of banks that are not only larger but also stronger, and thus in a better position to channel savings to productive investments.

## **Taxation**

Current Estonian Tax Legislation was enacted during the first phase of the transition reforms. The most important pieces of tax legislation - the new Law on Taxation, Law on Income Tax and the Law on VAT - came into effect in 1994. The Estonian tax system with its flat 26% rate that applies to individuals and 0% rate that applies to corporations is one of the most liberal tax regimes in the world.

### *Principal Taxes*

The system of taxation is described in the Law on Taxation. The existing state taxes are:

- income tax
- value-added tax (VAT)
- social tax (social security contributions)
- excise taxes on:

- tobacco
- alcoholic beverages
- motor fuel
- motor vehicles
- packages
- gambling tax
- land tax.

Currently, Estonia does not impose any customs duties or gift or estate taxes. Various transactions may be subject to payment of state fees (stamp fees).

Local governments have the authority to impose local taxes, but effectively in only a few municipalities have all or some of the following local taxes been introduced: sales tax, boat tax, tax on advertising and commercials, tax on closure of streets and roads, motor vehicle tax and tax for keeping the animals.

### *Income Tax*

The general rule individual income tax is to aggregate the income from all sources and then subject it to a single 26% flat tax rate. Corporate income the tax rate is 0%.

Estonian residents (individuals having a permanent home in Estonia or staying in Estonia more than 183 days in a calendar year and companies formed under Estonian laws) are subject to income tax on their worldwide income. Credit is given for taxes paid abroad. Non-residents are subject to Estonian tax on their Estonian source income.

The relatively low tax rate in Estonia is however balanced by the small number of allowable deductions for individuals.

The taxable income of a company is calculated by adjusting its net profit as shown in its income statement (profit and loss account) in accordance with the legislation. Capital gains are added to taxable income and taxed at the ordinary income tax rate.

Dividends paid out to resident and non-resident shareholders are subject to a tax at the gross-up rate of 26/74 of the amount of the dividend. This tax may be credited against the corporate income tax due in subsequent periods. Dividends to non-residents who own less than 25% of the share capital of the distributing company are also liable to an additional 26% withholding tax.

Losses may in general be carried forward for up to five years; capital losses derived from the disposal of land and securities may be set off against similar gains but without time limit.

Estonian tax laws do not currently include any restrictions on the deductibility of interest payments nor contain thin capitalisation or CFC rules. A general transfer pricing anti-avoidance provision applies to transactions between related resident and non-resident persons.

A company liable to tax is required to file an annual tax return together with annual accounts to tax board within the six month from its accounting date. The tax year normally runs from January 1 to December 31. Companies with fiscal years different from the calendar year may

account for tax on the basis of such fiscal year. (See below for further information on this subject).

Tax is paid in equal monthly instalments, which are calculated as 1/12th of the corporate income tax calculated in the previous tax return.

#### *Income tax incentives*

From 1 January 1998, new income tax incentives were introduced for the underdeveloped regions of Estonia. Companies are able to deduct from their taxable income the costs related to the acquisition and improvement of tangible fixed assets (except assets with the value of less than EEK 5 000 and motor vehicles), which are situated in regions listed by the Government. This regional tax incentive is scheduled to remain in force until 31 December 2007.

#### *Value Added Tax*

Estonian VAT corresponds to the VAT of European countries and is based on the principle of tax credit. VAT is charged at the rate of 18% (exceptional rates of 0% and 5% apply to certain goods and services) unless the goods or services are outside the scope of VAT or exempt from VAT. The tax rate for exports is zero. The VAT treatment for the export of services is subject to the list of services established by the Ministry of Finance.

Taxable persons are individuals and legal entities having a taxable supply as a result of conducting business. With respect to importation, an importer is a taxable person, whether or not he is engaged in a business. Taxpayers with annual supplies of less than EEK 250,000 are not required to register for VAT purposes.

Foreign legal entities are generally not registered for VAT purposes. However, branches of foreign entities must register in the same manner as local legal entities. Provided that the foreign country grants reciprocal rights to Estonian residents, Estonian VAT is refunded to non-resident taxable persons who purchase taxable goods and services in Estonia.

#### *Social Tax*

Employers registered in Estonia must pay social tax on all payments made to employees, except on those specifically exempted by law. In the case of an individual engaged in business and registered with the tax authorities, social tax is paid by the individual. Fringe benefits are included to the definition of taxable payments. Currently only an employer and an individual engaged in business are liable to make social security contributions. An employee is not required to pay social tax.

The rate of social security contributions is 33% (20% for social security and 13% for health insurance).

#### *Other Taxes*

Land tax is levied on the taxable value of all land (other than that which is specifically exempt) based on an official valuation. Taxable persons are the owners and for an initial period up to 31 December 2000 also certain users of the land. The annual land tax rate varies be-

tween 0.5% and 2.0% of the taxable value of the land. The council of the local authority establishes the land tax rate.

Excises are levied on tobacco, alcoholic beverages, motor fuel, motor vehicles and packages.

A customs procedure fee of 0.5% on goods imported or exported was replaced, with effect from 1 April, 1995, by a flat state fee of EEK 200 on each customs declaration submitted by a legal person. Currently, there are no other custom duties in Estonia.

#### *Tax treaties*

Estonia has effective tax treaties with Belarus, Canada, Czech Republic, Denmark, Finland, Germany, Iceland, Ireland, Latvia, Lithuania, Netherlands, Norway, Poland, Sweden, Ukraine and the United Kingdom. Treaties with China, France, Italy, Moldova and the USA have been signed, but have not yet become effective.

Estonia has comprehensive withholding taxes on payments made to non-residents. Under the double tax treaties a significant reduction in the rate of withholding tax is available. In order to apply the lower tax treaty rates, application form TM2 ("Application concerning relief from Estonian tax withheld at source") must be submitted to the tax authorities. Along with the application a non-resident recipient must present the Estonian payer with a certificate confirming his residency along with their data required by the form.

#### **Market development, market conditions**

Privatisation - based on the privatisation law passed in 1993 - has advanced further, including in infrastructure. Competition is strong, notably because of the liberal trade regime. At the end of 1997, almost 80% of industrial production originated in the private sector.

The positive results and trends of Estonian industry and economy in general would suggest that the government's strategy to create a market-based business environment is proving successful. In particular, since 1997 there have been very significant increases in industrial output, exports of industrial products, labour productivity as well as in the number of new companies in the manufacturing sector. Restructuring the food processing industry remains however a key issue in the restructuring of the agricultural sector. The main challenge lying ahead Estonia in the industrial sector is the enlargement of the export base. This would be achieved by improving both the value added and quality standards of production at competitive costs. To that end new skills need to be developed, which requires adequate allocation of financial and human resources for education and quality policies.

Estonia continues to be a functioning market economy. It has strengthened the institutions of a market economy and improved the legal environment for market participants. The authorities have been able to adopt the correct economic policy measures when required although prudent macroeconomic management is needed to limit the risks associated with its large external imbalances. However, there is a need for further progress in land privatisation, in the liberalisation and adaptation of prices and in the strengthening of the regulatory framework of financial activities and capital markets.

## **Environmental regulations**

Since 1997, Estonia has adopted an important number of legal acts, with a view to aligning its legislation with the *acquis* in the field of environment, including the environmental impact assessment directives, the waste framework directive, the hazardous waste directive, the packaging and packaging waste directives, the emission from motor-vehicles directives, the nitrate directive and the drinking water directive. Estonia has made good progress generally in the approximation of legislation.

## **Intellectual and Industrial Property Rights**

Amendments and secondary implementing legislation, to the Trade Marks Act and the Patent Act have been adopted. The latter meet the requirements of WTO Agreement on trade of intellectual property. The parliament has ratified the Madrid Protocol and accession was made in December 1998. In November 1997 Estonia submitted its application to accede to the Munich Convention and has obtained observer status at the European Patent Organisation. The Industrial Design Protection Act and implementing regulations have also been adopted but amendments to the Copyright legislation are still needed. Weaknesses in the administrative and institutional capacity of Estonia to ensure effective implementation of copyright legislation still remain.

## **Export/import formalities**

Most goods can be imported without restrictions. There are restrictions for some, such as weapons and dangerous substances. Agricultural products from third country are the only products with import tariffs. Agricultural products with origin from EU or origin from countries with free trade agreement with Estonia are free from import duties.

Goods imported into or exported from Estonia must be cleared through Estonian customs where the following duties and taxes are collected:

- VAT, which is 18% on the CIF-value
- Customs procedure fee, 200 EEK

On some goods (tobacco, tobacco products, motor fuel, fuel oil, cars, motorbikes and drink packaging) there is also an excise duty.

A license is required for importing or exporting certain goods. Licenses are obtained from the Ministry of Economy.

The documentation requirements are

- signed commercial invoice
- certificate of origin; goods certificate EUR.1 or invoice declaration is needed if tariff advantages should apply according to the EU Europe agreement with Estonia, or any other free trade agreement.

- sanitary certificate issued by health- or plant protection authority in the exporting country; required for import of live animals, meat, other food products, feedstuff, live plants and parts of plants.

More information on customs procedures can be found on

<http://www.vm.ee/eng/index.html>

<http://mkaccdb.eu.int/wtdtar/wtdtar.pl>

[http://www.customs.ee/docseng/bluebook/contents\\_2.htm](http://www.customs.ee/docseng/bluebook/contents_2.htm)

## **Recommendations and hints**

The simplest way for EU exporters to establish on the Estonian market is to sell directly to end-user or retailer. Most companies have a purchasing department led by a *Purchasing manager*. When contacting an Estonian company you should start as high as possible in the organisation to be able to find out who has the decision power and who is the main responsible. Personal contacts are very important.

Most foreign companies established in Estonia have a local agent or representative. One exclusive agent/distributor is usually appointed to cover the entire country. Estonian importers often represent several different product lines. In selecting a representative, the exporter should check whether that company handles competing products. It is also possible to have an agreement based on sales on commission or to establish your own sales company.

Privately-owned wholesale and trading houses are particularly strong in certain specialised sectors, such as electronics, electrical components and instruments, pharmaceuticals and health care products, technical products and machinery, raw materials and chemicals.

Estonia as a market is rather small with price sensitive residents. Patience, humility and long-term objective are all important parts of a possible success here. Too many Europeans arrive here thinking they are first with unique ideas. Without contacts with any organisation with a broad business network, it is very hard and time consuming to establish on the Estonian market.

## **Negotiations, payment**

Estonia has the strongest, most developed banking system in the Baltic States. Foreign transactions are done through the SWiFT system and the banks have full IT support for their activities. The country has adopted a universal banking model that allows banks to participate in other financial activities including operating, leasing, insurance and brokerage firms. Several mergers has reduced the number of banks. The largest are *Hansapank*, *Eesti Ühispank*, *Nordea Bank*, *Sampo Bank*. All these can handle EUR.

Financing and guarantees for exports are provided by the Government-owned Foundation for Export Credits and Guarantees. Depending on the nature of the goods exported and on the risk of the trading partners, a portion of the export costs must be provided by the company in question. In addition to government activities, commercial banks provide financing for ex-

ports, when possible, with guarantees. The banks advice their customers on bank loans well as on loans granted by other credit institutions.

### **Useful addresses**

Euro Info Centre EE881  
Estonian Chamber of Commerce and Industry  
Toom-Kooli, 17  
EE-0001 Tallinn  
Estonia  
Responsible: Mr. Tiit Romulus  
Tel: +372 6 448079  
Fax: +372 6 460245  
E-mail: [tiit@koda.ee](mailto:tiit@koda.ee)  
Web-site: <http://www.koda.ee/euroinfokeskus>

Euro Info Centre EE882  
Narva Business Advisory Services Foundation  
Peetri, 1  
EE-20301 Narva  
Estonia  
Responsible: Mrs Anne Veevo  
Tel: +372 35 60 027/60 136  
Fax: +372 35 60 674  
E-mail: [eic.narva@mail.ee](mailto:eic.narva@mail.ee)  
Web-site: <http://www.kodu.neti.ee/~nbas>

Bank of Estonia  
Estonia pst. 13, 15095 Tallinn  
Phone: +372 6 310 911  
Fax: +372 6 310 836  
E-mail: [info@epbe.ee](mailto:info@epbe.ee)  
<http://www.ee/epbe/en>

Commercial Register  
Endla 10, 10122 Tallinn  
Phone: +372 6 103 151  
Fax: +372 6 103 153  
Email: [eer@eer.ee](mailto:eer@eer.ee)  
<http://www.eer.ee>

Estonian Investment Agency  
Roosikrantsi 11, 10119 Tallinn  
Phone: + 372 6 279 420  
Fax: + 372 6 279 427  
E-mail: [info@eia.ee](mailto:info@eia.ee)  
<http://www.eia.ee>

Estonian Chamber of Commerce and Industry  
Toom-Kooli 17, 10130 Tallinn  
Phone: +372 6 314 065  
Fax: +372 6 313 744  
E-mail: [koda@koda.ee](mailto:koda@koda.ee)  
<http://www.koda.ee>

Estonian Taxpayers Union  
Tõnismägi 2-3110, 10122 Tallinn  
Phone: +372 6 307 480  
Fax: +372 6 307 480  
E-mail: [emliit@online.ee](mailto:emliit@online.ee)  
<http://www.maksumaksjad.ee/>

Estonian Translation and Legislative Support Centre  
Tõnismägi 8, 10119 Tallinn  
Phone: +372 6 935 100  
Fax: +372 6 461 075  
E-mail: [keskus@legatext.ee](mailto:keskus@legatext.ee)  
<http://www.legatext.ee>

Ministry of Economic Affairs  
Harju 11, 15072 Tallinn  
Phone: +372 6 256 304  
Fax: +372 6 313 660  
E-mail: [kantselei@mineco.ee](mailto:kantselei@mineco.ee)  
<http://www.mineco.ee>

National Tax Board  
Endla 4, 15176 Tallinn  
Phone: +372 6 267 600  
Fax: +372 6 267 611  
E-mail: [maksuamet@ma.ee](mailto:maksuamet@ma.ee)  
<http://www.ma.ee>

Statistical Office of Estonia  
Endla 15, 15174 Tallinn  
Phone: +372 6 259 202  
Fax: +372 6 259 370  
E-mail: [stat@stat.ee](mailto:stat@stat.ee)  
<http://www.stat.ee>

### **Internet links**

- Bank of Estonia:
  - [www.ee/epbe/en](http://www.ee/epbe/en)
- Estonia Banking Association:

- [www.pangaliit.ee](http://www.pangaliit.ee)
- Estonia Chamber of Commerce and Industry:
  - [www.koda.ee](http://www.koda.ee)
- Estonia Investment Agency:
  - [www.eia.ee](http://www.eia.ee)
- Estonia Ministry of Foreign Affairs:
  - [www.vm.ee](http://www.vm.ee)
- Estonia Privatization Agency:
  - [www.eea.ee/english/indexe.htm](http://www.eea.ee/english/indexe.htm)
- Estonia State Web Centre
  - [www.gov.ee/en/](http://www.gov.ee/en/)
- Estonia Trade Council:
  - [www.ee/ETC](http://www.ee/ETC)
- Estonian Ministry of Economic Affairs
  - [www.mineco.ee](http://www.mineco.ee)
- Ministry of Finance of Estonia:
  - [www.fin.ee](http://www.fin.ee)
- The Parliament of Republic of Estonia:
  - [www.riigikogu.ee/englishindex.html](http://www.riigikogu.ee/englishindex.html)
- Statistical Office of Estonia
  - [www.stat.ee/wwwstat/eng\\_stat](http://www.stat.ee/wwwstat/eng_stat)
- Tallin Stock Exchange:
  - [www.tse.ee](http://www.tse.ee)
- The World Bank
  - [www.worldbank.org](http://www.worldbank.org)
  - [www.worldbank.org/html/extdr/regions.htm](http://www.worldbank.org/html/extdr/regions.htm)

## Statistics

Change of gross domestic product at constant prices  
3<sup>rd</sup> quarter 2000 in comparison with 3<sup>rd</sup> quarter 1999 7.0%

Change of consumer price index  
Oct 2000 in comparison with Oct 1999 5.7%

Change of producer price index  
Oct 2000 in comparison with Oct 1999 6.0%

Change of construction price index  
Oct 2000 in comparison with Oct 1999 2.8 %

Average monthly gross wages and salaries  
EEK 1999 4418

Trade balance, million EEK,	1999	-1170.0
	1998	-1542.4

<i>GD Product by years</i> months)	1995	1996	1997	1998	1999
Current prices (million kroons)	40705.1	52445.9	64323.7	73325,3	75360.2
In 1995 constant prices (million kroons)	40705.1	42297.0	46789.0	48995,7	48468.5
Change from previous year, %4.3		3.9	10.6	4.7	-1.1
<i>Unemployment rate, %</i> (ratio between the employed and the labour force)	9.7	10.0	9.7	9,9	12.3
<i>Export, quantity, 1000 t</i>	5311	5218	8173	11317	9132
<i>Export, value, million USD</i>	1840.4	2077.0	2931.3	3243.1	2937.7
<i>Import, quantity, 1000 t</i>	5658	4988	7151	7644	7638
<i>Import, value, million USD</i>	2546.2	3224.1	4436.8	4786.1	4107.7