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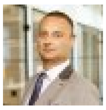
Donations to Ukraine and VAT 1/11/22



Senior Manager, Tax Reporting, Accounting and Strategy, PwC Latvia
Juris Boiko

As the war in Ukraine goes on, many companies have unselfishly donated to Ukrainian residents and to Ukrainian refugees having crossed the EU border. Does the current tax regime encourage donations? And how has the Latvian government responded to the present situation?

The Latvian VAT system is not designed to encourage donations. The VAT Act so far prescribed no relief on donations. Donations (gifts) were treated as taxable supplies, i.e. personal consumption.[1] Thus, if input tax had been deducted on donated goods, then 21% VAT had to be charged and paid to the government at the time of donation. The taxable amount was the acquisition or production cost of the goods.

Low-value gifts worth up to EUR 15 excluding VAT per person for the calendar year were so far the exception. There was no requirement for charging VAT on a low-value gift and the right to deduct input tax on the gift remained. The State Revenue Service (SRS) had expressed support for EU food donation policies providing for the member states to create conditions encouraging food donations, admitting that under certain conditions, companies might revalue their food inventories before a donation for VAT purposes and write them down, or write them off altogether. So VAT might be charged on the revalued amount and not the acquisition cost of goods. The procedures for measuring the book value of inventories, revaluations (write-downs) and wastage write-offs should be described in the company's accounting policy. Yet this practice so far applied to food only, with any write-down requiring a good reason.

The VAT directive[2] provides for an exemption on supplies of goods to approved entities that export those goods from the Community as part of their humanitarian, charitable or educational activities outside the Community. The Latvian VAT Act did not contain such a provision so far. The amendments of 10 March 2022 to the Support for Ukrainian Civilians Act (section 8.1) provide for a zero-rating on goods a registered taxable person supplies according to a contract, a statement of delivery and acceptance, or another supporting document, free of charge to a public benefit organisation that –

1. exports the goods from the EU as part of humanitarian aid and charitable donations to provide general support to Ukrainian residents;
2. supplies the goods to an entity recognised by another member state, which passes them as humanitarian aid or charitable donations to Ukrainian residents.

What does the new provision mean for taxable persons? Meeting these conditions results in personal consumption being zero-rated (instead of 21% VAT) and the entitlement to the deducted input tax stands. This provision is designed specifically to encourage donations to Ukrainian residents and applies from 24 February 2022.

We need to be careful in meeting the conditions for a zero-rating. Latvia has tried to follow the VAT directive's restrictions on donations quite precisely. Section 8.1(1) of the Support for Ukrainian Civilians Act provides for the need to pass a donation to a public benefit organisation – for export and not for assistance to refugees having crossed the EU border. A contract, a statement of delivery and acceptance, or another substantially similar document can serve as a supporting document for such transactions. Also, in the light of amendments to the Cabinet of Ministers' Rule No. 17 of 3 January 2013, *Application of*

Provisions of the VAT Act and Certain Requirements for Payment and Administration of VAT, you have to prove that your donation (humanitarian consignment) is sent to Ukraine. This provision is slightly confusing because it requires that only one of the documents confirming export listed in paragraph 16 of the Rule should be filed with Customs. The donor may zero-rate the domestic supply of goods to a charity organisation. The next supply is the actual export done by the charity organisation. The SRS might still come up with comments on this issue. It would a pity if the required package of documents for a zero-rating made this provision practically impossible to apply. As for donations to an entity recognised by another member state (a public benefit organisation), there is no direct reference to use made in Ukraine. In this case a donation might also be intended for Ukrainian refugees having crossed the EU border. To date, no relief is available on donations to municipalities.

Other member states, too, have passed into their VAT law extensive provisions to encourage donations. In Poland, input tax deduction rights remain on goods donated to NGOs (including Ukrainian), municipalities and other entities for dealing with the Ukraine crisis, whether the goods are removed to Ukraine or consumed to help refugees in Poland. Donors can also claim corporate and personal income tax relief.

The EU might respond to the Ukraine crisis by jointly adopting VAT rules to encourage donations in a crisis. And a proposal for corporate tax relief on donations to people affected by the Ukraine crisis is awaiting approval from the Latvian parliament.

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[1]Section 6(1) of the VAT Act

[2]Article 146(1)(c) of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax