New CIT Act: donations (3/5/18)

We have already informed our MindLink subscribers about the new CIT Act, including new rules for donations. This article explores differences in the CIT treatment of donations before and after 1 January 2018, when the new CIT Act came into force.

The treatment before 2018

The CIT Act provides that when filing the CIT return for 2017, companies are allowed to claim 85% tax relief on donations that meet the following conditions:

1. the donation is made to state-funded institutions and organisations that have public-benefit-organisation status under the Public Benefit Organisations Act at the time of receiving the donation; and
2. the tax relief does not exceed 20% of the total tax due.

The new CIT Act

After long discussions about donation relief that took place during preparation of the new CIT Act, it is now laid down that a donor may choose one of the following three methods of relief:

1. donations equal to 5% of last year's profit are deducted from the tax base (example 1); or
2. donations equal to 2% of last year's total gross wages on which national social insurance (NSI) contributions have been paid are deducted from the tax base (example 2); or
3. 75% of the donated amount is deducted from CIT due on a declared dividend, capped at 20% of the CIT charge on the dividend (example 3).

From 1 January 2018, companies are free to decide which method of donation relief is the best in terms of CIT. It should be noted that methods 1 and 2 allow the company to include donations in its business expenses and to not pay CIT up to certain limits. These methods of relief will benefit companies that do not plan on paying dividends, companies operating at a loss, and companies with retained earnings as at 31 December 2017 (any profits earned before 2018 can be distributed without applying the new CIT model).

The third method is similar to the existing model and provides for paying CIT for the tax period (month) in which the donation was made. In the month the shareholders decide to pay a dividend, the company can deduct 75% of the donated amount from CIT due on the declared dividend, capped at 20% of the CIT charge.

The new CIT Act even allows companies to change their chosen method of donation relief within a financial year. If a company has chosen method 1 or 2 and later decides to pay a dividend, the company can calculate and pay tax by adjusting its CIT return for the tax period in which the donation was made, and claim relief equal to 75% of the donated amount.

The three methods of applying CIT are compared in the following examples:

Example 1	Retained earnings for 2017: EUR 1,000 A donation not exceeding 5% of retained earnings: EUR 50	A donation of up to EUR 50 is exempt from CIT.

Example 2	Gross wages for 2017 on which NSI contributions have been paid: EUR 10,000 A donation not exceeding 2% of wages: EUR 200	A donation of up to EUR 200 is exempt from CIT.
Example 3	Declared net dividends: EUR 10,000 CIT charged on the dividend: EUR 2,500 Donation: EUR 200 CIT charged: EUR 200 / 0.8 x 20% = EUR 50	If 75% of the donation (75% of 200 = 150) does not exceed 20% of the CIT charge on net dividends (20% of 2,500 = 500), then 75% of the donation can be deducted from the CIT charge.

The new CIT Act lays down a number of conditions the company must meet before it can claim donation relief. The statutory requirements increase the administrative burden on the process that allows a payment to be treated as a donation. To claim donation relief, when filing its CIT return via the Electronic Declaration System, the company will have to file documents confirming the following facts:

1. the donee is resident in an EU/EEA country (in the form of a statement);
2. the donee has public-benefit-organisation status in its country of residence;
3. the donee is operating in a public benefit area that provides a significant benefit to the public; and
4. at least 75% of the donated amount has been used for public benefit purposes.

The CIT Act does not specify what documents a company should file with the State Revenue Service to confirm that it meets requirements 3 and 4. We believe that a contract giving details of these statements could serve the purpose.

It is important to note that donation relief cannot be claimed if the donee publicly uses the donor’s brand. However, if the donor’s name and logo do not occupy more than 1/20 of the text area of the list of donors, the company can still claim donation relief.

Finally, unlike the old model, which prohibited taxpayers from having a CIT debt exceeding EUR 150 on the 1st day of the second month of the tax period (that is 1 February in companies having a financial period that coincides with the calendar year), the new model prohibits such a debt on the 1st day of the tax period (month) in which the donation was made.