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Q & A

On

TAX & CUSTOMS ISSUES RELATED TO MACEDONIAN NONPROFIT ORGANIZATIONS

1. What are the major taxes and customs duties applicable to NPOs?

Once duly registered with a competent court register, NPOs gain the legal personality attribute. Thus, they automatically are subject to all fiscal instruments applicable to legal persons in general, with the exceptions regulated by law. NPOs are liable for profit tax at entity level, personal income tax and social contributions for their staff (except for volunteers), property tax, gift and inheritance tax, VAT on purchases of goods and services, customs and other import duties, as prescribed by tax and customs laws and secondary regulations. (See: Annex 1 List of relevant fiscal laws)

2. Where can I get more information on filing requirements and tax liabilities for my NPO?

The Ministry of Finance and the Public Revenue Office have informative services, booklets, free info lines, and web sites where you may get the information that you need.

3. Are we obliged to prepare financial plans and submit annual reports?

Yes, according to the Law on Accounting and the secondary regulation all legal persons must file an annual report with the ZPP (Payment Operations Service). Financial planning is at free disposition to the entities, but is strongly advisable for many reasons: better utilization of resources, more efficient management, more successful completion of goals and objectives of the NPO, etc. A professional, certified accountant best does the preparation of the annual accounts. This is especially important when NPO engages in economic activities and generates income, and is involved in importation or exportation of goods and/or services. Note that failure to comply with fiscal laws may be treated as tax evasion and even criminal penalties may be imposed to the executives or the board members of the NPO.

Moreover, bear in mind that financial planning and the main Law on Associations of Citizens and Foundations prescribes annual reporting, and the adoption of these important documents is in the statutory powers of the NGO Assembly.

4. Is it better to do the annual financial statements by ourselves or should we engage a certified accountant? Why?

Yes, the latter keeps you “on the safe side” although it will add to your running expenses. You are always better off when you have an accountant to do your bookkeeping and accounting. Of course, you need not employ one, but hire him for a specific task under contract for professional services.

5. My NPO is compelled to charge membership fees in order to cover operating expenses. Is income from fees taxable with profit tax?

NGOs are liable under the provisions of the Law on Profit Tax as any other legal person. Apart from the explicit statutory tax-exemption for entities employing disabled individuals, the law provides one possible legal relief from taxation of NGO income deriving from membership fees. Namely, tax-exempt is any type of income that is strictly designated for carrying on the activities of the legal person – the tax payer (from budgets, funds etc.). That type of income is not included in the NGO tax base for the purposes of profit tax. In our view, although LPT fails to explicitly mention membership fees, they, by their innate nature, obviously fall within the category of designated income, and subsequently ought to be treated as tax-exempt.

6. My NPO just received a sizable donation from a foreign organization. Is such a donation subject to tax? Do we have to report the donation to the competent authorities at the State Revenue Office?

The answer is no. The purpose of donated monies is fulfilling the statutory objectives of the NGO and donation is a type of income that is explicitly regulated by the LACF as legitimate source of income for

NGOs. No special reporting requirements are needed, but beware that according to the existing foreign payment operations law, you will receive the MKD value of the donation at the official rate published by the Central Bank of RM. That's because domestic entities are not allowed to hold foreign currency accounts in their name.

7. Our NPO needs resources for fulfilling the statutory goals and objectives. We are afraid the funds we raise from membership fees will not meet this goal. Can we engage in commercial activities to improve our financial sustainability?

Macedonian NGO'S are not allowed to engage in economic activities directly, but only through a separately established commercial subsidiary company. It is important to stress that this legal possibility must be reflected in the by-laws/statutes of the NGO. The company (which has to be set up in a legal form of either Ltd. or Inc. company) has got all attributes of a regular business entity regulated by commercial law, and is consequently being taxed like all business organizations.

This is a rather rigorous legal approach, given that the majority of CEECs allow some tax benefits at least for part of that income, under terms and conditions prescribed by law. Most often exempt from tax is the portion of the income used strictly for performing the activities of the NGO in question, or income related to it's main activity and purpose.

8. Is the rate of profit tax in our country very high?

Luckily, much lower than in other countries in the region, or in EU member countries. Macedonian profit tax rate is the lowest in the region and is set at 15% for all legal persons irrespective of size and activity, fact that may partially offset the negative effects of taxing income derived from economic activities.

9. How are we supposed to pursue that economic activity? Should we organize a business department within the NPO? Separate accounting, appoint general manager?

No, as is explained previously, the only legal way of performing economic activities by NGOs is through a separately established subsidiary company.

10. What is a wholly owned subsidiary?

It's a company solely owned by one by one founder, which can be a natural or juridical person, both domestic and foreign. More detailed rules concerning terms and condition for the establishment of a subsidiary ought be sought in the Commercial code. For the purpose of establishing licensed organizations (savings houses, banks, broker/dealer etc), the specific legislative requirements contained in other statutes must be taken into account.

11. How much will it cost to set up a commercial company?

The cost shall depend on the type of the company you wish to set up. The Commercial code regulates that issue, thus at the moment (beware for changes that are pending at year-end) statutory capital for an Ltd company is 5,000 DM in denar counter value, and for a corporation is 20,000 DM respectively. Other costs may arise from notary fees, stamp duties, registration fees, and consultant fee in case you are hiring a professional consultant or a lawyer to do the registration for you. Altogether the establishing costs may end up to be considerable, the income from the profits derived from this *economic activity* may very well secure the stable and sustainable existence and growth of your NGO, and justify the initial costs.

12. We cannot afford to pay-in the statutory capital for that company in-cash. Can we make contributions in-kind?

Contributions in-kind are allowed, generally in *res and in rights/royalties*. Contribution in labor and in personal services cannot qualify as equivalent for start-up capital of the company.

13. What if we set up a joint stock corporation and are the only shareholder? The Commercial Code requires at least 2 shareholders for AD. Does it mean we have to find a partner for this enterprise?

It is unclear which statute will prevail in this particular case, but we would strongly recommend that you choose to establish a Limited liability company as your subsidiary, for reasons of legal and factual simplicity and modest compliance requirements. The joint stock corporation is incomparably more formal, complex and with rigorous compliance requirements.

14. How shall our company be taxed? Are there any legal benefits and incentives if we use profits for developing our activities?

For now, no legal tax incentives are available concerning the profits of your subsidiary company. Notwithstanding the fact that the profits will be used for improving the activities of your NGO, they will be taxed as ordinary business income at 15% rate.

Comparatively, the so-called “related income” is tax-exempt; unlike “non-related income” that is subject to the normal tax rules. The concept of related income has one flaw: to determine the fine line between the related and unrelated income, which often times is a Tantalus task.

15. One of our members is getting married. He is not rich, and wonders if the NPO can lend him some money?

Lending monies to members is a sensitive issue. Since its obviously beyond the objectives and aims of the NPO it such and similar practices ought be avoided. If however there is a valid decision by the Managing Board for a loan to a member, there must be a written contract between the parties. Special attention must be paid to the interest on the loan, bearing in mind “arm’s length principle”, transaction between related parties. Generally accepted rule is that the interest should correspond to the market rate for similar financial loans.

16. My NPO had an excellent financial year. We are thinking of investing some money in securities. Is that legal for NPOs?

NGO’s may generate income from investments directly. Dividends from their subsidiary company are taxed at that company level with profit tax and is then received by the recipient entity. Of course, NGO may invest in stocks of various companies and generate income, which will not be

included in the tax base, if it has been taxed once at company level and if that company is resident of RM.

Dividends from non-resident companies may not enjoy this incentive, and will be taxed twice (second time at recipient level) unless a Double-Taxation Treaty between the countries is in place.

NGO's may receive interest from bank deposits and from debt instruments (government bonds, treasury notes etc.) that is taxable as ordinary business income, except interest from government bonds, which is tax exempt. Capital gains from sale of securities and immovable property are included in tax base at the amount of 70% and taxed as ordinary income. Capital losses may be off set by capital gains and the remaining losses may be carried-forward up to three years.

17. The stock markets are in a downturn. Maybe it's wiser to buy an office building downtown, and rent it. That way our NPO will have steady and sufficient income for pursuing our humanitarian purposes. What tax issues are relevant in that situation?

Income from rented real estate may be more stable and predictable than the security prices on the Macedonian Stock Exchange, especially since there are only a few companies listed with the official markets which is not much of a choice anyway.

18. We are buying government bonds, they are tax-free. What other assets or investments have preferential tax treatment for NGO's?

The latest amendments of the Personal Income Tax Law (8/01) provide for exemption from taxation of several types of interest: from government loans, a vista bank deposits, savings deposits, bonds issued by central government and municipalities. This benefit is in favor of individual resident taxpayers, and it is unclear weather the same treatment is extended to legal juridical persons (NGO's inclusive), since Profit Tax Law is not explicit on the same issue.

19. My NPO is founded for the purpose of raising funds to help Roma children. Our By-laws state that fundraising is a major objective of our organization, and that all funds must be used for

clothing, books and education. Our Board contemplates three possible ways of collecting money for that purpose:

- **one time fund raising campaign by selling T-shirts with motives from Roma children drawings;**
- **setting up an exhibition at a private mall with posters on the statute and living conditions of Roma population, and collecting contributions from customers;**
- **opening a small gallery shop for hand made works by Roma people as well as other goods. The shop would be open regular hours.**

What are the tax consequences of the three examples?

The first two situations where you raise money through donations and sporadic activities - occasionally putting up exhibitions where you collect contributions – are tax-exempt. The third case, however calls for commercial activity carried on regular basis, and the profits there of will be taxed at 15% tax rate.

20. An international organization decided to donate humanitarian aid to my NPO. Are we liable for customs and for VAT on that import?

Your NPO is not liable for VAT in this particular case, provided that you are a registered domestic humanitarian, NPO and NGO (Art. 27,10 of Law on VAT)

21. My NPO is engaged in helping abandoned pet animals. For that purpose we purchased animal food on which we paid VAT. Since the transaction was done in line with the main nonprofit goal of our organization, are we entitled to a VAT rebate?

VAT rebate is possible only for entities, which are registered VAT taxpayers. It is tricky weather this purchase of animal food should be done by a separate company or directly. In case of direct purchase by NPO that is not registered for VAT, there shall be no VAT rebate. This could be possible in case separate commercial company has been set up and is registered for VAT (has annual turnover in excess of 1.000.000 denars).

22. My NPO is planning to organize a seminar with registration fee, in order to cover the incurred costs. Are we compelled to charge VAT on the individual registration fee receipts?

Educational, training, upgrading of knowledge, and similar services are generally VAT exempt, but not if organized by NPOs and charged with entrance fee. Therefore, VAT should be calculated and charged.

23. In my NPO only volunteers have been engaged so far. However, as our activities grow we are considering hiring full time workers. Are we liable to pay income taxes and social security contributions for our workers?

The employees in NPOs have equal treatment as workers in other sectors of economy and/or government, with respect to their rights and duties under labor law and Collective contracts. Accordingly, employers are responsible for calculation and withholding of personal income tax and social security contributions prior to each distribution of wages and/or other remuneration, in accord to law. This solution corresponds to good international practices.

24. I wish to donate one Macedonian NPO. Will my donation be exempt from my personal income tax? What about gift tax of the NPO receiving the donation?

Unfortunately, individual philanthropists are not entitled to deduct from their taxable income the amount of donation they made to a NPO. The existing Law on personal income tax does not provide any tax incentives for encouraging gifts to associations of citizens and foundations.