

The Percentage tax designation considered in Croatia: What difference it can make? (November 2016)

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Introduction

The introduction of percentage tax designation mechanism in Croatia has never been properly considered in the form of a draft legal / policy proposal, although it has been frequently mentioned in many discussions on various policy options for creating more enabling environment for civil society development in Croatia. More specifically, during the discussions on the draft Law on Public Benefit Organisations in 2010, and following experiences of other countries of Central and Eastern Europe, the possible introduction of various tax benefits was proposed, including 1% tax designation mechanism, as an important incentive for applying for the status of public benefit organisations. Nevertheless, due to still widely felt consequences of economic crisis and budgetary cuts, but also due to the lack of solid costs and benefit analysis of the proposed draft law and related tax legislative changes, it was not accepted. The prospects of granting a right to a taxpayer to designate percentage of paid income tax to a non-profit, non-governmental organization or other type of public benefit entity has been always considered as desirable policy option by NGOs, but never received due attention of expert and academic community. The purpose of this text is to discuss possible outcome and effects of introducing percentage tax designation mechanism on sustainability of civil society in Croatia, and offer some recommendations to policy makers in this regard.

In search of appropriate policy framework for discussing tax designation mechanism in Croatia

In general, the predominant policy frameworks for exploring percentage tax designation mechanism in Croatia is “public funding of NGOs”, as well as “philanthropy”, and mostly in regard to ensuring sustainability of programs and projects of NGOs, as most numerous actors or organized civil society. On the other hand, part of media and more conservative, church related organizations have sometimes mentioned tax designation mechanism within the context of “ideological fights” with watch-dog NGOs (often perceived as left-wing), questioning their legitimacy, public/citizens’ support and advocating necessary budget cuts

for them, while leaving it only to individual citizens' donations or other sources of "non-political" funding of these organizations. Since adequate framing of discussions of this innovative mechanism seems to be essential for awareness rising of key stakeholders and citizens on the purpose and benefits of percentage tax designation models, it is necessary to explore pros and cons of various policy frameworks in Croatia.

Percentage mechanism as possible model of indirect public financial support of NGOs/civil society programs?

From the end of nineties, Croatian Government has been developing a very extensive system of public funding of NGOs both at national and local levels. Every year, around 80 to 100 calls for proposals and programs of public funding of NGOs are published at central level, with approximate value of 80-90 million euros, while the amount provided for NGOs at the local level is twice as high, approximately 180 million euros¹. As the overall amount of State and local/regional public funding amounts to around 30% of the overall revenues of the NGO sector in Croatia, an increasing attention has been given to identifying alternative models of strengthening the diversification of funding of NGOs and, consequently, decreasing the over-reliance of NGOs on direct public funding mechanisms.

During the parliamentary elections in 2015, green political party "Orah" developed a proposal of sectoral policy of sustainable development of civil society organisations, where percentage tax designation mechanism was proposed as alternative financing mechanism for ensuring durability of public benefit programs of civil society².

Although percentage mechanism can be a valuable source of additional funding for NGOs, it should be pointed out that it cannot be considered as a financial support mechanism to the not-for-profit sector/ civil society organizations. As experiences of other Central and East European countries show, in addition to NGOs and foundations as most common type of CSOs, the beneficiary groups of tax designation mechanism can also be other not-for-profit institutions, but also churches and political parties. Besides, even when the primary beneficiary group is civil society based not-for-profit entities, other types of public or private legal entities, but also needy individuals, are often included in the same group as eligible

¹ See Annual Report on Public Funding of Civil Society Organisations in 2014, adopted by Government of the Republic of Croatia; available at; www.udruga.vlada.hr

² The document is available at the following website: https://www.orah.hr/files/Prijedlog-politika/ORaH-Politika_odrzivog_razvoja_civilnog_drustva_2015.pdf

entities for the given percentage designation. For this reason, the „public financial support of NGOs/civil society“ might not be the most adequate policy framework for considering the introduction of percentage mechanism in Croatia. In addition, given the still predominant financial, economic crisis and overall media suspicion towards financing of NGOs, the policy framework of public funding of NGOs in terms of introducing additional (and not substitute) source of funds for NGOs, might prove to be even counterproductive. As a matter of fact, in view of the still low level of public support to distributing taxpayers' money to NGOs³, it is more likely to foresee that the introduction of percentage tax designation mechanism could be envisaged within the framework of proposed decrease of direct public funding and offering alternative, substitute mechanisms of ensuring sustainability of NGO programs.

Percentage mechanism as specific model of philanthropy?

Currently, there are basic tax benefits for both individual and corporate giving in the Law on Personal Revenue Tax and Law on Profit Tax which allow for 2% tax deduction for donations to public benefit programs of organisations working in different fields of public benefit, regulated by the laws. From 2006, Croatian Government has adopted two strategic documents for creating more enabling environment for civil society development (first from 2006 to 2011, and the second from 2012 to 2016), with measures and activities related to ensuring financial sustainability of NGOs, but also amendments of tax legislation with the aim of ensuring better environment for both individual and corporate philanthropy in Croatia.

During the period of implementing these two strategies, no amendments of tax legislation have been made, but discussions were intensified on how to promote more extensive use of current tax benefits, as well as to open the space for testing new, innovative models of promoting philanthropy. Besides, through the EU funded grant schemes additional funding has been provided for research, awareness raising campaigns and testing new models in both individual and corporate philanthropy, including crowdfunding and similar online giving mechanisms⁴.

³ TACSO survey from 2012 showed decreasing support of citizens to direct State budget funding of NGOs, compared to the same research done in 2007. The Report is available at <http://www.tacso.org/documents/reports/?id=7826>

⁴ See for example IPA 2012 grant scheme „Fostering Innovative Forms of Philanthropy in Local Communities to Support Sustainability of Civil Society“ worth 0,5 million EUR.

However, there is still the lack of understanding of fundamental difference between philanthropy and percentage designation mechanism. Unlike, philanthropy where private individual or corporate resources are used to support public benefit causes, and are considered as donations, in the case of the percentage mechanism the allocated resources, although coming from personal revenues, are not considered as private resources, but taxes that the individual would pay anyway. This also means that the percentage designation option is only available to taxpayers, unlike philanthropy that is open to anyone. This leads to conclusion that the percentage mechanism should rather be considered as a specific form of a participatory budgeting but not philanthropy.

Percentage mechanism as form of participatory budgeting

The fundamental characteristic of tax percentage designation mechanism is related to delegating the decision making power to a taxpayer over a distribution of portion of taxes. In that context, this mechanism fits into the overall framework of participatory budgeting, which is a process of democratic deliberation and decision-making in which ordinary citizens decide how to allocate part of a municipal or public budget. More specifically, participatory budgeting allows citizens to identify, discuss, and prioritize public spending projects, and gives them the power to make real decisions about how their money is spent.

Recently, more efforts have been invested in promoting participatory budgeting trends at the local level in Croatia. Through EU funded projects, pilot initiatives of participatory budgeting have been introduced in several Croatian cities. Some of these initiatives, such as Pazin city budgeting, have proved to be sustainable, even after the end of project through which they were introduced and supported⁵. However, it must be noticed that participatory budgeting practices still have a very limited outreach and scope at the local level. At the national level, budgetary programming and execution still remain seen as very distant, close and not inclusive. This also holds for designing and implementing tax policy. In view of almost non-existent practice of participatory budgeting at the national level, this still seems to be a rather weak policy framework for considering the introduction of percentage mechanism in Croatia.

Legal environment for supporting civil society sustainability in Croatia

⁵ For more information see the website of the City of Pazin Participatory Budget Programming: <http://proracun.pazin.hr/>

The overall legal environment for the work of civil society organisations in Croatia is generally considered to be supportive, and in line with international standards.

The new Law on Associations entered into force on October 1, 2014, and it is considered to ensure the freedom and autonomy of work of associations as most numerous actors of organized civil society. The clear terminology of the law prevents unwarranted state control over CSOs and CSOs are protected from the possibility of the state dissolving a CSO for political or arbitrary reasons. Following the adoption of the Law on associations, a Government Regulation on Criteria, Standards and Procedures of Financing public benefit programs of Associations was adopted in 2015. Besides, a Regulation laying down minimum conditions for the provision of social services were passed in March 2014 and amended in May 2015, setting basic requirements for CSOs in this area.

The law on foundations is considered to be the most obsolete part of legal framework for civil society organisations/ non-profit organisations, and the procedures for establishing foundations are still seen as burdensome and too long. The changes of the Law on foundations have been on the Government agenda for some time already.

The data provided in Table 2 illustrates the structure of civil society organisations⁶ in Croatia.

Table 1: NUMBER OF CIVIL SOCIETY ORGANISATIONS IN CROATIA, 2014

Type of organisations	Number of registered organisations
Citizens' associations	51837
Foreign associations	137
Foundations	207
Funds	13
Trade Unions	650
Employers' associations	63
Private institutes	452
Religious communities	52
Organisational forms of religious communities	377
Legal entities of the Catholic Church	2038
Legal entities of the Orthodox Church	429

Source: *the official registrars of the Ministry of Public Administration, the Ministry of Finance, the Ministry of Labour and Pensions, and regional public administration offices, (September 2014)*

The new Law on Financial Operations and Accountancy of Non-Profit Organizations, which entered into force on 1 January 2015, allows for public accessibility of all financial reports of

⁶ Civil society organisations (CSOs) typically include a variety of forms, such as grass-roots initiatives, community groups, social movements, online groups, NGOs, foundations, labour unions, employers' associations, faith-based organisations, social entrepreneurs, social cooperatives, and other organisational structures whose members are united by a general interest and who also act as mediators between the public authorities and citizens (EESC, 1999).

non-profit organisations which are required to submit these reports, according to the law. All CSO income, including that from economic activities, is exempt from taxation under the Law on Financial Operations and Accountancy of Non-Profit Organizations. In addition, humanitarian organizations are exempt from VAT on purchases made for humanitarian purposes and all organizations, regardless of their area of activity, are exempt from VAT when using EU funds. Individual and corporate taxpayers can deduct up to 2 percent of their taxable income for charitable contributions to eligible CSOs. Associations may engage in economic activities, but cannot use the income to benefit their members or third parties. Any profits earned must be used to realize the objectives set out in the association's statute. There is still no legal framework for social enterprises or entrepreneurship, though the Strategy of Development of Social Entrepreneurship was adopted in 2015. For the period 2014-2020 substantial European Social Fund grant schemes have been ensured for launching and developing social enterprises.

Tax legislative environment for the work of CSOs and development of philanthropy

Croatia generally provides for favourable tax environment for the work of CSOs and the development of philanthropy. Civil society organizations are generally exempted from corporate income tax, as long as they pursue public or mutual benefit goals. Income from economic activities of CSOs is taxed only if those activities give rise to the issue of "unjustified privileged position on the market", which needs to be established by tax authorities on a case-by-case basis.

Donations by corporations (in money and in kind) to cultural, scientific, educational, medical, humanitarian, sport, religious, ecological and other purposes of public benefit are exempted up to 2% of their gross annual income in the preceding year. The tax exempt percentage may be higher, based on a decision of the line ministry on financing particular programs and actions⁷. When it comes to the personal income tax, the Law on Income Tax⁸ foresees that individuals can donate under the same conditions set out for corporations in the Profit Tax Law. Namely, tax deductions are available for all taxpayers for donations up to 2 percent of their previous year's income as evidenced in the previous year's annual personal income tax return. In view of the EU Court case law, it may be necessary to revise tax legislation to allow

⁷ Article 7(7), Profit Tax Law

⁸ Article 36 (12) Income Tax Law

tax deductions to giving not only to in country CSOs, but also to those operating in other EU member states.

One of the key challenges frequently mentioned in the context of the legislative framework for philanthropy is related to the lack of coherent approach to defining the concept of public benefit status and activities. Tax laws and the Law on Foundations and Funds bring a non-exhaustive list of eligible activities considered as public benefit: "...cultural, educational, scientific, spiritual, sport, medical, ecological and other activities which are deemed for public benefit or which generally contribute to the well-being of the society". The Law on Institutes emphasizes that a private institute may be established in order to permanently pursue: "educational, scientific, cultural, information, sport and physical culture, technical culture, child care, medical, social protection, care of persons in need and other not-for profit activities"⁹. On the other hand, the Law on Associations defines programs and projects of public benefit as "rounded and thematically clearly defined sets / set of activities that are in accordance with the values laid down in the Constitution of the Republic of Croatia and the implementation of which the long-term or limited duration of action makes visible the added social value which raises the quality of life of the individual and promotes the development of the wider community"¹⁰. In addition, it brings a more comprehensive list of public benefit activities of NGOs, and defines them as "activities that contribute to the protection and promotion of human rights, protection and promotion of rights of national minorities, the protection and promotion of the rights of persons with disabilities and children with disabilities, the elderly and infirm, and equality and peace-making and the fight against violence and discrimination, promoting the value of the war, protection, care and education of children and young people and their active participation in society, preventing and combating all forms of addiction, development of democratic political culture, protection and promotion of the rights of minority social groups, promotion and development of volunteering, social services and humanitarian activities, promotion and development of social entrepreneurship, protection of consumer rights, environmental protection and nature and the protection and preservation of cultural heritage, sustainable development, community development, international development cooperation, protection of the health, development and promotion of science , education, lifelong learning, culture and art, technical and IT culture, sports, volunteer firefighting, search and rescue and other activities that by their nature or according

⁹ Article 1(2) of the Law on Institutes

¹⁰ Article 32 (3) of Law on associations

to special regulations on the financing of public needs in a particular area can be considered as the action of interest to the common good”¹¹.

This definition of public benefit programs, projects and activities of NGOs is also related to the implementation of the Regulation on Criteria, Standards and Procedures of Public Funding of public benefit programs and projects of NGOs, as key regulatory framework for direct funding of public benefit programs and projects.

As seen from above-mentioned, there is a lack of clarity and coherency in regard to the definition of public benefit activities in the legislative framework for the work of CSOs and relevant tax laws. This may be challenging in terms of determining CSOs and other legal entities that could be eligible for possible future percentage tax designations.

Capacities of NGOs for fundraising and advocacy

According to the USAID NGO sustainability index, the organizational capacities of CSOs in Croatia are still weak, mostly due to great inequalities in organizational capacity between smaller and larger organizations and between CSOs in major urban centers and smaller, more rural areas. Organisational capacities can be measured in terms of potential for mobilizing citizens’ support to their programs/initiatives, number of employees, involvement of volunteers, availability of equipment. Generally, staff in smaller organizations often lacks professional knowledge and skills as a result of their inability to participate in training, including on applying for EU funds. On the other hand, some CSOs demonstrated extraordinary ability to garner support from the public ¹². For example, there are several big CSOs that deal with specific humanitarian (and emotional) projects and with support of national media regularly manage to mobilize huge support from citizens for some fundraising actions for needy persons (or response to natural disasters). A good example is the Foundation Ana Rukavina which has been successfully organizing humanitarian and marketing activities for more than ten years with the goal to collect financial and other resources for the maintenance and expansion of the Croatian voluntary bone marrow donor Registry and for the operation of the private and public cord blood bank. In addition, Croatian Red Cross managed to mobilize large support from citizens and companies following extensive flooding in Croatia and South East Europe.

¹¹ Article 32 (4) of Law on Associations

¹² See NGO Sustainability Index 2015 for Croatia

The Top 10 associations receiving the highest amount of financial resources from private individuals in 2014 and 2015 and their fields of activities:

Table 2: Top 10 NGOs receivers of citizens' donations

2014	Amount (EUR)	2015	Amount (EUR)
1.Croatian Red Cross (national umbrella/headquarters - humanitarian)	3,111,417.73	1.RTL helps Children - humanitarian association (humanitarian, social welfare work for children in need/run by national TV station)	279,079.33
2.Association Radio Maria (non-profit catholic radio station)	257,632.13	2. Red Noses - Doctors Clowns Association (humanitarian/social welfare)	241,948.80
3. Red Noses - Doctors Clowns Association (humanitarian/social welfare)	197,378.93	3. Association Radio Maria (non-profit catholic radio station)	228,996.13
4. Association Fountain of Mercy (humanitarian, social welfare work in Croatia and abroad- Africa/South America)	183,286.13	4. Croatian Red Cross (national umbrella/headquarters - humanitarian)	193,625.20
5. RTL helps Children - humanitarian association (humanitarian, social welfare work for children in need)	141,738.93	5. Mary's Meals (humanitarian, social welfare work for children in need)	187,996.00
6. Mary's Meals (humanitarian, social welfare work for children in need)	125,803.47	6. Association Fountain of Mercy (humanitarian, social welfare work in Croatia and abroad- Africa/South America)	180,476.13
7. Cultural Centre Harmica (youth education/Opus Dei)	121,296.93	7. Cultural Centre Harmica (youth education/Opus Dei)	124,641.07
8. Croatian Red Cross- Osijek City Association (humanitarian)	107,908.80	8. Society for promotion of Christian values - Christofori	99,657.07
9.Croatian Red Cross Županja City Association (humanitarian)	106,384.13	9. Centre for Unborn Life Betlehem (Christian/Family/ Demographic policy)	91,367.60
10. Centre for Unborn Life Betlehem (Christian/Family/ Demographic policy)	90.669,46	10. Community Good Shepherd (Christian/ Charismatic Prayer)	83,344.53

Source: Ministry of Finance, Registrar of Non-Profit Organisations, 2016

As it can be seen from the table above, the biggest potential for fundraising and mobilizing citizens' donations is with humanitarian, social welfare and church related organisations. On the other hand, CSOs focused on areas such as human rights protection and various public policy watch-dog activities generally receive very little citizens' donations, and continue to rely on direct project or operating grants from different domestic and international public and private sources.

When it comes to potential of NGOs to involve citizens in advocacy campaigns for public policy changes, an area where NGOs succeeded in gaining extensive public support, and especially support from famous persons, is the protection of natural and public resources. A recent examples includes the successful grass-route initiative "do not give our seaside" which stopped big Government sponsored strategic investment project of oil and gas exploitation in Adriatic sea. Besides, there are examples of conservative, church supported organisations that also demonstrate substantial capacity for mobilization of citizens for their advocacy campaigns. The most prominent among these NGOs is the Association "On behalf of the family" (*U ime obitelji*), a conservative organization which gathered more than 700.000 signatures to launch the constitutional referendum which was successfully organized in 2013, resulting in an amendment to the constitution in order to define marriage as being a union between a man and a woman (and create a constitutional prohibition against same-sex marriage).

Recent trends of new coalitions among trade unions, human rights based NGOs and various civic initiatives showed increasing advocacy potential of NGOs, which was especially visible in case of campaigns against the privatization of highways.

The still limited advocacy capacities of NGOs are reflected in the fact that only 1% of all registered NGOs take part in public consultations on draft laws. According to the Government Office for Cooperation with NGOs' Report on the Implementation of Consultations with the Interested Public in the Procedures of Passing Laws, Other Rules, and Regulations¹³, 608 public consultations were held on draft laws, rules, and regulations in 2015. The most active contributors to public consultations are individual citizens (70% of all contributors), while NGOs account to only 7% of all contributors. Only 433 NGOs took part in public

¹³ Report is available at the www.udruga.vlada.hr

consultations in 2015, which is a slight decrease compared to 2015 when 506 NGO got involved in commenting draft policies of ministries.

Despite a great number of available calls for proposals (from 70 to 100 calls for proposals annually at central level) and existence of three years' operating grants distributed by the National Foundation for Civil Society Development (with numerous requirements for advanced strategic planning and focus of organisations), a big challenge for a number of CSOs in Croatia is related to the “mission drift phenomenon”, as they tend to apply to as many tenders as possible and therefore frequently work in areas beyond their stated missions and visions.

It is still only larger organizations and those applying for operating grants of the National Foundation for Civil Society Development that implement strategic plans and introduce more advanced governance structures, while other types of organizations typically do not.

The number of persons employed in the non-profit sector is continuously growing and was 22.310 in 2015, which is 1,7% of the overall number of employees in Croatia, while the number of employees in NGOs was 12.182, or less than 1% of all employees in the same year.

Table 3: THE NUMBER OF EMPLOYEES IN NON-PROFIT ORGANISATIONS IN CROATIA		
Year	Number of employees in non-profit organisations	Percentage of total number of employed persons
2008	17,291	1.11
2009	18,228	1.21
2010	18,667	1.31
2011	19,610	1.43
2012	19,484	1.40
2013	20,946	1.55
2014	21,912	1,68
2015	22,310	1,70

SOURCE: Source: Ministry of Finance, Registry of Non-profit Organisations, 2016.; State Statistical Office, 2016

The capacities for mobilizing volunteers are increasing, but are still low. In 2015, 52.208 volunteers were involved in different organisations and institutions in Croatia, providing for 2 943 902 volunteer hours¹⁴. 1010 associations reported involvement of volunteers in 2015, which makes 81% of all organisers of volunteering in Croatia. Nevertheless, compared to the

¹⁴ See Report from Ministry of Social Policy and Youth for 2015 – statistics also available at: <http://volontiram.info/nm/novosti/item/478-statisticki-podaci-za-2015-iz-izvjesca-mspm-u>

interest of citizens for volunteering (more than 10.000 interested citizens only in Zagreb Volunteer Centre database by the beginning of 2014¹⁵), there is still a lack of capacities for receiving and managing volunteers. The capacities for management of volunteers still remain rather low, and there is a wide gap between the number of citizens interested in volunteering and organisations ready to receive volunteers.

When it comes to basic equipment for work of NGOs, the last research conducted by the National Foundation for Civil Society Development on the state of development of NGO sector in 2011¹⁶ showed that 15% of NGOs do not have premises for their work, while 25% do not have basic IT equipment and access to internet.

Financial viability of NGOs

According to data of Ministry of Finance' Registar of Non-Profit Organisations, the overall income of NGOs in 2014 was 654.103.587.66 EUR. The structure of revenues of NGOs show that donations of citizens account for only 1.7% of total revenues of NGOs in Croatia, while the share of donations of companies accounts to 6.8%. In addition, all foundations in the country received donations of citizens which account to only 1.5% of total revenues of foundations in 2014. State and local / regional government grants still represent dominant source of funding of NGOs, accounting for 28% of their overall income, while membership fees' share is only 10%.

Table 4: Structure of income of NGOs in Croatia in 2015

Source of income	% in the overall income of NGOs
Income from economic activities	18.60
Membership fees/contributions	10.27
Executing public competences delegated by special laws	15.04
Revenue from property	2.30
Other revenues	6.11
Transfers from related/umbrella NGOs	4.85
Donations from State budget	7.00
Donations from local/regional government bodies	16.20
Revenues from international organisations/foreign governments	8.83
Revenues from companies and other legal entities	6.21
Revenues from citizens/individual donations	1.34

¹⁵ <http://www.vcz.hr/info-pult/novosti-i-dogadjanja/10000-volonterka-registriran-u-bazi-vcza/>

¹⁶ http://zaklada.civilnodrustvo.hr/upload/File/hr/izdavastvo/digitalna_zbirka/procjena_stanja_2011.pdf

Other donations	3.24
Total revenue (676,360,368.93 EUR)	

SOURCE: Ministry of Finance, 2016

A very extensive and decentralized system of direct State funding of NGOs in Croatia has been developing since 1999 onwards and encompasses more than twenty State bodies with average 90 calls for proposals/grant schemes published every year.

Table 5: State Budget funding for CSOs programs and projects from 1999 to 2014

Budget year	Overall State budget allocation for CSO projects and programs (EUR)	Number of financed CSO projects and programs
1999	3.775.536	276
2000	2.739.432	348
2001	2.958.519	481
2002	2.291.852	450
2003	2.278.519	442
2004	14.812.850	2.733
2005	18.200.536	3.163
2006	42.884.909	2.766
2007	62.692.279	4.923
2008	83.222.676	6.350
2009	70.612.927	5.611
2010	65.201.641	5.125
2011	73.330.613	5.258
2012	68.428.864	4.791
2013	74.699.425	5.725
2014	86.998.931,46	5827

Source: Government Office for Cooperation with NGOs, 2015, www.udruga.vlada.hr

The standards and procedures of allocation of public funding have been largely harmonized across all government bodies. Government Office for Cooperation with NGOs prepares and publishes annual plan of grant schemes with details on expected launch of every call for proposals. These plans are presented and discussed with NGOs at traditional Annual Info

Days on Public Funding of NGOs which are held soon after the adoption of the State budget and Government Regulation on Criteria for distribution of revenues from games of chance¹⁷.

The analysis of received financial reports of associations/NGOs for 2015 shows that the majority of associations (58%) have annual budget less than 15.000 EUR. On the other hand around 100 NGOs have budget close to or more than 1 million EUR, while only 5 organisations have annual budgets higher than 13 million EUR. Below is an overview of data on NGOs' annual budgets in 2015, collected from 13165 associations that submitted their annual financial reports, according to the requirements of the Law on Financial Operations and Accountancy of Non-Profit Organizations.

Table 6: Annual budget of NGOs in 2015

Annual budget of NGOs	Number of NGOs
Up to 100,000 HRK (15.000 EUR)	7688
From 100 to 500 000 HRK (15-65.000 EUR)	3847
From 500 to 1million HRK (65.000-130.000 EUR)	861
From 1 to 5 million HRK (130.000 – 650.000 EUR)	669
From 5 to 10 million HRK (650.000 – 1,3 million EUR)	52
From 10 to 50 million HRK (1,3 million – 6,5 million EUR)	42
From 50 to 100 million HRK (6,5 million – 13 million EUR)	1
From 100 to 200 million HRK (13 million EUR – 26 million EUR)	4
Over 200 million HRK (over 26 million EUR)	1

Source: Ministry of Finance, Registrar of Non-Profit Organisations, 2016

This confirms quite a strong discrepancy in financial viability among different categories of NGOs. In general, less developed organizations are unable to access funds, and most organizations lack sustained funding.

State supported infrastructure for enhancing civil society development

The institutional framework for supporting civil society development in Croatia began to develop in 1998 with the establishment of the Office for Cooperation with NGOs, followed by the setting up of the Council for the Development of Civil Society in 2002, and the

¹⁷ According to the Law on games of chance, 50% of revenues from games of chance are invested into civil society organisations' programs in eight areas, defined by the law.

National Foundation for Civil Society Development in 2003. The most important strategic documents and acts promoting civil dialogue are the 'National Strategy for Creating an Enabling Environment for the Development of Civil Society' (first for the period 2006-2011, and then for 2012-2016 period), as well as the 'Code of Practice on Consultation with the Interested Public in Procedures of Adopting Laws, Other Regulations and Acts'. The Government Office for Cooperation with NGOs supports the development of the legal, institutional, and financial framework for the operation of associations and creating enabling environment for development of a strong and autonomous civil society as an indispensable partner to the government in the preparation and implementation of public policies. It also runs the Program of co-financing of the EU projects of CSOs. NFCSD acts as the public foundation focused on increasing capacities of CSOs by providing operating grants and conducting a number of support programs. Among others, the NFCSD has supported the Program of Regional Development and Strengthening the Capacity of CSOs since 2007. The five regional support centres developed through this program offer information services, consulting, and training services to CSOs at the local and regional levels, with a focus on preparing them to apply for EU funds. In addition, the National Foundation supports the work of four partner local community foundations, which manage the small scales grant schemes for local civic initiatives. The Government Office and the Foundation form part of the operating structure for the European Social Fund, ensuring the implementation of a number of CSO capacity building programs until 2020, worth almost 90 million euros. The most significant institutional mechanism for civil dialogue is the Council for Civil Society Development (CCSD), the government's advisory body. It is composed of 31 members: fifteen representatives of various government bodies and sixteen representatives of organised civil society, of which thirteen are representatives of NGOs, one represents the trade unions (nominated by the coordination of trade union federations), one represents employers' associations (nominated by the Croatian Union of Employers), and one represents foundations. The Council acts as an important platform for agenda setting regarding key policies affecting sustainability of civil society.

Public image of NGOs

According to the TACSO survey on the visibility and public perception of NGOs in Croatia, conducted in 2012¹⁸, a positive general attitude about NGOs and their activities is characteristic for slightly more than three quarters of Croatian citizens (76%), somewhat less than one quarter express a neutral attitude (22%), while the proportion of citizens with a general negative attitude is negligible. A positive general attitude towards NGOs is more characteristic for younger citizens, employed persons, and citizens from villages with a medium and high level of urbanization.

Around one quarter of citizens (26%) experienced at least one benefit from NGO activities (of seven encompassed) which indicates an increase compared to data collected in 2007 (17%).

NGO Sustainability Index for 2015 shows that Croatian media still does not show significant interest in civil society, and media coverage of CSO activities largely depends on the interest of reporters and editors in topics related to the civil society sector. On the other hand, local media show far more interest in CSOs than the leading national media, especially public television.

During 2015 parliamentary elections' campaign, part of politicians launched strong media campaign against CSOs for "parasitizing" on the state budget and taking portion of limited state funds that could be used more effectively in other programs, and therefore threatened to cut CSO funding programs. This was preceded by several cases of alleged mismanagement of funds collected through large humanitarian actions by some NGOs, which contributed to numerous negative media coverage of NGO activities.

To contribute to improving public image of NGOs, during past several years Government sponsored manifestation "Days of Open Door of NGOs" was held, when associations open their doors to citizens to present their programs and activities. The purpose of NGO's Open Door Days is to strengthen solidarity and trust in local communities and remind the public of the important role of associations in mobilizing citizens to solve community problems. In 2015, as many as 500 associations from all counties in Croatia participated in Open Door Days. In addition, a mobile application Udruginfo (Associations info) was launched to increase the visibility of associations and citizen participation in their activities.

In general, despite gradual progress, the public understanding of the role of CSOs in society is limited and much mistrust remains, mostly due to the lack of positive discourse of politicians, but also lack of capacities of NGOs to proactively present their programs to wider public.

¹⁸ The Report is available here: <http://www.tacso.org/documents/reports/?id=7826>

Exploring possible strengths and weaknesses of introducing the percentage tax designation mechanism in Croatia

At the stage when Croatian Government is drafting the new Strategy for creating more Enabling Environment for Civil Society Development 2017 - 2021, it is important to explore possible positive and negative effects of introducing 1% tax designation mechanism in Croatia.

One of the key expectations from percentage tax designation mechanisms is usually related to increased participation of citizens in the work of CSOs, either as members or volunteers. The official data from 2014 show that the density of NGOs is quite high in Croatia - on every registered NGO, there are approximately 81 inhabitants. On the other hand, according to the last official report on the number of volunteers in 2015, only 2% of all registered NGOs¹⁹ involve volunteers in their work. The number of reported volunteers in 2015 was 52 208, which is an increase in 14% compared to 2014. If the reported number of volunteers is compared to the number of NGOs that submitted reports (1110 or 81% of all organisers of volunteers), an average 40 volunteers per NGO may be considered as very high. However, if this data is compared to the overall population, than 1,2% of citizens engaged in volunteering is indeed very low²⁰.

The density of NGOs in Croatia has been continuously growing in past 15 years, mostly due to a very liberal legislative framework for registering NGOs. Also, the data on the number of volunteers are showing permanent increase²¹. Although these data indicate rather high level of rootedness of NGOs in Croatia, this may be misleading mainly because of a large number of formally registered, but inactive NGOs²², as well as still low level of capacities for management of volunteers, including running the evidence on number of volunteers. Therefore, there are no sufficiently reliable indicators for analysing possible effects of introducing the percentage tax designation mechanism on increased participation of citizens in the work of NGOs.

¹⁹ Only 1110 NGOs reported involving volunteers in their work in 2015.

²⁰ It has to be taken into account that many NGOs do not fulfill their legal obligation of annual reporting on the number of volunteers, so this data should be considered with caution.

²¹ As the submission of reports on the number of volunteers was recently introduced as a precondition for getting funding at some ministries' grant schemes for NGOs, the increase in number of volunteers may be regarded as a consequence of better reporting by NGOs.

²² One of the valid indicators of activity of NGOs is compulsory submission of annual financial reports. Only 21.527 NGOs submitted their annual financial reports to the Ministry of Finance in 2015, which is around 40% of all registered NGOs.

In addition to “rootedness or citizen-reconnection” arguments, NGO visibility and public image related reasons seem to be dominant in all discussions on strengths and benefits of introducing percentage tax designation mechanisms in Croatia. As the lack of social marketing and public relations skills of NGOs in Croatia has usually been mentioned as one of the key sources of their disconnection from citizens/public and threats to their sustainability, it goes without saying that introducing legal possibility for citizens to allocate percentage of public money for public benefit programs would serve as strong incentive for more proactive outreach to citizens and media, and improving public recognition of their work.

For the majority of NGOs, the perspective of getting rather easy, flexible and less bureaucratic public funding would certainly seem as a valuable alternative to currently predominant complex and demanding direct public funding procedures in the EU and national grant schemes, as well as in local and regional government calls for proposals.

Additional positive effects may be envisaged in regard to clarifying the public benefit status of different non-profit legal entities, as well as in strengthening the values of solidarity. Besides, the designation of public funds by citizens, without any political or economic influence, may also contribute to raising awareness on the importance of participatory budgeting standards in Croatia.

Potential effects of percentage mechanisms on the development of the philanthropy and culture of giving in Croatia are difficult to assess, especially because of the fundamental difference between classical philanthropy mechanisms and percentage tax designation, as already explained before.

The biggest number of citizens’ donations in last years was collected following extensive media supported campaigns related to very specific and emotionally strong cases of humanitarian, health or social welfare character. Donations were predominantly allocated through phone calls or SMS messages and required the lowest possible participation efforts from citizens. On the other hand, current individual philanthropic mechanisms in the form of personal revenue tax deductions are barely used. In 2014, only 0,6% (or 3614 citizens) of all citizens that submitted their personal revenue tax returns forms actually used to possibility of

tax deduction for donations given to public benefit purposes. In 2015, that percentage was even lower (2404), probably because of the automatic analysis of personal tax revenue returns by Tax administration²³. These data may lead to the conclusion that citizens prefer to use low effort digital philanthropy mechanisms and are generally reluctant to engaging in paper work and bureaucratic procedures required for any tax deductions for given donations.

However, the possibility of taking autonomous decisions on the allocation of portion of public money to organisations of personal choice may be attractive to a number of citizens and in long term could lead to strengthening links with organisations and public benefit programs they have chosen to support.

Key weakness of percentage tax designation mechanism may be related to further deepening of the gap between big and small organisations. As already stressed before, large majority of active NGOs fall into the category of small organisations with annual budget lower than 15.000 EUR and expected low potential for social marketing. In the absence of sufficient financial resources to create meaningful marketing campaign and get adequate media coverage, small organisations may fail to connect with enough taxpayers and therefore loose opportunities provided by this mechanism.

Prospects of reducing direct public funding for NGOs programs or cancelling existing individual philanthropy mechanisms in the form of personal revenue tax deductions are very probable negative effects of introducing percentage tax designation in Croatia. This is especially so because different stakeholders tend to mention percentage designation mechanism in the context of necessary State budget cuts for NGOs and rarely as alternative, additional source of funding and sustainability of NGOs.

When it comes to possible cancelling of existing individual philanthropy mechanisms, there are not enough solid arguments for that, as the overall amount of tax deductions for given individual donations amount to only 0,07% of the overall amount of taxable personal revenue in 2014. Nevertheless, in view of experiences of some countries of Central and Eastern Europe (for example Hungary and Slovakia) which completely abolished or drastically cut off

²³ Official data gathered from Tax Administration statistics.

the tax deductions related to both, individual and corporate donations, this threat should be given proper attention.

The key challenge and obstacle to introducing percentage tax designation mechanism in Croatia is related to perception of potential negative effects on State and local budget, however small it could be. As key beneficiaries of personal revenue tax are local and regional government bodies (municipalities, cities and counties), strong opposition to additional decrease of the level of their revenues could be expected.

The overall income from personal revenue tax in 2014 was 1,812 billion EUR. The maximum estimated revenue from 1% designation mechanism would be 18,1 million EUR. As experiences of most countries show that approximately 35% of maximum foreseen amount actually gets designated to final beneficiaries, the potential realistic designation could amount to 6,3 million EUR.

As the overall annual amount of State budget funding for NGOs in 2014 amounts to approximately 90 million EUR, the possible share of potential new source of funds for NGOs through percentage designation mechanisms would be only 7%. Therefore, arguments in favour of possible reduction of state or local government budget funding to NGOs due to introduction of percentage mechanism look rather weak and would certainly receive strong opposition from most NGOs that are currently beneficiaries of any form of public funding.

Concluding remarks

A well established and decentralized system of direct public funding of NGOs in Croatia, with advanced standards and procedures of allocation of significant funds available at central, local and regional levels, has decreased the potential of large majority of NGO to mobilize citizens' support for their core activities. Therefore, in the personal opinion of the author of this report, the most important positive effect of introducing percentage tax designation mechanism in Croatia would be the creation of strong incentive for NGOs and other non-profit entities to increase visibility of their public benefit programs and find innovative ways of communicating their activities to citizens and media.

Despite negative experiences of several countries related to abolishment of existing tax incentives for individual and corporate philanthropy, following the adoption of percentage tax designation mechanism, this innovative mechanism of supporting the sustainability of civil society deserves adequate evidence based debate with participation of key interested stakeholders and decision-makers in Croatia.