

International tax alert

Ernst & Young Albania

Expatriate structures and Albanian law

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Executive summary

This Tax Alert presents the tax aspects of expatriate assignments in Albania and relevant issues that need to be resolved before the fiscal year end, which in Albania coincides always with the calendar year.

Assignment related charges invoiced by the home country employer to the Albanian company, if not properly addressed, may lead to double taxation or to unnecessary risk exposure to tax and penalty assessments. Therefore it is recommended that companies review well before the end of December the contractual terms to make sure that they capture properly the purpose and economic reality of the expatriate assignment and conclude whether:

- ▶ the home country charges are subject to the internal withholding taxation rules, making the tax deductibility of the expense conditional on its payment before year end,
- ▶ the assignee is obliged or not to file individual income tax declaration in Albania in respect of the amounts paid to him in his home country for the activity performed in Albania,
- ▶ the assignment provides benefits to the host entity or serves primarily the reporting to the parent company abroad,
- ▶ the activity of the assignee at the premises of the host entity is creating a taxable permanent establishment of his home country employer in Albania.



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Background

An international assignment could be structured either as a supply of staff or supply of service. In the former, the risks and control of the employee remains with the host country, while in the latter case, the risks and control of the employee remain with the home country employer company.

In the typical structure for international assignments, the assignee will usually remain an employee of the home country employer company, with participation in home country benefits including pension and social security and (usually) home country payroll delivery. The host country is then recharged for the home country costs, and may also provide assignment related benefits such as housing locally. This basic structure is usually preferred for continuity of service in employment law terms and conditions.

At issue is what has been “sold” in this recharge of costs – a supply of services or a supply of staff. Depending on what the answer would be, the tax implications for the parties involved are different. Furthermore, duration of the assignment for 183 days and consistency of the contractual terms with the actual nature of the supply are also important.

Detailed discussion

Invoice payment before year end important for the expense recognition, should consultancy or management services be supplied

The Albanian tax law makes the tax deductibility of charges relating to technical or management services conditional on the payment of the amounts before December 31st. Indeed, pursuant to the Albanian profit tax law, expenses for those services, which are subject to withholding taxation, are not tax deductible if they are not paid until the fiscal year end. Among the cross-border charges which are subject to withholding taxation are listed the charges for technical and management services. Such withholding taxation is triggered in Albania upon payment, regardless of the time of accrual of the expenses.

Accordingly, the charges for the expatriate assignment, if they relate to consultancy or management services, will have to be paid before fiscal year end, in order for the service recipient to claim tax deduction. Therefore it is important that the amount of the relevant charges is determined and paid before fiscal year end. Alternatively, the tax administration provides in its guidelines the option to pay not the full amount but the corresponding withholding tax before year end, in order for the expense to be tax deductible.

This rule applies also in case where double taxation treaty relief can be claimed. Hence, regardless of the status of the home country employer, as tax treaty country resident or not, the payment of the amount needs to be planned and effected before fiscal year end, unless the payer of the income has previously sought and received approval from the Albanian tax administration for the application of the relief provided in the applicable tax treaty.

By contrast, the supply of personnel does not trigger application of the internal withholding tax rules and therefore the tax deductibility of the relevant charges is not dependant on payment before fiscal year end. This requires that the home country employer is only obliged to make the staff available to the host entity and does not bear any responsibility on the assignee effectively providing certain technical, consultancy or management services.



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Personal tax obligations of the assignee in Albania

Should the assignee be on a split payroll and be also remunerated by the host entity, the relevant amounts will be subject to social security contributions and payroll tax in Albania processed by the host entity. The individual will have no obligation to declare them by means of annual income tax return.

By contrast, any amounts paid to him by the home country employer for his activity in Albania will have, in several circumstances, to be declared by the individual via an annual income tax return, which is due for filing by 30th January. Such circumstances are the following:

- ▶ the individual is not tax treaty country resident
- ▶ the individual is a tax treaty country resident but the assignment in Albania will last more than 183 days in any twelve month period
- ▶ the assignment is structured as a supply of staff

In the latter case, the amounts paid to the assignee by the home country employer and relating to his assignment will have to be declared by him with the annual income tax return filing, regardless of the duration of the assignment and of whether he is a tax treaty country resident or not.

Consequently, it is also important for the individual to know early enough the impact of the assignment structure and terms on his personal income tax obligations in Albania.

Benefit test and other transfer pricing aspects

In order for the host entity to claim tax deduction of the amounts invoiced by the home country employer, the assignment would have to relate to and be useful for the operations of the host entity.

Assignments serving primarily the reporting as a group internal auditor to the headquarters or other so called stewardship activities would not justify the deductibility of any relevant charges for tax purposes.

Furthermore, the methodology followed in determining any profit margin applied to the charges would also have to be available, upon a tax audit, and should reflect the application of the arm's length standard. The components of the charges should be clearly determined in the contract also for the assignee not to be challenged by the tax authorities as regards the offshore portion of his assignment income that he declared



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Services creating a permanent establishment risk for the home country employer

The activity of the assignee at the premises of the host entity could be viewed as creating a taxable permanent establishment of his home country employer in Albania. If an international assignment is structured as a supply of service, the assignee would be considered to be acting on behalf of the home country employer. Under this assignment structure, the home country employer may be exposed to the risk of creation of a permanent establishment (PE) in Albania, in which case he would have the obligation to register for tax purposes. This is particularly the case if the assignment is going to last for more than six months. Shorter term assignments would normally not trigger any tax exposure of the home country entity in Albania, provided it is a tax treaty country resident.

If the international assignment is structured as a supply of staff, whereby the home country employer does not bear any responsibility for the results of the activity of the assignee, who will work under the control of the host entity, no permanent establishment taxation would be triggered.

Other aspects

VAT

The Albanian VAT Code would consider the fee charge for both types of international assignment structures as a supply of service for the purpose of VAT. According to the VAT Code, a service provided by a non-resident entity would be considered as a service supplied in the place it is rendered and consumed, i.e. Albania in this case. Nevertheless, the home country employer would not need to register for VAT purposes in Albania, as long as the host entity is VAT registered and the activities rendered by the foreign company in Albania do not constitute a fixed establishment, creating the obligation for tax registration. In such case, the latter entity would apply the reverse charge. This self-charged VAT is at the same time credited, leading to no negative cash flow effect, provided that these services are related to the VAT liable activities of the Albanian host entity.

The home country employer must consider its implications on the supply of staff when the activity is related to immovable properties, where under certain conditions underlined in the Albanian legislation, the obligation to register for VAT purposes in Albania may arise.

Immigration and social security aspects

Generally, assignees would be required to pay social security contributions, regardless of the assignment structure. This may lead to double contribution of social securities in two different jurisdictions, unless a relief is available under bilateral agreements.

Any social security amounts paid by the home entity employer and charged to the host entity will not be tax deductible.

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