MASTER THESIS

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„The impact of International Tax Law on the Albanian Tax System under special consideration of EU membership negotiations“

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FRANK LIGORI

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To my lovely father,

HENRIK

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LIST OF ABBREVIATIONS

Art – Article
AIDA – Albanian Investment Development Agency
BIT – Bilateral Investment Treaty
CETA – The Comprehensive and Economic Trade Agreement
EC – European Commission
ECOFIN – Economic and Financial Affairs Council
ed. – edition
EFTA – Economic Free Trade Area
etc. – et cetera
et al. – and others
EU – European Union
FDI – Foreign Direct Investment
FTA – Free Trade Agreement
GDC – General Directorate of Customs
GDP – Gross Domestic Product
GTD – General Tax Directorate
GSA – Gambling Supervisory Authority
ICSID – International Centre for Settlement of International Disputes
IMF – International Monetary Fund
no – number
MS – Member State of European Union
OECD – Organization for Economic Cooperation and Development
para. – paragraph
PE – Permanent Establishment
pg. – page
SAA – Stabilization and Association Agreement
SE – Societas Europaea
TFEU – Treaty on the Functioning of the European Union
TPD – Tax Policy Directorate
VAT – Value-Added Tax
WTO – World Trade Organization

CHAPTER 1 – Introduction

In the past twenty years, Albania has significantly progressed economically and politically. The dramatic transitioning from communist rule to democracy has not been reached without drastic shift changes. After the fall of the communist system in the early 90s, serious efforts were made to reform the economy, converting it from a centralized economy to an open market system. The centralized economy shifted into an open market system by the efforts being made in the economic reform after the collapse of communism. Now the shifting is being finalized by the tax reform plan which will significantly strengthen the economy, leading Albania toward European Union (EU) integration.

Albania is a small country on the Balkan Peninsula with a resident population of about three million people. Many Albanians emigrated in the European countries in search for a better life, away from the economic and political insecurity of that time. The aspirations of Albanians for freedom and democracy, dreamt up by individuals had a vital role in the country's recovery. The slogan "*We want an Albania to be like all other European countries*" was used by the government to keep this dream alive. However, economic difficulties, high unemployment level and uncertainties in the judicial system were the main reasons for a relatively high rate of emigration and consequently, low level of Foreign Direct Investments. In 2014 Albania was awarded Candidate Status by the EU, leading Albania on the road to membership. The Stabilization and Association Agreement (*SAA*) signed by Albania in 2006, stipulated obligations aligning its legislation to EU requirements in a process of harmonization. The making of new laws and implementing related regulations is one of the biggest challenges Albania is facing nowadays.

This *Master Thesis*, is the culmination of an in-depth analysis of continuous studies in the field of taxation, aiming to give an overview of the impact of International Tax Law on the Albanian Tax System under special consideration of EU membership negotiations. As Albania is an aspiring country for EU membership, the current Albanian Taxation System functionality and the role of EU reforms are essential towards prosperity. Taxes are the main tool affecting the state's economy. Thus, to clearly understand how the taxation system influences the investment climate is a must. The discussion of tax policy issue is vital in understanding any states' decision making-behaviour.

Since the economic crisis of 2009, the Albanian government has tried to create a fair tax system based on principles and specified rules. In addition, EU is offering stronger incentives for pushing Albania ahead with the reform to bring the tax system in line with EU standards. Albania has so far achieved satisfactory results due to the influence of the EU law in the field on indirect taxation.

Firstly, this research will help me to develop my skills and broaden my knowledge in the field of taxation. Secondly, the readers will benefit by gaining a complete understanding of the efforts undertaken by a country that is making giant steps towards joining the EU. This will help foreign companies develop a clear understanding of Albanian tax system and the investment climate. Thirdly, this legal research will highlight the importance of fulfilling obligations arising under EU-membership negotiations, demonstrating the degree to which the Albanian tax system is already harmonized with the EU law. An outline of the substantial impact that the International Tax Law has on our domestic tax system regarding the issue of double taxation, will make the importance of this thesis apparent in conclusion.

This legal research examines several topics, raising numerous questions throughout the six chapters. ***Chapter One***, introduces the topic, outlining the aim of the thesis. ***Chapter Two***, deals with the history of the Albanian tax system, explaining the political and economic reasons that affected the tax system over these years. ***Chapter Three*** gives an overview of the Albanian tax system, showing the way in which this system functions. ***Chapter Four***, outlines the Albania's status regarding EU integration, the main directives governing in the EU and the importance of the International Treaties regulating the issue of double taxation. ***Chapter Five***, outlines the investment climate in Albania, taking into special consideration the way taxation system is affecting Foreign Direct Investments (FDI), as well as pros and cons of investing in Albania. ***Chapter Six*** deals with the conclusions of this scientific work and provides answers to the research questions related to the topic, giving recommendations to future development.

CHAPTER 2 – The development history of the Albanian Tax System

Section 2.1 – What is expected in this chapter?

The tax system in Albania has been in a continuous development throughout the establishment period of the Republic and Kingdom of Albania until today. An in-depth historical study of Albania and the analysis on Albania's tax system are crucial indicators of the evolution this tax system has undergone throughout the establishment period. The aim of this chapter is to give an overview of the tax system's development in my country. Among other things, it will also put in evidence the steps of progress starting from the Republic of Albania establishment period until today.

Throughout this chapter, apart from the historical description, I will analyze the political and economic reasons that have contributed in the regulation of the taxation system in my country. An in-depth analysis is crucial towards expanding our knowledge concerning the Albania's tax system evolution. The Reign period has perceived the rapid development of this tax system being assessed as sufficiently developed and modern for the time. In conclusion, this chapter will mainly focus on the period from 1990 to 2016, during which the Albanian tax legislation has completed its development, and continues to implement the European Union's "*Acquis Communautaire*[1]".

I have divided the history of Albanian tax system development into three historical periods as follows:

1. *The establishment of the Republic and Kingdom of Albania (1925 - 1944)*
2. *The Communist/Socialist Regime (1945 - 1990)*
3. *Democratic Era (1990 - nowadays)*

Section 2.2 – The establishment of the Republic and Kingdom of Albania

The tax system has faced drastic changes during the establishment period. The fiscal reform aimed in the recovery and development of agriculture and animal husbandry, by mitigating the effects of the financial crisis effects and reducing excess burden of taxation. Various attempts made up to reform the tax system on June 1924, failed because of the political situation. The economic crisis,

[1] Acquis Communautaire, this term is referred to the accumulated legislation, directives, regulations and court decisions which constitute the body of EU law.

the dramatic refusal to pay taxes and the failures in implementing reforms promised by the government, prevented the tax system realization and implementation.

In political terms, the efforts made to improve the tax legislation had a pivotal role. They were fundamental in the fulfillment of country's needs for development. In economic terms, the policies consisted in the creation of new sources of tax revenues for the state budget. Their main aim was to increase the tax collection level. Instantly, the development of the national economy started to soothe the consequences of the crisis for the population. The effects in tax change system concerning the removal of inherited privileges, the country's economic development and the crisis alleviation, relieved the country's tension.

The design of the tax system was oriented towards an intensive development from 1925 to 1939. During this period, *King Zog*[2] enacted several laws and decisions for the collection of the arrears aiming to improve the tax legislation. The further development of the taxation system and the tax policy of that period was characterized by:

a) *Introducing comprehensive tax laws and regulations based on international experiences;*
b) *Establishing and improving tax administration, particularly tax collection capacities;*
c) *Developing customs laws and customs administration;*
d) *Introducing certain incentives, relief and tax exemption for foreign investments/capital;*
e) *Increase of the tax burden and efficiency of tax collection, improving tax revenues.*

Subsection 2.2.1 – Taxation principles

On 1 December 1928, the "*Statute of the Kingdom of Albania*" was enacted. This Statute set the basic principles of taxation[3]. These principles were:

a) *Taxes are an obligation in conformity with the laws into force;*
b) *Taxes are only assigned and collected by law;*
c) *Tax privileges are prohibited;*
d) *Any discharge or modification of taxes and duties cannot be done except by law;*
e) *Monopolies are prohibited except by law and in favor of the State and Municipalities.*

[2] Ahmet Zogu was the leader of Albania from 1922-1939 serving as Prime Minister, President and finally as a King.
[3] Statute of the Kingdom of Albania, Title III 'Finances of State', chapter I 'Finances', articles 141-145.

The taxation system's power stemmed from this statute which stipulated: "*Taxes are an obligation of the Albanian people to defray the general expenses of the State*". These were the first made efforts which established a tax system based on accurate principles. At that time, the applied tax system basically maintained and ameliorated the previous Ottoman tax system. Moreover, elements from the western countries got incorporated in the tax system, improving the use of new methods in the field of taxation. In general, during King Zog's period, Albanian economy faced a significant growth with the continuous economic increase and development of a comprehensive tax system. Meantime, a record-keeping system was adopted and elaborated, in which accounting expertise took place.

Section 2.3 – The Communist/Socialist Regime

This period begins with the end of the *World War II*[4] and ends with the fall of the *Socialist system (1944-1991).* After World War II, the government in force pursued a policy of annihilation of the previous tax system, establishing a new tax system as a main policy. From 1945 to 1975 the main aim of this new tax system consisted in the weakening of the private property, whereas from 1977 to 1990 the role of this tax system consisted in the abolition of the private property.[5]

The tax policy was formally based on the principles of the *classic socialists*[6]. Considering those principles, the power of this tax system was used as a political and economic instrument for the implementation of high progressive taxes (*up to 80%*) on the highest class of the society. These instruments aimed their economic diminution, limiting the capitalist relations, as well as the economic power of the bourgeoisie. Taxes were used as the main tool leading to the loss of private property and consolidating all properties and tax income to the state.

The tax system formally contained central and local taxes. Both taxes imposed by law were mandatory; being deposited in the state budget at a certain amount and term. The central tax system consisted in taxes collected from the population, which for tax effects were classified based on the residence of the population that lived in the city and countryside. Regarding the population that

[4] World War II, also known as Second World War began in 1939 and ended in 1945.
[5] Iljaz Fishta and Mihal Ziu, *Historia e ekonomisë së Shqipërisë (1944-1960)* (Dita 2004) 148-152.
[6] Classic socialists – this term is referred to socialist leaders like Lenin, Stalin etc.

lived in the city the main taxes were: general income tax generated by the activity of traders and artisans, income tax on wages, income tax on people that were single and income tax on people that were married. In respect of the population that lived in the countryside the main taxes were: general income tax on individual agricultural economies, income tax on *kulaks*[7], the tax on alcoholic beverages and the income tax on the agricultural cooperatives. In addition to the taxes applied to the population whose residence was in the city or countryside, some other local taxes were implemented like: taxes on owners of vehicles like cars, motorcycles, bicycles; tax on animals; market tax; cleaning tax etc.

The private property elimination policy, the country's total isolation from the outside world and the implementation of a tax policy leading to the creation of a centralized system of economy, revealed that the tax system lost its economic competition and plunged the country into a deep crisis. This crisis erupted because of the socialist system inability to proceed efficiently without reforms. The implemented economic system was a "*hybrid system*" which contrasted from the other countries of the communist bloc. In conclusion, an eventual failure of the implemented system was followed by the creation of a tax system based on a free market economy.[8]

Section 2.4 – Democratic era

In Albania, the first legal acts aiming the establishment of a new tax system had its very beginning from 1991-1992. This period coincides with the drafting of the tax legislation, which took shape with his proclamation in January 1992 and subsequently with the approval of the law "*on Income Tax*[9]" on 14 July 1992. During this period, some important laws allowing private ownership and foreign investments were enacted. The Albanian Parliament enacted a "***tax law***" package on January 1992, which created the necessary legal basis in the field of taxes and fees. This package created a necessary new fiscal instrument, providing opportunities to secure public revenues and ease the crisis that the country has been experiencing. This new tax legislation which began to be enforced in 1992, consisted in a simple income tax law, a turnover tax and some other national taxes and fees, can be considered as the base of the new modern tax system.

[7] Kulaks, this term was used in Russia, referring to the higher income farmers who had bigger farms than most of the Russian peasants.
[8] Adriatik Mateli, *Sistemi tatimor në Shqipëri* (Tiranë 2013) 104.
[9] Law no.7585, date 14.07.1992.

The new tax system was developed based on the direct and indirect application of taxes as following:

a) Direct taxes (income tax, small business tax)

b) Indirect taxes (turnover tax - replaced by VAT in 1996, excise tax and customs duties)

Albanian tax system consists in a two-tier system: national taxes and duties (administrated by central government) and local taxes and fees (administrated by local municipalities):[10]

a) National taxes and duties – collected by two main agencies that are: Central Tax Administration/General Tax Directorate and Customs Administration;

b) Local taxes and fees – administrated and collected by tax offices of municipalities.

The Albanian tax policy institutions, supported by related international organizations, intended to establish a modern tax system based in self-compliance. The fiscal authority was based on the good will of the taxpayers to fulfill their tax obligations. During this period, the shifting of the centralized economy system into a free market economy was fundamental, in which the main characteristic would be the private property. This shifting was realized by relying on the experience of Central and Western Europe countries. The fiscal reform aimed a radical change which lead to the formation of a tax system with modern fiscal instruments, reorganizing all its components within the tax system. A rational and effective tax system must be accompanied with a prudent and effective policy, which provides instruments and mechanisms of a market economy that applies direct and indirect taxes relying on a proportionate form of taxation.

Subsection 2.4.1 – The tax reform in a timeline

1991-1995 – This period is the beginning of a new tax system development. New economic instruments were presented in the country's market by the new fiscal package. The tax legislation conscription started on 1991 and got implemented on 1992. The Parliament enacted a new fiscal package on March 1993. In the field of taxation, the politics were characterized by the intensification of taxation of all economic entities operating in the country. An increase of taxes and the level of tariffs, aimed the increase of public revenues to satisfy the country's economic needs. The tax legislation relied on these policies through the improvement of a required set of laws, rules and norms, which forced businesses and citizens to pay taxes. During this period, many

[10] Al-tax, 'Fiscal Studies' <www.al-tax.org> assessed 27 March 2017.

laws were drafted and enacted. Among all, the ones of a high importance are: the law on "*Excise*[11]", the law on "*Income tax*[12]" and the law on "*Profit tax*[13]".

1995-2002 – The legislative package implemented by the state, entirely upgraded the previous tax system. This legal package applied modern elements and implemented new methods in the field of taxes. The country's growing needs for money demanded the implementation of a modern tax system to increase public revenues and accordingly distribute these public revenues for the economic and social development of the country. Due to these reasons, the tax administration had the right to use indirect methods of control assessing the tax liabilities of taxpayers when they violate the governing tax laws.[14] In the development process of the tax legislation, the expert assistance of the *International Monetary Fund (IMF)* provided a huge contribution, particularly influential for the continual expertise of the *Fiscal Affairs Department* of the *IMF*.

The legal package maintained the principles of the previous tax system which was based on two important group of taxes: indirect taxes and direct taxes. ***Indirect taxes*** were developed with a new type of tax (*VAT*[15]*)* and with the amendment of the law "*on Excise duties*[16]*"*, whereas ***direct taxes*** were enriched and developed with new elements like: *Income tax*[17]*, Profit tax, Small business tax*[18]*, National taxes and Gambling taxes*.

2002-2016 – The tax system simply maintained and improved the legal package of the previous years. The tax legislation enhancement is made obvious in the collection and administration of social security contributions by the tax authorities. That period got characterized by the continuous change and improvement of the tax legislation, as well as the reconstruction of tax administration. The legal changes aimed the implementation and consolidation of the modern tax system by enacting laws, regulations and modern procedures for the administration of taxes and fees. As a result, many of the previous tax laws were further developed and amended.

[11] Law no.7678, date 03.03.1993.
[12] Law no.7585, date 14.07.1992.
[13] Law no.7677, date 03.03.1993.
[14] Zef Preçi, *Probleme të rritjes ekonomike në Shqipëri* (QSHKE 1999) 124.
[15] Law no.7928, date 27.04.1995.
[16] Law no.8976, date 12.12.2002, amended the previous law on '*Excise duties*' (see 11).
[17] Law no.8438, date 18.12.1998, amended the previous law on '*Income Tax*' (see 12).
[18] Law no.8313, date 26.03.1998.

CHAPTER 3 – Albanian Tax System

Section 3.1 – What is expected in this Chapter?

This chapter summarizes the Albanian tax system and customs legislation. The Albanian tax legislation, including by-law provisions consists in several thousand pages of legal provisions. Hence, this summary highlights only the main basic principles and rules. There are no detailed explanations shown on related provisions, procedures and technicalities. Considering Albania's updated tax legislation, this chapter highlights the basic rules in the field of taxation.

A rapid change and development of the new tax legislation paves the way towards the development of collaborative economy. In some cases, it contains contradictory or unclear provisions giving no exact rulings in certain situations. Tax law provisions are subject to many changes. Consequently, the implementation of new regulations and procedures are not often associated with adequate information and related tax services. This leads to unintentional mistakes by taxpayers who may produce additional tax dues and penalties. Contradictory provisions with no clear technical rulings create alternations in interpreting of these rules. Therefore, the considerable mistakes by the tax audit inspectors, may lead again in an unclear situation. Regarding this, there is a continuous need for updating tax law provisions and procedures writing authorization within the *General Tax Directorate (GTD)* and *Tax Policy Directorate (TPD)* in the Ministry of Finance. The responsible authorities produce technical rulings on tax law implementation and related regulations, as well as interpret and implement the conventions for the avoidance of double taxation.[19] The Albanian tax legislation is subject to continuous amendments, developments and changes due to a rapid economic development that Albania is experiencing.

Section 3.2 – Tax concepts and principles

Taxation is defined as the process by which the State, through its law-making body races revenue uses, to defray expenses of the government. With the term "*tax*" we must understand, 'compulsory payments, exacted by the State that do not confer any direct individual entitlement to specific goods or services in return. A key characteristic of taxation in modern tax systems is that taxation

[19] <www.tatime.gov.al> assessed 11 April 2017, here you can find all the informations related to Albanian tax system.

is "*parametric*": in other words, it is governed by legislation which defines in advance the basis of individual tax liability.'[20]

Taxes and fees are the core of the Albanian tax system, constituting the main source of income in the State's budget. According to the law "*on the tax procedures in the Republic of Albania*[21]", the term "*tax*" is referred as follows: "Tax is a mandatory and refundable payment in the State's Budget or in the budget of local government bodies, established by law, which is not done in exchange of certain goods or services".

There are four main principles governing in the Albanian tax system:[22]

1. *Principle of legality* – the rules, values and ways of collection of all kind of taxes and duties shall be drafted and assigned by law.
2. *Annual principle* – according to which, the parliament must annually give to the government the authorization for the collection of taxes.
3. *Principle of equality* – according to which, the tax burden should be proportionate to the taxpayer's ability to pay.
4. *Principle of convenience* – according to which, taxes should be collected in a way and time that is convenient to the taxpayer.

Taxes are among the most important economic instruments in the collection of public revenues and have even been presented in a variety of forms in the Albanian tax legislation. Under the Albanian legislation, considering the time of the income creation and its spending time, taxes are divided into two parts: direct and indirect taxes. According to this criterion, taxes paid at time of income creation represent the group of direct taxes, whereas taxes paid at the time of income expenditure are included in the group of indirect taxes. Examples of direct taxes are: income tax, profit tax, small business tax, national taxes and gambling tax. Examples of indirect taxes are: value added tax *(VAT),* excise tax and customs duties.

[20] Stephen Smith, *Taxation, a very short introduction* (Oxford University Press 2015) 4-5.
[21] Law no.9920, date 19.05.2008, Article 5, para ë.
[22] Hastings Lyon, *Principles of Taxation* (Bibliobazaar 2009) 98.

Section 3.3 – Overview of the Albanian tax system

The Albanian tax system consists of:

1. National taxes and duties
2. Local taxes and fees
3. Tax procedures
4. Tax authorities
5. International tax treaties

Table 1

Subsection 3.3.1 – National taxes and duties

National taxes and duties consists of:

1. Income taxes
2. Social security taxes
3. Value Added Tax (VAT)
4. Excise tax
5. Gambling taxes
6. Other national taxes and fees
7. Customs duties

Table 2

3.3.1.1 Income taxes – are regulated by the law "*on income tax*[23]" and are divided in three forms:

- *a) The personal income tax*
- *b) The corporation income tax (profit tax)*
- *c) Withholding tax*

The personal income tax – The personal income tax is based on the principle of residence. Resident individuals are taxed on their worldwide income, whereas non-residents are taxed only on the Albanian sourced income. The residence principle is regulated under this law in very simple terms. A resident is an individual, who has a permanent establishment in Albania[24], and

[23] See 17.
[24] Law no.8438, date 28.12.1998, Article 3, para 1.

continuously or intermittently stays in Albania for more than 183 days during the taxable year[25]. In addition, a resident is also a legal person whose headquarter is in Albania.[26]

As mentioned above, resident individuals are taxed on their worldwide income, but the law does not provide clear definitions or procedures, particularly regarding taxation of the foreign sourced income. For all these reasons, definitions or procedures regarding the taxation of the foreign sourced income should be immediately implemented. The taxation of the personal income is mostly based on a withholding tax system, obliging companies or entrepreneurs to withhold tax on payments done to individuals. In most of the cases this tax levied on payments is the final one.

Personal income tax is levied on the following categories of income:[27]

a) *Income from wages and other dependent services;*
b) *Income from dividends as a shareholder in a company or the profit as a partner;*
c) *Interest income or income from bonds, securities and treasury bills;*
d) *Income derived from copyright and intellectual property;*
e) *Income from rents and royalties;*
f) *Net income from immovable properties;*
g) *Net income from sale of shares or other securities;*
h) *Other personal incomes.*

Personal income tax is levied at a flat rate of 15% on gross income. Exemptions from this general rule are incomes from salaries, income from sale of immovable properties and income from the sale of shares. Incomes from salaries are taxed in a progressive basis, whereas the other two are taxed on a net basis. Albanian tax system exempts certain categories of income from the personal income tax. According to the law "*on income tax*" the following incomes are exempted:[28]

a) *Income generated as the result of compulsory insurance of social security and healthcare scheme, as well as economic aid to families and individuals with no incomes or low incomes as set out in the relevant legislation;*

[25] Law no.8438, date 28.12.1998, Article 3, para 2.
[26] Law no.8438, date 28.12.1998, Article 3, para 3.
[27] Law no.8438, date 28.12.1998, see Article 8.
[28] Law no.8438, date 28.12.1998, see Article 8/1, *exempted incomes*.

b) *Scholarships of pupils and students;*
c) *Benefits received in the cases of diseases or accidents, in accordance with relevant provisions and legislations;*
d) *Income received, both monetary and in kind, given to the owners of properties as a bonus for expropriation made by the state for public interests;*
e) *Income exempted under international agreements ratified by the Parliament;*
f) *Income from compensations taken with Court decisions;*
g) *Income received from the institutions of the State for achievements in science, sport, culture*
h) *Contributions from the employer for the life and health insurance of the employee;*
i) *Income received because of financial compensation to former owners and former political prisoners.*

As it is explained above, incomes from salaries are taxed on a progressive basis. The Income Tax Law does not grant any personal allowances or deductions from the taxable income. Tax exemption is given only for monthly salaries below 30.000 Albanian LEK[29] (ALL). As it can be seen from the table below, the part of monthly salary over 30.000 ALL but below 130.000 ALL is taxed at a rate of 13%. The part of the monthly salary over 130.000 ALL is taxed at a rate of 23%. The new government that came into force in 2013, approved this new form of taxation reasoning that this progressive tax system helps to provide a solution against income inequality – who earns more will pay more and who earns less will pay less. Taxation systems that apply taxation in progressive rates offer also higher overall levels of revenue, elevating nation's benefits. More than 80% of the countries in Europe apply this form of taxation.

MONTHLY INCOME		**TAX RATE (%)**
From (*ALL*)	To (*ALL*)	
0	30.000	0%
30.001	130.000	+13% of the amount over 30.000 *ALL*
130.001	Over	13.000 *ALL* + 23% of the amount over 130.000 *ALL*

Table 3[30]

[29] *LEK* – is the Albanian currency.
[30] Table 3 – Employment income tax, <www.financa.gov.al> assessed 5 April 2017.

The employment tax must be monthly withheld from salaries, payments and wages, being remitted to the related tax office monthly. Employers should register perforce in the related tax office, which withholds the employment tax and social & health insurance contributions from their employees' gross salaries. Employment income tax and social & health insurance contributions withheld from employees, as well as employer's part of social & health insurance contributions must be paid to the regional tax directorate where the employer is registered within day 20 of the coming month.[31]

Individual income derived from the sale of immovable properties, including land and/or buildings is taxed at a flat rate of 15% on net basis. Income from the sale of shares of any kind is also taxed at a flat rate of 15% on net basis. This means that the positive difference between the selling price and purchasing price is taxed at 15%. Bonuses, allowances, indemnities, benefits in kind and other compensations are generally individual taxable income, or classified as tax nondeductible expenses for the company.

All individual taxpayers, residents in Albania, who have worldwide annual income more than 2.000.000 *ALL,* must fill in the Individual Annual Income Declaration. The individuals who are not residents, having an annual income from sources in Albania more than 2.000.000 *ALL* have the same obligations as well. This declaration needs to be done every year, until April 20 of the previous year.[32]

The corporation income tax (profit tax) – Subject of the corporation income tax are companies or individuals engaged in independent business activities and any other person regardless of juridical form of registration which are registered as VAT taxpayers.[33] Banks are normally subject of corporation income tax, except for Bank of Albania which is profit tax exempted. Profit tax is levied at a general flat rate of 15%.[34] The taxable period has its starting point on January 1st and finishes on December 31st of each calendar year. Albanian tax law applies the principle of

[31] Law no.8438, date 28.12.1998, Article 10.
[32] Law no.8438, date 28.12.1998, Article 13, paras 2-3.
[33] Law no.8438, date 28.12.1998, Article 16.
[34] Law no.8438, date 28.12.1998, Article 28.

worldwide taxation. Thus, resident taxpayers are tax subjects on their worldwide profits, while non-resident taxpayers are tax subjects on the profits derived from sources in Albania.[35]

Exemptions from the corporation income tax (*profit tax*) are:[36]

- *Organs of central and local government;*
- *Bank of Albania;*
- *Juridical persons which exercise only activities of a religious, humanitarian, charitable, scientific or educational character, the profit or property of which is not used for the benefit of the founders or their members;*
- *Labor organizations or chambers of commerce, industry or agriculture, the property or profit of which is not used for the benefit of an individual or one of their members;*
- *International organizations, agencies of technical cooperation and their representatives, and other persons, the tax exemption of which is provided by agreements, as ratified by Albanian Parliament;*
- *The cinematographic film production houses, licensed and subsidized by the National Center of Cinematography*.

Taxable profit is defined as the difference between revenues and related expenses. The determination of the taxable base starts with the profit shown on the balance sheet, which must be corrected with the deductible and non-deductible expenses explained as follows:

- Expenses which allow deduction from the taxable base are those who directly serve to the business profits.[37] Such expenses include depreciation allowances, rent, raw materials, spare parts, power and utilities, insurance premiums, interests, entertainment and other representation expenses. All these expenses must be proved and supported with documents by the taxpayer. The document used for the deduction of the expense is the fiscal invoice, with or without VAT, approved by the Ministry of Finance.
- Expenses which are not deductible for tax purposes are:[38] the cost of buying and improving the land and the site; the cost of buying, improving, renovating and reconstructing the

[35] Law no.8438, date 28.12.1998, Article 17.
[36] Law no.8483, date 28.12.1998, Article 18.
[37] Law no.8438, date 28.12.1998, Article 20.
[38] Law no.8438, date 28.12.1998, Article 21.

assets of the activity, which are depreciated in accordance with the provisions of this law; the increase of the basic capital of the company of the increase of the contribution of any person in the partnership; the value of the compensation in kind; dividends declared and profit distribution for partners; interest, depreciation and any other expenses in excess of the rates or amounts set by the related provisions of this law; fines and penalties arising from the break of legal and contractual provisions; the creation or increase of the reserves and any special funds, except for the cases provided by law; personal income tax, excise duties, profit tax and deductible value added tax; representative expenses which excess the value of 0.3% of the annual turnover; all expenses of a private nature which are not directly related to the business of the enterprise; sponsorship expenses which excess 3% of the profit before tax; expenses for gifts; any other expense, the amount of which is not supported with documents by the taxpayer; expenses for technical, consultancy and management services invoiced by third parties to which it is not paid the withholding tax enters the tax period; loses and scarce during production; transition or storing that excess the norms set by the Council of Ministers; expenses for salaries, remunerations or other forms of personal income not paid by the banking system; cash payments more than *150.000 ALL*.

Business travel and hotel expenses for bank employees, when they travel outside the district for business purposes are a deductible expense for the company. Such expenses must be classified as non-deductible, if they are done for individuals who are not employees of the company or if they are not included in the company's payroll list.

Taxpayers must make quarterly advance payments in conformity with the procedures defined in this law. These advance payments are to be done enter March 30th, June 30th, September 30th and December 30th.[39] The profit tax prepayment calculation is based on the profit tax of the two previous years. By March 31st of the following year, any taxpayer must present to the tax office the annual profit tax return and financial statements, including the accounting balance sheet, statements of profits and loss convoyed with necessary explanations. Capital gains from the sale of company's fixed business assets, are taxed as part of company's ordinary business income and

[39] Law no.8438, date 28.12.1998, Article 30, para 1.

loses may be carried forward for three coming years. Dividends distributed by Albanian resident companies to other Albanian resident companies are not a subject of the corporation income tax – due to the so-called exemption of participation.

Withholding tax – Companies, financial institutions, banks, budgetary institutions or any other legal entity registered in Albania, including entrepreneurs generally called small businesses, are obliged to withhold income tax at a flat rate of 15%. This tax is withheld on the gross amount done to any payment done to Albanian resident individuals or to non-resident individuals, in consideration for services, dividends, interest, royalties, rental income etc. This tax may be decreased to 10%, 5% or 0% if such payments are done to residents of countries with which Albania has a convention for the avoidance of double taxation.

This law "*on income taxes*", defines the obligation of all entities, which are registered to Albanian tax authorities, to withhold 15% tax on payments done to individuals or non-resident persons, either individuals or companies.[40] The withholding tax is a final tax, as such recipients of income that is considered Albanian sourced income are not registered to Albanian tax authorities. This tax is not applicable if the recipient of the income is another Albanian resident, company or individual entrepreneur registered in Albanian tax authorities – as such persons declare and pay income taxes in Albania.

3.3.1.2 Social security taxes – Social and health security contributions in Albania are regulated under the provisions of the law "*on the collection of obligatory social and health security contributions in the Republic of Albania*[41]" and a series of other law and by-law provisions, including several decisions of the Council of Ministers. It is precisely one of the rulings[42] of the Council of Ministers, that regulates the liabilities, tariffs and procedures for calculation and payment of the social and health insurance contributions.

[40] Law no.8438, date 28.12.1998, Article 33.
[41] Law no.9136, date 11.09.2003.
[42] Ruling of the Council of Ministers no.1114, date 30.07.2008.

Under the provisions of the above-mentioned legislation, both employees and employers are obliged to pay social and health contributions which depend on the employees' wage and salary. The social contribution is determined in percentage on the gross salary, and cannot be levied under a certain monthly salary (*22.000 ALL*) and above a maximum salary (*97.030 ALL*).[43] The monthly salary more than *97.030 ALL* is not subject to social insurance contributions. Health contributions are calculated on the gross salary amount without minimum or maximum levels. The Council of Ministers has the right to determine the level of the minimum and maximum salary for social insurance calculation purposes.

In the Republic of Albania, health and social security contributions are levied at a rate of *27.9%* of the gross salary as follows:[44]

- *16.7%* by the employer, *15%* for social security contributions & *1.7%* for health contributions;
- *11.2 %* by the employee, *9.5%* for social security contributions & *1.7%* for health contributions.

The insurance contributions are calculated and withheld by the employer and must be remitted monthly to the related tax office, not later than date 20 of the coming month. Self-employed persons pay social insurance contributions which are calculated at a rate of 23% of the minimum gross salary (*22.000 ALL*) and 3.4% on the double value of the minimum gross salary.[45] The Government has defined a minimum monthly salary which is *22.000 ALL* and under this minimum salary employers are not allowed to hire employees. The payment of the social and health security contributions has priority compared to other taxes or debts of individuals constricted to pay such contributions under the provisions of the above-mentioned legislation. The benefits deriving from the social security system are not taxable in Albania.

3.3.1.3 The Value-Added Tax (VAT) – The Value-Added Tax in Albania was first implemented, based on the law "*on Value-Added Tax*[46]" in 1995. This new type of tax brought an innovation in

[43] Ruling of the Council of Ministers no.1114, date 30.07.2008, Chapter 2, para 2.
[44] Ruling of the Council of Ministers no.1114, date 30.07.2008, Chapter 3, para 3.
[45] Ruling of the Council of Ministers no.1114, date 30.07.2008, Chapter 3, para 6.
[46] See 15.

the Albanian tax system. VAT is the most uncontested type of tax that generates the most income in the fiscal budget of Albania. The application of VAT made the Albanian tax system to develop a comprehensive understanding of the process. 'VAT is a general tax on consumption of goods and services, proportional to their price, which is charged at each stage of production and distribution process without tax price. VAT is applied to all supplies of goods and services performed against payment within the territory of the Republic of Albania, by a taxable person acting as such and on all imports of goods in the territory of the Republic of Albania.'[47] During the last decade, the revenues from VAT faced a significant growth. This tax has been in the center of numerous political and legal debates that lead in the amendment of the previous law. For these reasons, in 2014, these debates lead to the adoption of the new law "*on Value-Added Tax*[48]".

VAT taxable persons are the juridical individuals; or any other person who carries out an economic activity, independent form the purpose or citizenship of an individual.[49] Such persons are the ones, whose annual turnover have exceeded or will exceed the amount of *5.000.000 ALL*. Taxable supply means a supply of goods and services; the import of goods in Albania other than certain exempt supplies as provided by the provisions of this law.
The time of the supply shall be considered the time when the invoice for the goods or services is issued.[50] A person making a taxable supply must issue an invoice immediately after the time when the goods are delivered or made available to the purchaser, or the time of service provision. When a person makes a taxable supply, and receives payment for the supply before goods are delivered, made available to the purchaser or services are rendered, this person is obliged to issue an invoice for the supply, at or immediately after the time of receiving the payment.

The place of supply varies in case of goods and service supplies. In the case of good supplies, the place of the supply is in Albania if the good delivered is physically in Albania when it is made available to the purchaser. If the delivery or availability involves the transportation of the goods, the place of the supply is in Albania, if these goods are sent from Albania to another country. If

[47] VAT definition by GDT <www.tatime.gov.al/eng/c/6/71/value-added-tax> assessed 12 May 2017.
[48] Law no.92/2014, date 24.07.2014. This law is partially harmonized with the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [2006] OJ L347/1 1-118, amended.
[49] Law no.92/2014, date 24.07.2014, Chapter 2, Article 3, para 1.
[50] Law no.92/2014, date 24.07.2014, Chapter 3, Section 1, Article 9.

these goods are sent from another country, the place of supply depends on who is importing them.[51] For example, a supply of electricity, water or gas is designed to be supplied in Albania, when the supplier (reseller) has its headquarters in Albania, otherwise the place of supply for these goods is in the place where the consumer has consumed them.[52]

In the case of the place of services supply, for services provided to a taxable person, the place of the supply is where the recipient has established his business or has created his first establishment. In the case of services provided to a non-taxable person, the place of the supply is where the supplier has established his business.[53]

Considering definitions, the phrase "*importation of goods*" has the same meaning as in Customs Law. The importation takes place at the time provided in customs law, whether the imported goods are subject to customs duties according to that law. The taxable value of the taxable supply is the total payment for this supply, except as otherwise provided on VAT law.[54] The taxable value of the supply includes tariffs, taxes, duties and other similar payments except from VAT. The taxable supply of the imported goods is comprised of the import specified value by the Customs Authorities, based on customs legislation of the Republic of Albania. In Albania, the rate of the value-added tax[55] for the supplies of goods and services is ***20%***, except for the cases when 0% tax rate is applicable as provided in the VAT law. The taxable period is a calendar month.

In this context, it is important to mention that there are some VAT exemptions from the taxable supplies. Albanian VAT is a broad-based tax with minimal exceptions which are the following:[56]

- Postal services supply and other accessory goods in this service supply:
- Supply of medicines, active implantable medical devices and implantable medical devices;
- Supply of health services and other activities strongly related to them;
- Supply of services performed by independent groups of persons carrying on an activity exempt from VAT or which don't have the quality of a taxable person;

[51] Law no.92/2014, date 24.07.2014, Chapter 4, Section 1, Article 19.
[52] Law no.92/2014, date 24.07.2014, Chapter 4, Section 1, Article 21.
[53] Law no.92/2014, date 24.07.2014, Chapter 4, Section 1, Article 21, para 2.
[54] Law no.92/2014, date 24.07.2014, Chapter 6, Articles 36-39
[55] Law no.92/2014, date 24.07.2014, Chapter 7, Article 48.
[56] Law no.92/2014, date 24.07.2014, Chapter 8, Section 1, Articles 51-53.

- Goods and services provided in return for reduced payments by non-profit organizations, which have the status of "non-profit organizations for public benefit" and by religious or philosophical organizations;
- Educational, cultural, sport services and other services with public interest;
- Services supplied by public Albanian radios and televisions;
- Insurance and re-insurance services;
- Granting and negotiation of credit, as well as management of loans by lenders;
- Negotiation or any other agreement guaranteeing loans or any other security for money and the management of credit guarantees by lenders;
- Transactions including negotiation concerning exchange operations;
- Deposits, current accounts supplying liquidity through payments, transfers, debt-making awards, checks and other negotiable instruments, except debt collection services;
- Transactions, including negotiation concerning currency, bank notes or coins, used as legal tender, except for coins and banknotes for collection, namely gold coins, silver or any other metal coins or banknotes that are not normally used as legal tender payment of interest or numismatic coins;
- Management of investment funds, in terms of the law on "*collective investment undertakings*[57]";
- A pre-value supply of postage stamps for use of postal services in the Republic of Albania and other similar stamps;
- Gambling activities and casinos;
- Supply of buildings or parts of building, as well as the supply of land on which the building stands, in addition to supplying the construction process and rent;
- Supply of goods and services used only for an exempted activity;
- Supply of identity cards for citizens;
- Supply of books and newspapers;
- Supply of advertisement services from written and electronic media;
- Supply of services intended only for the research phase of petroleum operations, carried out by contractors or subcontractors;

[57] Law no.10198, date 10.12.2009.

The import of machineries and equipment's can profit from a deferred payment system. Under this payment system, VAT should not be paid on such machineries at the Customs Office in the period of import. Apart from this, Albanian tax legislation provides for zero-rated supplies, which are very important. The VAT rate is 0 on the following transactions:[58]

- Exportation of goods from the territory of the Republic of Albania;
- International transport of goods and passengers;

In contrast to a transaction involving an exempt supply, VAT could be recovered in the case of a zero-rated supply input.

The tax credit[59] for a tax period is the total VAT in respect of all taxable supplies made to the taxable person during the tax period by other taxable persons and all importations of goods made by a taxable person during this tax period, where those supplies and importations were made for the purposes of taxable supplies, made or to be made by a taxable person. In other words, VAT paid on goods and services used in a VAT person's business that are purchased from other persons liable to taxation during the taxable period and VAT paid on imported goods during the taxable period, are in both cases recoverable (*creditable*). Reimbursement of VAT is allowed if the excess tax credit is carried for three successive months and the claimed reimbursement exceeds the sum of 400.000 ALL.[60]

The VAT "*reverse change mechanism*" is applicable on import of services from Albanian VAT taxpayers. The application of VAT reverse charge for imports of services was made obligatory from May 2008. The Instruction of the Minister of Finance[61], regulates all the procedures for VAT reverse charge application in import of services. In such cases, the Albanian company which receives services from non-resident companies is considered for VAT purposes, as having been supplied with such service within Albania, and the Albanian company is required to apply the VAT "*reverse change mechanism*".[62]

[58] Law no.92/2014, date 24.07.2014, Chapter 8, Section 3, Subsection 1.
[59] Law no.92/2014, date 24.07.2014, Chapter 9, Section 1, Article 69, para 1.
[60] Law no.92/2014, date 24.07.2014, Chapter 9, Section 4, Article 77, para 1.
[61] Instruction of Minister of Finance no.17, date 13.05.2008.
[62] Instruction of Minister of Finance no.17. date 13.05.2008, para 4.

Under this approach, the company issues a VAT invoice where the seller and the buyer are stated at the same time. The value of the service is the amount of the invoice issued by the non-resident service provider, leading to the calculation of the Albanian VAT rate of 20% over that amount. This invoice is registered in both VAT purchasing book and VAT sales book. In the case of a VAT taxpayer who has only VAT-able supplies the VAT effect from the "reverse charge" is zero. The situation is not the same for companies, whose basic activity is VAT exempted, therefore input VAT is not creditable for the company. Thus, the reverse charge increases the payable VAT for the company. On one hand, financial services are VAT exempted, but on the other hand in the case of import of financial services, the companies are not required to implement the VAT "*reverse charge*". In the following table are shown VAT rates in some countries near Albania.

COUNTRY NAME	VAT RATES %
ALBANIA	**20**
GREECE	**23**
SERBIA	**20**
MACEDONIA	**18**
CROATIA	**25**
MONTENEGRO	**17**
ROMANIA	**24**

Table 4[63]

3.3.1.4 Excise tax – The excise taxes are regulated by the law on "*Excise duties in the Republic of Albania*[64]". This law defines manufacturing general rules; holding, storing, movement and control of excise goods, by setting specific rules on excise duties applied on the consumption of energy products, alcohol and alcoholic beverages, tobacco and its by-products.[65] Excise duties are levied on the domestic consumption of certain goods and are administrated by the Customs Authorities. For excise goods, the excise duty occurs at the releasing time of these consumption goods in the

[63] Table 4, VAT rates in some of the Balkan countries.
[64] Law no.61/2012, date 24.05.2012. This law is partially harmonized with the Council Directive 2008/118/EC of 16 December 2008 concerning the general arrangements for excise duty and repealing Directive 92/12/EEC [2008] OJ L9/12 30.
[65] Law no.61/2012, date 24.05.2012, Article 1.

territory of the Republic of Albania.[66] Goods exempted[67] from the excise duties are those intended to be used: for official and personal purposes in the frame of diplomatic and consular missions; for official and personal purposes of International Organizations recognized as such by the Republic of Albania; for the armed forces of any Member State of NATO with the exception of Albania's armed forces; excise goods imported in the personal luggage of passengers or imported by other means of international transportation, taxed according to the limits prescribed in the customs legislation; exported goods like fuel, fishing equipments, energy products etc. Exemption from payment of excise duties is also granted to excise goods delivered by Duty Free shops and carried as personal luggage by the passengers leaving Albanian territory by air or sea.[68] These are the exemptions from excise duties provided in the Albanian legislation.

The following tables show some of the most important imported goods, subject to an excise tax under the Albanian tax legislation. Daily consumption goods like: coffee, energy drinks, alcohol and tobaccos represent the main goods imported in the territory of Albania.

CATEGORIES OF COFFEE	EXCISE RATE (ALL/kg)
Non-roasted coffee	0
Roasted coffee	60
Coffee husks & skin	50
Extract, essences and concentrates of coffee	250

Table 5[69]

PRODUCT	EXCISE RATE (ALL/liter)
Energy Drinks	30

Table 6[70]

[66] Law no.61/2012, date 24.05.2012, Article 4.
[67] Law no.61/2012, date 24.05.2012, Article 10.
[68] Law no.61/2012, date 24.05.2012, Article 12.
[69] Table 5 – Excise duties on *Coffee* (General Custom Directory).
[70] Table 6 – Excise duties on *Energy Drinks* (General Customs Directory).

CATEGORIES OF ALCOHOLIC PRODUCTS	DESCRIPTION OF PRODUCTS	EXCISE RATE (ALL/HL)
Beer	Beer made of malt in quantities up to 200.000 hectoliters/year	360
Beer	Beer made of malt in quantities more than 200.000 hectoliters/year	710
Still wine & still fermented beverages	Still wine in quantities up to 10.000 hectoliters/year	3.000 for wine of an actual alcoholic strength up to *12.5%* vol.; 4.000 for more than *12.5%* vol.
Still wine & still fermented beverages	Still wine in quantities more than 10.000 hectoliters/year	10.000 for wine of an actual alcoholic strength up to *12.5%* vol.; 12.000 for more than *12.5%* vol.
Sparkling wines, Champagne & fermented beverages	Spumante, Champagnes and Sparkling wines	5.200
Intermediate alcohol beverages	Intermediate alcoholic beverages of an actual alcoholic strength by volume exceeding *15%* vol., but not exceeding *22%* vol.	5.200
Alcoholic beverages (Sprits)	Alcoholic beverages in quantities up to 20.000 hectoliters/year	65.000/hL of anhydrous alcohol
Alcoholic beverages (Spirits)	Alcoholic beverages in quantities more than 20.000 hectoliters/year	84.500/hL of anhydrous alcohol
Non-denatured ethyl alcohol	Non-denatured ethyl alcohol of an actual alcoholic strength 80% vol. or more	45.000/hL of anhydrous alcohol
Denatured ethyl alcohol	Denatured ethyl-alcohol	0
Albanian Raki	Albanian Raki	20.000/hL of anhydrous alcohol

Table 7[71]

CATEGORIES OF TOBACCO	DESCRIPTION	EXCISE RATE
Cigars & Cigarillos	Cigars & cigarillos containing tobacco	2.500 *ALL*/kg
Cigars containing tobacco	Cigars containing tobacco	5.500 ALL/1.000 items; From 1 January 2016 – 6.000 *ALL*/1.000 pieces.

[71] Table 7 – Excise duties on *Alcoholic products* (General Customs Directory).

		From 1 January 2017 – 6.500 *ALL*/1.000 pieces.
Cigars, cigarillos & cigarettes containing tobacco substitutes	Cigars, cigarillos & cigarettes containing tobacco substitutes	2.240 *ALL*/kg
Other manufactured tobacco & tobacco substitutes	Other manufactured tobacco & tobacco substitutes; "homogenized" or "reconstituted" tobacco; tobacco extracts and essences	4.400 *ALL*/kg; From 1 January 2016 = 5.100 *ALL*/kg. From 1 January 2017 = 5.800 *ALL*/kg.

Table 8[72]

3.3.1.5 Gambling Taxes – In the Republic of Albania, the taxation of gambling activities is regulated under the provisions of the law "*On games of fortune*[73]". The purpose of this law[74] is to establish the necessary legal framework for the organization, conditions of game chance operations and to allow such companies to exercise this activity. This purpose includes: the organization and functioning of Gambling Supervisory Authority (GSA); supervision and control of the activities of the chance game organizers; gambling licensing; rights and obligations of the operators of the games of chance and distribution of income from gambling. Gambling categories[75] exercised in the Republic of Albania are: sports bets, bets for track races, casinos/casinos established in 5 star hotels, electronic casino, national lottery and television bingo. The field of application of this law includes entities that exercise the activities mentioned above.

The Gambling Supervisory Authority is the responsible institution for licensing, supervising and controlling the legal exercise of the activity organizers in the field of gambling. GSA is a public legal entity, with its headquarters is Tirana and under control of the Minister of Finance.[76] The Prime Minister approves GSA organizational structure with the proposal of the Minister of Finance, in accordance with the legislation in force. GSA is composed of control inspectors, certification inspectors for gambling equipment and inspectors for enforcement of coercive measures. Head of the GSA is appointed by the Minister of Finance, in accordance with the legislation in force.[77]

[72] Table 8 – Excise duties on *Tobaccos* (General Customs Directory).
[73] Law no.155/2015, date 21.12.2015.
[74] Law no.155/2015, date 21.12.2015, Article 2.
[75] Law no.155/2015, date 21.12.2015, Article 5.
[76] Law no.155/2015, date 21.12.2015, Chapter II, Article 10.
[77] Law no.155/2015, date 21.12.2015, Chapter II, Article 11.

Gambling activities that are taxed under the provisions of this law are exempted from the value-added tax[78]. Gross gambling revenues for all categories of gambling as specified above are subject to a 15% monthly gambling tax, determined as the amount left to the operator from the difference between the total amounts played by the participants and the amount earned by them. This amount is payable at the Regional Tax Directorate within the 15th of the following month.[79]

3.3.1.6 Other national taxes and fees – In the Republic of Albania, other national taxes and fees are regulated under the provisions of the law "*On national taxes and fees*[80]". The purpose of this law is to define the types of national taxes and fees that apply in the Republic of Albania, the level of national taxes, calculation procedures and collection, the transfer of the national taxes and fees to the State's Budget, as well as duties belonging to the tax agents.[81] National taxes are[82]: port tax, circulation tax for petroleum, tax on used vehicles, mineral rent tax, act & stamp tax, the carbon tax on gasoline, tax for the exercise of fishing activity, packaging tax, tax on written insurance premiums except of life insurance premiums and some other minor taxes and fees. The tax rates on the national taxes and fees are:[83]

- *Port tax* – 1 Euro. This tax is paid for each touch, for all ships entering in the ports of the territory of the Republic of Albania carrying out business transactions.
- *Circulation tax for petroleum* – 27 *ALL*/liter for petrol and 27*ALL*/liter for gasoline.
- *Tax on used vehicles* – This tax is annual and valid for 365 days. This tax is determined according to the formula: cylinder in cm^3 x fixed coefficient by age x fixed fee for the type of fuel. Fixed fee for the types of fuel are: 12.5 *ALL* for diesel and 10 *ALL* for gasoline.
- *Carbon tax* – The carbon tax is levied: 1.5 *ALL*/liter for petrol; 3 *ALL*/liter for gasoline; 3 *ALL*/kg for coal; 3 *ALL*/liter for solar; 3 *ALL*/liter for fuel oil; 3 *ALL*/liter for kerosene; 3 *ALL*/kg for petroleum coke.
- *Packaging tax* – Plastic packaging tax is fixed at a rate of 100 *ALL*/kg and is exercised on both, imports and domestic productions. Only for local recycling industry, packaging taxes produced from recycled plastic waste generated in the country shall be set at 1 *ALL*/kg.

[78] Law no.155/2015, date 21.12.2015, Chapter 11, Article 52, para.1.
[79] Law no.155/2015, date 21.12.2015, Chapter 11, Article 52, para.2.
[80] Law no.9975, date 28.07.2008.
[81] Law no.9975, date 28.07.2008, Article 1.
[82] Law no.9975, date 28.07.2008, Article 3.
[83] Law no.9975, date 28.07.2008, Article 4.

- *Tax on written insurance premiums* – Taxes on written premiums, excluding insurance premiums for life products, travel health and green card, is 10% of the premium's sum.

3.3.1.7 Customs duties – The Albanian Customs Code regulates the customs duties applied in the territory of Albania. The Customs activity ensures the interests protection of the Republic of Albania, concerning imports, exports and goods in transit, regardless of the way of transport, with respect to international shipments, border crossing and free circulation of goods, persons and their luggage.[84] Customs duties are levied on all goods being imported in the Republic of Albania, except in the cases provided in customs legislation. The customs value of imported goods is the transaction value and includes the price of the commodities shown in the invoice, transport and insurance cost.[85] Customs authorities, for the purposes of assessing the custom duty, have the right to use reference prices, based on market prices. This happens in cases of uncertainties, in which abusive prices may be shown on the invoice. The customs value is stipulated on the customs declaration, when goods are declared for a customs-approved treatment or use.

The customs duties are only *ad-valorem*[86]. There are six rates of customs duties: 0%, 2%, 5%, 6%, 10% and 15%, which form the so-called "*conventional or basic rates*" and are applied under the principle of the "*Most Favored Nation*". Albania has shifted in a liberal trade regime. As a result, most of the goods originating from EU Countries face a 0-tariff rate. The maximum rate of 15% is applied to such products like: jewelry, textiles etc. Customs duties rates are decreasing continuously since Albania joined the World Trade Organization (*WTO*). Other preferential tariff rates, which are always less than basic rates, are applied under Free Trade Agreements (*FTA*) and especially under Stabilization and Association Agreement (*SAA*) with the European Union. Moreover, this is one of the most important benefits that Albania enjoys since being a member of WTO, having a total impact on Albania's economic growth.

The duties assessed must be paid in Albanian Lek (*ALL*). Foreign currencies should be converted using the official exchange rates of the Bank of Albania.[87] New exchange rates are determined each month and are used through all the month, unless the fluctuation of daily exchange rate is

[84] Albanian Customs Code, Chapter 1, Article 2.
[85] Albanian Customs Code, Chapter 3, Article 34, point 1.
[86] *Ad-valorem*, means according to the value of goods.
[87] Albania Customs Code, Chapter 3, Section 4, Article 27.

more than 5%[88]. Exemptions from customs duties are given in cases provided by the customs legislation, which is fully aligned with the international standards in this matter. Specific agreements concluded by Albania, such as the case of aids, soft credits or governmental agreements may provide for exemptions. These exemptions should be expressively mentioned in the concerned governmental agreements; ratified by the Parliament.

Subsection 3.3.2 – Local taxes and fees

In the Republic of Albania, local taxes and fees are regulated by the law "*On the System of Local Taxes*[89]" and consist of:

1. The small business tax
2. The immovable property tax
3. The hotel tax
4. Tax for impact on infrastructure
5. Tax on alienation of immovable properties
6. Motor vehicles tax
7. Other local taxes and fees

Table 9

3.3.2.1 The small business tax – Small business activities are subject to a small business tax. These small business activities are such activities whose annual turnover does not exceed 8.000.000 *ALL*.[90] The businesses with annual turnover from 0 to 5.000.000 *ALL*, are subject to a 0% tax rate, whereas businesses with their annual turnover from 5.000.000 to 8.000.000 *ALL*, are subject to a 5% tax rate on their profit before tax.[91] These tax rates were amended by the winning government on 2013. Any taxpayer subject to simplified profit tax on small businesses is bound by February 10th of the year following the taxable period, to submit an annual statement indicating the details of total income, deductible expenses, taxable income, payable taxes and any other particularities

[88] Albania Customs Code, Chapter 3, Article 40, para 3(c).
[89] Law no.9632, date 30.10.2006.
[90] Law no.9632, date 30.10.2006, Chapter 3, Article 10.
[91] Law no.9632, date 30.10.2006, Chapter 3, Article 11.

prescribed by the instruction of the Minister of Finance for the completion and submission of the annual tax declaration.[92]

3.3.2.2 The immovable property tax – Subject to the immovable property tax are all natural or legal persons, domestic or foreigners, owners or users of the immovable properties in the territory of the Republic of Albania, regardless of the utilization level of these assets. The owner or co-owner and the user of the immovable property are liable to pay the immovable property tax. Taxes on immovable property includes: *taxes on buildings; tax on agricultural land* and *land tax*[93]. The building tax is defined in *ALL/m*^{2} per calendar year and fluctuates due to district categories and the purpose for which buildings are used.[94] For instance, residential dwelling houses have lower rates than buildings that are used for business purposes. The land tax is defined in *ALL/ha* per calendar year and varies based on the category of land.[95] According to this criterion, the agricultural land is divided in 10 categories mainly based on soil, fertility and other criteria.

3.3.2.3 The hotel tax – The hotel tax[96] is another local tax governing in the Albanian Tax System. This tax is set in a fixed value for each night a guest stays in a hotel. The value differs varying on the location and hotel type. The hotel owner remits the tax to the local government within the 5th day of each month for the previous month.

3.3.2.4 Tax for impact on infrastructure[97] – The tax base of the tax for impact on infrastructure from new buildings or construction, is the value of the new investment. The tax rate is defined by the local government at a rate of 1-3% on the value of the investment. This tax fluctuates from 2-4% for Tirana & Durres municipalities. The tax for impact on infrastructure is paid by the investor at the time of building license issue.

[92] Law no.9632, date 30.10.2006, Chapter 3, Article 16.
[93] Law no.9632, date 30.10.2006, Chapter 4, Article 20.
[94] Law no.9632, date 30.10.2006, Chapter 4, Article 22.
[95] Law no.9632, date 30.10.2006, Chapter 4, Article 23 & Article 23/1.
[96] Law no.9632, date 30.10.2006, Chapter 5, Article 26.
[97] Law no.9632, date 30.10.2006, Chapter 5, Article 27.

3.3.2.5 The tax on alienation of immovable properties[98] – The tax on alienation of immovable properties applies to all buildings and real estates, at the time of ownership transfer of rights over them. In accordance with the laws into force, each person who transfers the ownership of the immovable property pays this tax before the registration. The tax base is the building surface which is subject to transfer. The level of this tax varies from 100-1000 *ALL* for each m^2, depending on the municipality. For other properties, the tax base is their selling value and the tax rate is 2%. Exemptions from this tax[99] are: National Housing, Ministry of Finance and other central & local government bodies; persons who are subject to the personal income tax; subjects who donate immovable properties and the direct beneficiaries are: state institutions and public institutions; religious communities or non-profit organizations when the grant is correlated to that part of their non-profit activity.

3.3.2.6 Motor vehicles tax – The motor vehicles tax is a fixed amount tax which must be paid on a motor vehicle, such as a car, truck, motor home and other vehicles depending on their type and capacity. This annual tax is paid by the vehicle owner.

3.3.2.7 Other local taxes and fees[100] – These types of taxes include some local fees and tariffs paid by businesses which occupy public areas, also leading to the payment of advertisement fees.

The local governments like the Council of Municipality or the Council of Commune, have the right to change the tax rate as much as 30%. Any change must be implemented equally for all businesses. Local governments also have the authority to introduce new taxes fees or tariffs, within the scope and related laws provision. The local taxes and fees make up for a portion of State and Municipalities budget, which gets collected and invested to improve community's life. In the last two years big changes are taking place in Albania, especially in the infrastructure context, building new green areas and renewing the main cities infrastructure in Albania. Changes in infrastructure will contribute to an increase of tourism influx in summer and winter too, as infrastructure is an important determinant factor regarding tourism development.

[98] Law no.9632, date 30.10.2006, Chapter 5, Article 28.
[99] Law no.9632, date 30.10.2006, Chapter 5, Article 29.
[100] Law no.9632, date 30.10.2006, Chapter 5, Article 32.

Subsection 3.3.3 – Tax procedures

In the Republic of Albania, tax procedures are regulated under the provisions of the law "*On Tax Procedures in the Republic of Albania*[101]". This law was determinant towards leading the Republic of Albania in a modern and effective tax administration system. Furthermore, this law introduced a new method of collecting taxes, finally abolishing the irregular and arbitrary practices, developing a self-declaration principle and highlighting a transparent relationship between the tax administration and taxpayers. The object of this law consists in regulating the procedures for administering taxes, as well as principles of organization and functioning of the tax administration in the Republic of Albania.[102] This law applies to: taxpayers, tax administration, tax agents, withholding tax agents and persons who pay contributions for social & health insurance, as well as other persons defined by the legislation.[103] As explained above, this law was fundamental not only in the building of a new modern tax administration; also in the beginning of the harmonization process within the *EU Acquis*.

This law brought a novelty related to the term "*resident*", as the previous law didn't contain a definition of this legal important term. If a legal individual meets one of the following criteria, is to be considered as an Albanian resident. A resident taxpayer is the individual/legal person who[104]:

- Has a residence in the Republic of Albania;
- Has an Albanian citizenship and exercises diplomatic functions on behalf of the Republic of Albania outside its territory;
- Stays in the Republic of Albania, continuously or intermittently more than 183 days/year;
- Is registered as an Albanian legal person;
- Has its place of business management in the Republic of Albania;
- Has a permanent establishment in the Republic of Albania;

As I mentioned in the very beginning of this subsection, this law introduced some basic principles by which the tax administration should be guided. Under this law, the tax administration is not

[101] Law no.9920, date 19.05.2008.
[102] Law no.9920, date 19.05.2008, Article 1.
[103] Law no.9920, date 19.05.2008, Article 2.
[104] Law no.9920, date 19.05.2008, Article 8.

entitled only in exercising the right of the collection of taxes, but is bound to carefully apply and enforce the law in the same way for all taxpayers. Some of the most important principles are[105]:

- The uniform and effective application of legislation by the tax administration;
- Promotion of voluntary compliance with the tax legislation through information, education and publication of by-laws;
- Cooperation with domestic and international tax authorities, in the view of globalization of the world economies;
- Developing strategies and taking appropriate measures to reduce the risks arising from the bad-application of tax legislation;
- Self-esteem and self-declaration of the tax liability by the taxpayers.

Moreover, this law regulates also the general procedures for tax declaration, collection, tax audit including: organization and structure of tax administration, taxpayers' rights and obligations, registration and de-registration of taxpayers, taxpayer's documentation and accounting for tax purposes, taxpayer's obligation to provide information and to enable tax controls in business facilities, obligation of the third parties to provide information to the tax authorities, tax declaration and tax assessment procedures, the right to use alternative methods by the tax authorities for the tax assessment, enforced collection of unpaid taxes, responsibility of owners, shareholders and administrators for tax debts, tax investigation, administrative appeals, sanctions and tax audit.

Subsection 3.3.4 – Tax Authorities

Tax authorities are the main players of any taxation system. They are the heart of citizens relationship with the state, which contribute towards reaching a well-functioning tax system, by enforcing the respective legislation as their main objective. According to the law "*On Tax Procedures in the Republic of Albania*", the tax administration in the Republic of Albania is composed of central tax administration and local tax administration. The central tax administration includes: General Tax Directorate (*GTD*), Regional Directorates and its units. The local tax administration includes: Local Tax Offices under the authority of local government. The central tax administration, is a central institution under the control of the Ministry of Finance.[106] GTD is

[105] Law no.9920, date 19.05.2008, Chapter 2, Article 12.
[106] Law no.9920, date 19.05.2008, Chapter 2, Article 13.

the only central tax authority in the Republic of Albania that implements and administers national taxes, public fees and collections of contributions.[107] All the Regional Directorates are under the authority of the Director of the GTD. In Albania, there are 15 Regional Directorates. Banks are administered by the Large Taxpayers Unit, located in Tirana. Local taxes are administered by the Local Tax Offices of Municipalities and Communes. Custom duties and VAT on imported goods are administered by General Directorate of Customs (*GDC*). Regional Customs Directorates are under control of the GDC. Tax policies and drafting of laws are proposed to the Council of Ministers and Parliament by the Ministry of Finance after being coordinated with related institutions and groups of interests.

CHAPTER 4 – Albania status in a line with the harmonization process with the *Acquis Communautaire*. EU tax law and International Treaties avoiding double-taxation

Section 4.1 – What is expected in this Chapter?

Albania was awarded candidate status on June 2014, moving now within touching distance of starting EU membership. The Stabilization and Association Agreement (*SAA*) between Albania and EU was successfully agreed and signed on 12 June 2006. Albania has implemented smoothly its obligations being extensively engaged with EU institution throughout years. SAA is leading Albania in the harmonization process, stipulating obligations in alignment with EU acquis. Despite this, many reforms are needed to be undertaken in the field of tax law. The European integration dreamt up by individuals who had a vital role in Albania's accession road, would be achieved only if the Albanian legislation implements and try to harmonize its legislation with the so-called *Acquis Communautaire*. Thus, this process is essential in the context of European Integration, demanding hard work to fulfil all the requirements needed to finalize it. Nowadays, Albania is making serious efforts towards a better alignment with the EU standards. The domestic tax legislation alignment with the EU acquis constitutes one of the big challenges my country is facing in the road towards EU membership.

[107] Law nr.9920, date 19.05.2008, Chapter II, Article 14.

Firstly, this chapter aims to give an overview of the harmonization progress of Albania in the field of taxation. Secondly, it is fundamental to understand the European Union taxation system, highlighting the main and the most important directives enacted by the European Commission in the field of direct taxation. Thirdly, double-taxation is one of the biggest issues Europe is facing nowadays, an essential matter of tool avoidance relying on the International Treaties between Albania and some EU Countries.

Section 4.2 – Albania progress in harmonizing tax legislation with the Acquis Communautaire

In the very beginning of Albania's tax system development, serious efforts were made to create a moderated system based on principles and exact rules. Signed on 16 June 2006, the EU-Albania SAA aims to support Albania's transition, as well as facilitating its economic shift into the European Union's single market. One of the aims of this association is to support the efforts of Albania to develop its economic and international cooperation, through the approximation of its legislation to that of the Community.[108] This cooperation must be also developed among other fields, in the field of taxation. The main tools helping in the establishment of this cooperation is by including measures to reform the fiscal system and tax administration. Accordingly, the main goal of these reforms is to ensure effectiveness of tax collection and fight against fiscal fraud.[109] This was a break-through to start the harmonization process, leading to the adoption and alignment of some of the domestic tax laws with the respective ones in the Acquis.

The Treaty of Functioning of European Union (TFEU) is the primary law governing in the EU. Regarding to indirect taxation, Article 113 of TFEU provides for the harmonization of legislation concerning turnover taxes, VAT, excise duties and other forms of indirect taxation to the extent that such harmonization is necessary to ensure the establishment and the functioning of the internal market and to avoid distortion of competition.[110] In Albania, exist these types of indirect taxes that enjoy a partial harmonization with the respective ones in the Acquis Communautaire. The Albanian law "*on VAT*" it is partially harmonized with the Directive 2006/112/EC "*on the common system of VAT*". Also, the law "*on Excise Duties*" is partially harmonized with the Directive

[108] Stabilization and Association Agreement between the European Communities and their Member States, of the one part, and the Republic of Albania, on the other part [2009] OJ L107/166, art 1 para 2 (*SAA*).
[109] SAA art 98 para 1.
[110] Consolidated version of the Treaty on the Functioning of the European Union [2012] OJ C326/47, art 113.

2008/118/EC "*concerning general arrangements for excise duties*". In relation to these Directives, Albania has made a good progress in the harmonization process. These reforms are highlighted in the yearly European Commission's progress reports on Albania. Value-added tax and excise duties are two of the most crucial indirect taxes that affect free movement of goods and the freedom to provide services. This is the main reason why harmonization within the European Union is essential. Albania also is a part of the EU's Fiscalis 2020 programme. European Commission enacted a Regulation[111] with the goal of establishing a programme (Fiscalis 2020) helping the cooperation between states and tax authorities, as they are the key players in the functioning of taxation systems. The main aim of this programme is to improve the functioning of the tax system in the internal market.[112]

According to EC Progress Report[113]: 'Albania is ***moderately prepared*** in the area of tax system functioning. Significant progress was reached on legislative approximation with the *acquis* on value added tax and excise. Revenue performance in 2015 exceeded targets, largely resulting from fighting the informal economy. On ***indirect taxation***, amendments to the VAT law were adopted on October 2015 regarding exemptions for machinery and equipment correlated to investments. The law still contains VAT exemptions, which are not in line with the *acquis*. The refund of VAT occurs broadly nowadays within the legal deadlines and low-risk VAT refunds are processed automatically. Excise duties for some domestic beer production were reduced and reimbursement for imported biofuels excise got introduced. Further steps are needed to align excise rates with the *acquis*'.[114]

The Albanian law "*on VAT*" is partially aligned with the Directive of the EC, but according to the EC Report, this law still contains some VAT exemptions which are not in line with the Acquis. A few exempt supplies provided by the Albanian law which are not in line with the *Acquis* are: supply of pharmaceutical products; supply of ID cards; supply of printing house services for newspapers;

[111] Council Regulation (EC) 1286/2013 of 11 December 2013 establishing an action programme to improve the operation of taxation systems in the European Union for the period 2014-2020 (Fiscalis 2020) and repealing Decision No 1482/2007/EC [2013] OJ L 347/25.
[112] '*Essentials on Fiscalis 2020'* <www.ec.europa.eu/taxation_customs/fiscalis-programme/essentials-fiscalis-2020_en> accessed 5 June 2017.
[113] Commission, 'Commission staff working document, Albania report 2016' COM (2016) 715 final.
[114] Commission, 'Commission staff working document, Albania report 2016' COM (2016) 715 final, ch 16, 50.

supply of advertisement services by written and electronic media and supply of goods and services classified as related to the research phase of hydrocarbon operations. Furthermore, there are also a few exemptions on import of goods which are not in line with the *Acquis*: import of machinery and equipment for investments of contractual value more than 50 million *ALL*; import for inward processing and agribusiness activities and import of goods for the production activity of small enterprises. Certain exemptions are obligatory for the Member States, whereas others are optional. However, most of the exemptions on Albanian VAT law are harmonized with the related ones in the EU VAT Directive.[115]

Regarding to the excise duties in EU, European Commission apart from the Directive 2008/118/EC, has enacted two directives regulating alcohol excise duties: Directive "*on the harmonization of the structures of excise duties on alcohol and alcoholic beverages*[116]", ensuring a harmonized structural basis to the alcohol duties, and Directive *"on the approximation of the rates of the excise duty on alcohol and alcoholic beverages*[117]", which aims at approximation of minimum rates. Albania excise rates on alcohol and alcohol beverages are mostly in line with those set out by the directives. According to the EC Progress Report, Albania has made further steps in the harmonization process by reducing excise duties to some domestic beer production. In Albania, minimum excise rates on alcohol and alcohol beverages are in line with those in the *Acquis*.

Small problems are arising with the excise rates on tobaccos. Albanian excise duties on tobacco are not in line with those set out in the Council Directive "*on the structure and rates of excise duty applied to manufactured tobacco*[118]". Excise rate for Cigars & Cigarillos in Albania is approximately 18.49 Euro/kg, whereas in EU is 12 Euro/kg.[119] This is the reason why the EC Progress Report mentions that further steps are needed to align excise rates with the *Acquis*.

[115] Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [2006] OJ L347/1, VAT exemptions, art 131 to 167.
[116] Council Directive 92/83/EEC of 19 October 1992 on the harmonization of the structures of excise duties on alcohol and alcoholic beverages [1992] OJ L316/21.
[117] Council Directive 92/84/EEC of 19 October 1992 on the approximation of the rates of the excise duty on alcohol and alcoholic beverages [1992] OJ L316/29.
[118] Council Directive 2011/64/EU of 21 June 2011 on the structure and rates of excise duty applied to manufactured tobacco [2011] OJ L176/24.
[119] Council Directive 2011/64/EU, art 12, para 2(a).

Considering *direct taxes*, TFEU takes a different approach towards them due to the following reasons. EC Treaty (Treaty of Rome, 1957) left these type of taxes outside of its scope because they were not seen as key players for the establishment and development of the internal market. On the other hand, Member States were not willing to give up their competences and treat direct taxes in the EU level, reasoning that they were convenient instruments driving forward their economy. As a result, direct taxes remain also nowadays within the competence of Member States.[120] As there aren't any specific provisions in the field of direct taxation, Art. 115 of TFEU is the only tool left providing for a legal basis to start the harmonization process. Considering that TFEU is a matter of primary law, it grants the Council the right to enact directives aligning laws and regulations influencing the functioning of the internal market. The adoption of these directives require unanimity in the Council and in this context, the will of the Member States plays a vital role. Direct taxes are the ones who may affect the domestic economic policies of the Member States thus, it requires that all Member States give up their competences, which in this case is more than difficult. The fact that every provision provided by these laws should satisfy all Member States, is obstructing the harmonization of direct taxes on the European level.[121]

According to the EC Progress Report on Albania: '***on direct taxation***, the 2016 budget and fiscal package reduced the tax burden on small businesses'.[122] The fiscal policy of the government in force made radical changes on direct taxation, adopting a progressive tax system on incomes generated from salaries. Taxation systems that apply a taxation in progressive rates also offer higher overall levels of revenue and for this reason there is an elevation in nation's benefits. Corporate taxes are in line with most of the Member States of the EU. In the current tax policy of the EU, there is no harmonization of the systems of the Member States on direct taxation. They are free to choose tax systems, considered to be the most appropriate. The harmonization policy of the EU was mainly based on indirect taxation, because those are the ones who can mainly affect free movement of goods and hinder the internal market.

[120] Lukasz Adamczyk and Alicja Majdanska, 'The sources of EU Law Relevant for Direct Taxation' in Michael Lang, Pasquale Pistone, Josef Schuch and Claus Staringer (eds), *Introduction to European Tax Law on Direct Taxation* (Linde 2016), 14 para 43.
[121] Adamczyk and Majdanska (n 120) 14 para 44.
[122] See n 114.

It is important to mention that, as Albania is a country aspiring to join the EU, the Albanian tax system principles are harmonized with the principles of the so-called "*Code of Conduct for Business Taxation*[123]". This Code of Conduct doesn't have a binding power, but it has a strong political influence. During that time, EU was facing a harmful tax competition. Consequently, after a wide-range debate, government representatives of Member States meeting within the Council conducted this Code with the simple purpose of preventing this harmful tax competition by rolling-back the existing tax measures. This Code provides for measures in any legal forms but also a specified test, assessing whether a tax measure is harmful or not. All tax measures providing for low efficiency level in preventing this particular issue are therefore covered by this Code of Conduct.[124]

The European Commission highlighted also the decisive steps taken by the government regarding administrative cooperation and mutual assistance. GTD and Custom Authorities established a joint risk unit. According to the Progress Report: 'the GTD receives support from the International Monetary Fund to implement the compliance risk management strategy, and from the United States for law revisions and debt/VAT collection'[125]. To sum up, the European family is towards the road of becoming a reality for the Albanian citizens, as Albania is smoothly fulfilling its obligations and implementing the directives of the EU; still many reforms are needed to be taken to accelerate as much as possible the integration process.

Section 4.3 – EU tax law considering the main directives in the field of direct taxation

As it is commonly known, EU law is divided in primary law and secondary law. Since the time of creation of the Treaty of Rome, the harmonization of the group of direct taxes was not seen as important, as long as they do not directly affect the free trade between Member States. Years later with the internal market in a continuous development, the need for harmonization of direct taxes

[123] Resolution of the Council and the representatives of the governments of the Member States, meeting within the Council of 1 December 1997 on the code of conduct for business taxation (1998) OJ C2/2, pp. 2-5.
[124] Marie-Ann Kronthaler and Yinon Tzubery, 'The State Aid Provisions of the TFEU in Tax Matters' in Lang, Pistone, Schuch and Staringer (eds), *Introduction to European Tax Law on Direct Taxation* (Linde 2016), 98-99 para 339-340.
[125] See n 112-113.

grew up reaching a satisfying level. Still, in the field of direct taxation, this harmonization is incomplete relying only in some directives with a specific profile on taxation of companies.[126]

In European Union, the legislation is divided into primary and secondary law. Regulations are binding legal instruments that are applicable among all Member States. On the other hand, directives are not binding instruments but they provide for a set of rules that the Member States must comply with. The EU tax legislation was subject to a continuous development, leading to the adoption of some Directives providing specified rules for the removal of tax obstacles within the internal market.[127] This section aims to give an overview of the directives that remove tax obstacles within the internal market, namely: the ***Parent-Subsidiary Directive***[128], the ***Merger Directive***[129] and the ***Interest and Royalty Directive***[130].

Subsection 4.3.1 – The Parent-Subsidiary Directive

On 23 July 1990, the European Council adopted the so-called Parent-Subsidiary Directive. It is clearly understandable from the name, that this Directive deals with a group of companies established in the EU. This Directive aims to achieve two main goals. Firstly, it establishes a set of rules providing under specified conditions for the elimination of withholding taxes on dividends between associated companies in different Member States.[131] Secondly, this Directive provides measures for the eliminating double taxation between these associated group of companies.

As every other directive, this one contains definitions which are essential in its functioning. *Article 2* of the Directive provides for a definition of the terms "***company of a Member State***". The terms

[126] Adamczyk and Majdanska, 'The sources of EU Law Relevant for Direct Taxation' in Lang et al (eds), *Introduction to European Tax Law on direct taxation* (Linde 2006), 18 para 58.
[127] ibid 19 para 59.
[128] Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States [2011] OJ L345/8 (*The Parent-Subsidiary Directive*).
[129] Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchange of shares concerning companies of different Member States and to the transfer of registered office of an SE or SCE between Member States [2009] OJ L310/84 (*The Merger Directive*).
[130] Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States [2003] OJ L157/49 (*The Interest and Royalty Directive*).
[131] Adamczyk and Majdanska, 'The sources of EU Law Relevant for Direct Taxation' in Lang et al (eds), *Introduction to European Tax Law on direct taxation* (Linde 2006), 19 para 60.

"***company of a Member State***" shall mean any company that meets these requisites specified in the Article 2 of the Directive as follows[132]:

- it takes one of the forms listed in the *Annex* of the Directive;
- resides in a EU Member State for tax purposes and under any Double Tax Treaty agreed with a third State is not considered as a resident outside the EU;
- it is subject to one of the taxes listed in *Annex* of the Directive without any possibility of an option or of being exempt.

The application of this Directive is fully connected with the definition of what constitutes a parent and subsidiary company. The relationship between the parent company and its subsidiary plays a fundamental role in the application of the provisions of this Directive. As it is defined in *Article 3(1)(a)* a "***parent company***" is a company that has a minimum shareholding of 10% in the capital of the company of another Member State and the "***subsidiary company***" is defined by the Article *3(1)(b)* as the latter company whose shares in capital are being held by the parent company. The Directive oblige both companies to fulfill the requirements of *Article 2* in order to classify them as a "***company of a Member State***". Furthermore, *Article 3(1)(a)(ii)* provides for another way of participation on the subsidiary, simply by holding these shares in capital through a permanent establishment situated in the State of the subsidiary.[133] However, the Directive provides in the *Article 3(2)* two more options in order to enjoy the status of Parent Company as provided in the *Article 3(1)(a)*. The first option is that Member States based on a bilateral agreement, can replace the holding in capital criterion with the holding of the voting rights on its subsidiary. So, it introduces another option of control, not only by holding share capital but also by holding the voting rights. The other option provides for an uninterrupted shareholding period of at least two years.[134]

Another definition which is essential in the functioning of this Directive, is the term "*permanent establishment*". This term has the same meaning as the one provided in the OECD Model Convention. The term "*permanent establishment*" is the same as the one introduced into the OECD

[132] Mario Tenore, 'The Parent-Subsidiary Directive' in Lang et al (eds), *Introduction to European Tax Law on Direct Taxation* (Linde 2016) 135 para 463.
[133] Tenore (n 132) 136 para 467.
[134] ibid 137 para 470.

Model Convention. 'For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partially carried on'.[135]

The most crucial part is the application of this Directive. There are three cases to take in consideration correlated to the application of this Directive. *Firstly*, the application of the Directive in the State of the parent company; *secondly*, the application of the Directive in the State of the subsidiary company and *thirdly*, application of the Directive to permanent establishment.

In the case of application of the Directive in the State of the parent company, *Article 4* obliges the State of the parent company to eliminate double taxation of the profits received from the State of the subsidiary, excepting profits deriving as an outcome of the liquidation of the subsidiary. As provided in the Directive, such elimination of double taxation is done in two ways: by exempting profits received by the subsidiary or by taxing such profits while crediting the corporate tax paid by the latter.[136] This is an essential point in the functioning of this Directive. Hereto, *Article (4)(1)(a)* establishes a rule in respect to profits that are non-deductible for the subsidiary. In this case, the State where the parent company is established must exempt from tax these profits paid by the subsidiary. In the opposite case, if profits are deductible, the State of residence is obliged to tax the dividends flowing from the subsidiary to the parent company.[137] To sum up, Member States have the choice between the adoption of credit or exemption method when they are in line with primary law on inbound of dividends.

In the case of application of the Directive in the State of the subsidiary, *Article 5* obliges the State of the subsidiary to exempt the distribution of profits to its parent from withholding tax. As mentioned above, the exemption of the distribution of profits from withholding tax in the State of the Subsidiary is well-connected with the aim of this Directive. Exempting such profits, eliminates the double taxation in the State where the Parent company is established.[138]

[135] Convention between (State A) and (State B) with respect to taxes on income and capital (2014) ('OECD Model Convention') art 5.
[136] Tenore (n 132) 141 para 486.
[137] ibid 142 para 487.
[138] ibid 145 para 501.

Lastly, the case of the application of the Directive to a permanent establishment leads us to a triangular situation with three companies in three different Member States. *Article 1(c)* provides the obligation of the State of the permanent establishment that receives such profits from the parent companies, to eliminate double taxation by choosing one of methods (credit or exemption) relying on the rules provided in the *Article 4* of the Directive.[139] In my opinion, it is still unclear how is the Directive dealing with the situation where the permanent establishment of the parent company is situated also in the State of the subsidiary making internal distribution of profits, whereas the parent is situated in a different Member State. The question here is whether the Directive applies not only to cross-distribution of profits, but also to internal distributions in this triangular case.

Subsection 4.3.2 – The Merger Directive

The Merger Directive is another important piece of legislation which was adopted by the Council on 23 July 1990 and later amended in 2009. The Council had its main aim establishing an open internal market without fiscal obstacles, leading to the adoption of this Directive applicable to cross-border reorganizations mostly known as mergers. As every Directive regulating the field of direct taxation, the Merger Directive was introduced as a tool aiming the removal of fiscal obstacles involving companies established in two or more Member States. The main goal of the Merger Directive is providing deferral of capital gains if tax values of assets and liabilities of the transferring company is taken over by the receiving company.[140]

In the Merger Directive, the term "company from a Member State" is fundamental in its functioning. This essential term is somehow the same as provided in the Parent-Subsidiary Directive. *Article 3* of the Directive, provides for three requirements to classify as a "company from a Member State": First, such company must take one of the forms in the annex; Second, the company must be resident for tax purposes in a Member State of the EU and third, this company must be subject to one of the taxes provided in the annex of the Directive.[141] All these requirements must be meet in the same time to enjoy the status of "company from a Member State". As this

[139] Tenore (n 132) 148 para 509.
[140] European Commission 'Merger Directive' <www.ec.europa.eu/taxation_customs/business/company-tax/merger-directive_en#objectives> assessed 15 June 2017.
[141] Mathias Hofstätter and Daniela Hohenwarter-Mayr, 'The Merger Directive' in Lang et al (eds), *Introduction to European Tax Law on Direct Taxation* (Linde 2016) 159 para 527.

Directive deals with companies, it is vital to have a definition of what constitutes a "company from a Member State". Nonetheless, the Directive does not oblige companies to comply in the same time with these requirements only in one Member State.[142]

The Merger Directive contains definitions which are essential for its specific functioning. The Directive provides in *Article 2(a)(i)* the definition of what constitutes a ***merger***. Merger is a process where one or more companies merge together, transferring all the assets and liabilities without going into liquidation. In respect of that, the Directive in *Article 2(a)(ii)* and *Article 2(a)(iii)* introduces two merger types, respectively when two companies merge and form a new one, and when the company whose share capital is being held from another company merges with the latter.[143] Furthermore, the Directive provides definitions for other types of cross-border reorganizations as ***divisions*** and ***partial divisions***. According to the *Article 2(b)*, a *division* is an operation where a company transfers all the assets and liabilities to two or more existing new companies without going into liquidation whereas *partial divisions* are defined by the *Article 2(c)* as an operation where a company transfer one or more branches of activity (not all assets and liabilities[144]) to one or more existing new companies without going into liquidation.[145] This Directive contains also definitions of the transfer of assets, exchange of shares and transfer of the registered office of an SE and SCE, respectively in *Articles 2(d)(e)*.

Like every Directive, the implementation of the Merger Directive brings tax consequences on the company level. As mentioned in the beginning of this subsection, the main purpose of the Directive is no taxation of capital gains to the difference between the real value and the value of the time of reorganization as provided in the *Article 4* of the Directive. *Article 4(4)* provides that this deferral is done by a so-called roll-over mechanism, meaning that the receiving company takes over all the assets and liabilities of the companies transferring them.[146] Concerning tax consequences the Merger Directive distinguishes between taxation at company's levels, and taxation at the level of affected shareholders.

[142] Hofstätter and Hohenwarter-Mayr (n 141) 160 para 531.
[143] ibid 161 para 535.
[144] The difference between divisions and partial divisions as provided in the Directive.
[145] Hofstätter and Hohenwarter-Mayr (n 141) 161 para 539.
[146] ibid 163 para 547.

'Tax consequences at the level of companies involved are:

1. Deferral of capital gains tax if tax values of assets and liabilities of the transferring of company is taken over by the receiving company (roll-over of tax values) & assets and liabilities transferred remain effectively connected with a PE of the receiving company in the MS of the transferring company *(Articles 4,9 and 12)*;
2. Carry-over of tax deductible provisions and tax-free reserves *(Articles 5,9 and 13/1)*;
3. Takeover of losses to PE of receiving company situated in the MS of the transferring company *(Articles 6 and 13/2)*;
4. No taxation of gains resulting from the cancellation of shares in up-stream merger *(Art. 7)*
5. Transfer of PE in a triangular case: tax neutrality in the PE state; MS of the transferring company may recapture foreign PE losses; and under tax treaty credit method, the MS of transferring company may tax hidden reserves but should give notional credit'[147]

'Tax consequences at the level of shareholders involved are:

1. Deferral of capital gains tax upon exchange of shares resulting from a merger, division, exchange of shares or partial division if the tax values are carried over by the shareholders *(Article 8/1 and 8/2)*
2. Roll-over of acquisition costs;
3. Corresponding deferral rules for transfer of registered office of SE or SCE'[148]

Subsection 4.3.3 – The Interest and Royalty Directive

The third and one of the most important EU Directives in the field of direct taxation is the Interest and Royalty Directive aiming the abolishment of taxation regarding cross-border interest and royalty payments. This Directive was enacted by the Commission in 2013 and started to be enforced later in 2014. Moreover, this Directive applies somehow the principle of non-discrimination; interest and royalty payments made between companies in different Member States must enjoy the same tax conditions as those made between companies of the same State.[149] The main aim of this Directive is exempting withholding taxes on interest and royalty payments made

[147] Hofstätter and Hohenwarter-Mayr (n 141) 180, see the table giving an overview of the Functioning of the Directive.
[148] ibid 180, see the table giving an overview of the Functioning of the Directive; see taxation of shareholders involved.
[149] Dimitar Hristov, 'The Interest and Royalty Directive' in Lang et al (eds), *Introduction to European Tax Law on Direct Taxation* (Linde 2016) 184 para 595.

between associated companies. *Article 1* of the Directive established precise principles and rules which are essential in its functioning. Thus, according to the *Article 1(1)* the ***source State*** exempts from source state tax, interest and royalty payments made by a company or a permanent establishment of that company situated in another Member State. This source state tax is mostly referred as a domestic withholding tax. Moreover, *Article 1(3)* and *Article 1(4)* of the Directive introduce the terms ***payer*** and ***beneficial owner***. According to these Articles, a *payer* of interest and royalties shall be referred as a PE only if these payments are a tax-deductible expense in the State where is situated, whereas a *beneficial owner* is treated as a company or permanent establishment that receives these payments only for its benefit and not as an intermediary or agent. Furthermore, *Article 1(7)* introduces a requirement regarding the applicability of this Directive. This requirement relies on a link that the company/permanent establishment treated as a *payer* and the company/permanent establishment treated as the *beneficial owner* must have. They must enjoy the status of ***associated companies***.[150] If they are not associated companies *Article 1* of the Directive is not anymore applicable.

Taking into consideration the application requirements of the Interest and Royalty Directive, there are some requirements to be met in order that this directive enjoy full applicability. These requirements for the application of this directive are fundamental regarding the substantive and personal scope of application. Regarding the personal scope of application, a "***company of a MS***" is required to make sure that the Directive is applicable. [151] As in every other Directive, the term "**company of a MS**" plays a vital role in this context. This term is introduced by the *Article 3(a)* and according to this article, the companies must fulfill three requirements to fall into the scope of this term. These requirements are introduced by the points *(i)(ii)* and *(iii)*. First *(i)*, the company must take one of the forms listed in the annex[152]. Second *(ii)*, the company must be resident for tax purposes in MS and third *(iii)*, it is subject to a corporate tax without being exempt.

Considering permanent establishments, the Directive makes its application conditional in the following situation. Hence, according to the *Article 1(8)*, the permanent establishment of a

[150] Hristov (n 149) 184 para 596.
[151] ibid 187 para 603.
[152] The list of legal form of companies here is similar to the list provided in the Parent-Subsidiary Directive.

company of a MS is situated in a third country and carries out wholly or partially the business of that company of a MS, does not enjoy the exemption from the source state tax provided in *Article 1(1)*. Therefore, *Article 1(1)* is not applicable anymore.[153]

As mentioned above, the Directive provides for a source tax exemption only in respect of associated companies of Member States. In every other case the Directive is not applicable and therefore no tax exemption is provided. In this context, the Directive provides for two different forms of association particularly in the *Article 3(b)*. According to this Article, ***Company A*** is considered an associated company of ***Company B*** in the cases where: First, ***Company A*** holds at least 25% in the capital of ***Company B*** (*direct vertical association*) and second, when another company (***Company C***) holds in the same time at least 25% of the capital of the ***Company A*** and 25% of the capital of the ***Company B*** (*direct horizontal association*).[154] Only on these two grounds the Directive is applicable, therefore companies of the third states are excluded from the scope of the Directive. MS can optionally substitute the minimum 25% holding in capital requirement with voting rights or implement a minimum holding period (e.g. for two years).[155]

Regarding the substantive scope of application, the source tax exemption applies to ***interest*** and ***royalty*** payments. This Directive contains a list of specific payments in which the provisions are not applicable. The exclusions of specific payments are referred in the *Articles 4(1)(a)(b)(c)(d)* of the Interest and Royalty Directive.

To sum up, the Interest and Royalty Directive provides full exemption from domestic source tax on interest and royalty payments made between an association of companies where the payer (source) is a company of a MS or a PE of a company of a MS and the payee (beneficial owner) is a company of a MS or a PE of a company of that MS.[156] Association of companies have to fulfill two requirements: the beneficial owner has to have a minimum 25% share capital on the source company and to hold these shares for 2 years as a minimum period.[157]

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[153] Hristov (n 149) 189 para 607.
[154] ibid 190, paras 609 610.
[155] Dimitar Hristov 'Lecture of European and International Tax Law' LL.M Program in International and European Business Law, University of Vienna (November 2016) see slide 58.
[156] Hristov (n 149) 200, see the table giving an overview of the functioning of the Interest and Royalty Directive.
[157] ibid 200.

Section 4.4 – The concept of double taxation and the International Treaties avoiding it

The existence of double taxation is one of the most common problems in European tax systems. Double taxation is also a matter of international law, thus one of the main solutions for the avoidance of this problem are the International Conventions between States. 'A Double Taxation Convention, is an agreement which is concluded between two States to prevent a person who is fully liable to tax in one of the States (or sometimes in both states) from being taxed on the same income or capital in both States.'[158]

Double taxation is a big issue affecting not only companies but also residents. European Union is fighting this problem because double taxation is a decisive factor establishing obstacles to the free movement of workers. Many of EU countries tax the same worldwide income of their residents not only in the country from where this income derives but also in their country of residence.[159] Apart from this, States usually tax their residents' income on the corporate and personal level in the same time, establishing a situation where residents pay more taxes than they have to (*limited tax liability*).[160] For these reasons, cooperation between MS is essential in fighting this issue.

There are two different kinds of double taxation, ***juridical*** and ***economic*** double taxation. Juridical double taxation is referred to the situation where a taxable person is taxed twice in both MS on the same income, whereas economic double taxation is referred to the situation where two different taxpayers are taxed in the same time on the same income.[161]

Albania is moderately preparing the network of International Conventions with many international institutions, governments of other states, international financial institutions for the avoidance of double taxation. The road towards EU integration requires cooperation with international institutions like IMF, World Bank, European Bank etc. Bilateral assistance and cooperation agreements with many European countries, contain provisions regarding tax treatment and tax consequences of investments and other transactions related with these agreements. As it is

[158] Mogens Rasmussen, 'International Double Taxation' (Kluwer Law International 2011) 1 §1.01.
[159] Is the situation when for example, an Austrian citizen that lives in Vienna works in Bratislava (Slovakia) and his income is taxed both in Slovakia and in Austria. The same situation is referred also in the corporate level.
[160] Rasmussen (n 158) 1 §1.03.
[161] ibid 1-2 §1.02 and §1.04

commonly known, double taxation is a matter of international law and prevails over domestic law thus, all the International Conventions for the avoidance of double taxation signed by Albania prevail over Albanian domestic tax law. Hitherto, Albania has concluded 41 tax treaties for the avoidance of double taxation. Lastly, the implementation of tax treaties in Albania is regulated under the provisions of the Instruction of the Minister of Finance "*on agreements for avoidance of double taxation and prevention of fiscal evasion*[162]".

As mentioned above, the conventions between MS are the most important tools for avoiding double taxation. Mostly, these conventions rely on the model provided by the OECD Model Convention[163]. It is important to point out that this Convention is not binding among MS, because it is just a Model Convention and therefore provides only an example that should be considered by the MS while drafting and signing double tax Conventions between them. Apart from the allocation rules, this Convention provides two methods for avoiding double taxation: ***Exemption***[164] and ***Credit***[165] method. For the purposes of explaining both methods: *(S)* is the State of the source and *(R)* is the State of residence.

The exemption method provides specific rules for its application. This method relies on the principle that the State of residence does not tax the income which is taxed in the State from where this income derives. This method is applicable in two ways as follows[166]:

1. ***Full exemption*** – meaning that the income which may be taxed in the ***State (S)***, from where this income derives is exempted by ***State (R)*** of residence. Hence, this income is not subject to tax in the State of residence.[167]
2. ***Exemption with progression*** – meaning that ***State (R)*** of residence exempts from tax the income which may be taxed in ***State (S)*** from where this income derives, but considers this income when levying the tax on the rest of the income. Nowadays, this method is rarely applicable compared to 'full exemption'.

[162] Instruction of Minister of Finance no.6, date 10.02.2004.
[163] See n 135.
[164] OECD Model Convention, ch 5 art 23A.
[165] ibid art 23B.
[166] 'Commentaries on the articles of the Model Tax Convention', (OECD 2010) 309 paras 13-14 <www.oecd.org/berlin/publikationen/43324465.pdf> assessed 16 June 2017.
[167] See n 159, in this case Austria exempts from tax the income derived from the work of the Austrian citizen in Bratislava (Slovakia).

Apart from the exemption method, the OECD Model Convention provides for another important method which is called the ***credit method***. The credit method is different from exemption method because it takes a deeper look on the tax, providing specific rules for its application. This method relies on the principle that ***State (R)*** of residence after calculating the tax on the income levied on the ***State (S)***, from where this income derives, credits the tax paid in the ***State (S)***. This method is also applicable in two ways as follows[168]:

1. ***Full credit*** – meaning that ***State (R)*** of residence credits all the tax amount which may be paid in the ***State (S)***, from where this income derives.
2. ***Ordinary credit*** – meaning that if the tax paid in ***State (S)***, from where this income derives is higher than the tax levied in ***State (R)*** of residence, then ***State (R)*** of residence credits not more than the tax amount levied on ***State (S)***.

To sum up, the difference between the methods lies in the exemption method relying at the income, while the credit method relies at tax. Regarding the credit method, the State of residence has the taxing right, crediting the tax paid in the source State. It is important to mention that the amount to be credited is up to maximum amount of tax payable in the residence state. For example, if the tax in the State of residence is 10% and in the other State is 20%, in this case the maximum creditable amount of tax is 10%.

CHAPTER 5 – The investment climate in Albania

Section 5.1 – What is expected in this Chapter?

This chapter aims to develop the issue of the investment climate in Albania relying on the reports of some EU-institutions. Albania's transition from a difficult 50-year communist/socialist rule and centralized economy to an open market economy brought severe consequences. These notorious years prevented the development of the country's economy in many fields. Due to these reasons, many reforms were undertaken aiming the establishment of a market economy like in every other country in EU. In the recent 20 years, Albania faced a huge development especially in the field of economy. Many international institutions are helping Albania to establish a strong market

[168] 'Commentaries on the articles of the Model Tax Convention', (OECD 2010) 309 paras 15-16 <www.oecd.org/berlin/publikationen/43324465.pdf> assessed 16 June 2017.

economy, opening the road towards the European Union. After the entry of Albania in SAA with the EU and its Member States, the process of European integration is being accelerated by the fulfillment of the obligations deriving from this important agreement.

After highlighting the Albanian tax system in the 3rd Chapter, this chapter provides to the readers the way this tax system is affecting the investment climate taking into special consideration *Foreign Direct Investments (FDI)*. FDIs are essential in upgrading the economy. Thus, it is important to implement a liberal foreign investment regime with the goal of increasing as much as possible the number of these investments Albania. The government's objectives are clear, consisting in starting a policy goal to attract foreign investments, the main drivers of the economic growth. In conclusion, this chapter stops at giving the *pros* and *cons* of investing in Albania, determining all the factors which influence the investment climate. This is based on some researches of the Albanian Investment Development Agency (*AIDA*).

Section 5.2 – Investment climate in Albania

The communist regime left Albania in a backward situation, with a brittle economy and a lot of political insecurity. International aids in collaboration with the strategic partners helped Albania to overcome this transitioning period, aiming to establish a market economy. The road toward prosperity was full of obstacles because Albania was one of the poorest countries in Europe. Moreover, many reforms were undertaken to overcome these obstacles, leading to a significant progress and attracting many foreign investments. The exports started to grow and this gave a breath to the economy. According to the World Bank group in Albania, the importance of the reforms aiming the country's recovery shall be implemented as soon as possible, taking into special consideration the creation of more job places and the improvement of the market competition.[169]

ALBANIA	**2016**
Population, million	2.9
GDP, current US$ billion	11.4
GDP per capital, current US$	4146,8

Table 10[170]

[169] World Bank, 'An overview of the World Bank's work in Albania' (April 2007) <http://pubdocs.worldbank.org/en/801391492682079441/Albania-Snapshot-April-2017.pdf > assessed 13 May 2017.
[170] Table 10 – Current GDP rates in Albania (World Bank).

After the reforms, the Albanian economy started to see the light at the end of the tunnel. In 2014, the economy faced a growth of 2.1%, as the exports started to flower. This lead to the growth of the Gross Domestic Public (*GDP*) achieving a rate of 2.8%. The sectors who played a fundamental role in the economic growth were mainly based in the construction industries and energy power, respectively with a growth rate of 1.96% and 0.72%. As the country was facing a renaissance, the GDP continued its growing. The most important pillars in the Albanian GDP are the services and commerce sectors of services with a rate of 45.4%.[171] The increase and development of the tourism sector brought the country's economy in a higher level, aiming at reaching the EU levels. The economic policy of the government started to soothe with big steps the consequences of the crisis and directed the country towards a further development.

As summarized above, tax and many other legislative reforms brought many legal and economic incentives. Many new laws in public and private spheres were enacted and further amended. The most important step was made by ratifying the so-called "*Investment Charter*" aiming to reform the legal environment attracting Foreign Direct Investments (*FDIs*) in Balkans.[172] Many reforms aimed not only the economic sector but also facilitating the bureaucracies in establishing and registering companies. The tax environment is composed by one of the lowest VAT rates in the region providing for exemptions for machineries and imports with an investment value of more than 400.000 Euros.[173] These facilities provided by the Albanian tax legislation attracted many FDIs, leading to a further growth of the economy.

The further development of the economy brought the continuous need for implementing specific laws in specific sectors. In 2015, after long regulatory disputes, the Albanian Parliament enacted the law "*on Strategic Investments*[174]". The purpose of this law is to establish precise rules and principles aiming to build a conductive environment for all strategic investments. By enacting this law, the Government foresees the attraction of investors, bringing new funds in the Albanian economy. Due to this, strategic investments are considered as having full public interest leading

[171] Al-Tax 'Tax system and Investment climate in Albania' (2016), fiscal paper no.2016/01/01, 6 <www.scribd.com/doc/294614306/Tax-System-and-Investment-Climate-in-Albania-2016> assessed 12 June 2017.
[172] Al-Tax 'Tax system and Investment climate in Albania' (2016), fiscal paper no.2016/01/01, 7-8 <www.scribd.com/doc/294614306/Tax-System-and-Investment-Climate-in-Albania-2016> assessed 12 June 2017.
[173] ibid 9.
[174] Law no.55/2015, date 28.05.2015.

to the approval of specific exemptions if investors will develop their activity to free economic zones. The Albanian Investment Development Agency (*AIDA*), in the country is the relevant authority providing information about the requirements to set up a business.[175]According to AIDA, Albania benefits from the extensive Free Trade Agreements (FTAs) with many countries in the whole world, giving free access to more than 600 million customers.

During the last 15 years Albania has made a huge progress in the investment field, attracting many investors to invest in Albania. The government reforms in this field helped to create an open taxation system in line with EU Member States, eradicating the past restrictions and opening the road of Albania towards the European Union. Albania now is an open market economy with a liberalized trade and completely privatized bank sector. Furthermore, Albania's geographical location offers a big trade potential with EU markets as it has 420 km coast line and is in the heart of Balkan Peninsula.

Section 5.3 – Foreign Direct Investments (FDI)

'Foreign direct investment means every kind of asset in the territory of a foreign State (host State) owned or controlled, directly or indirectly, by an investor of another State (home State). A more detailed definition is contained in Article 8.1 CETA[176] 2016 as follows: "Investment means every kind of asset that an investor owns or controls, directly or indirectly, that has characteristics of an investment, which includes a certain duration and other characteristics such as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk". Foreign investments are sometimes subject to risks such as direct or indirect expropriation. The main purpose of foreign investment law is to establish a favorable investment climate based on rules governing the various investment situations, including mechanisms to protect investors against foreign risks. Rules, for instance, taking a foreign property must be accompanied by prompt, adequate and effective compensation (so-called *Hull Formula*), are core provisions of any instrument governing foreign investments. The law of foreign investments is traditionally based on Bilateral Investment Treaties (*BITs*), concession agreements and, as far as dispute settlement procedures are concerned, the World Bank Convention for the Settlement of Disputes between

[175] See n 173.
[176] The Comprehensive and Economic Trade Agreement, is a free trade agreement between Canada & EU.

States and Nationals of Other States of 1966 (*ICSID Convention*). CETA is also a source of foreign investment law.'[177]

Albania enacted for the first time in 1993 the law "*On Foreign Investments*[178]" and has a liberal regime toward foreign investments. According to this law, foreign investments are allowed and treated based on equal conditions as domestic investments. They enjoy in anytime equal treatment, full protection and security.[179] The Albanian law "*on Foreign Investments*" is based on the most favored nation principle. As Albania is part of WTO, this is one of the most principles, meaning that it you grant a special favor to a country, you must grant this favor to all WTO Member States. The Republic of Albania is part of 43 bilateral agreements for protecting foreign investments.

The Albanian law "*on FDI*", brought some legal incentives for foreign investors like:

1. No need for a prior government authorization to start the investment;[180]
2. Foreign investment may not be expropriated or nationalized directly or indirectly;[181]
3. Foreign investors have the right to expatriate all the funds and from their investments;[182]
4. All foreign investments enjoy the "*Most Favored Nation treatment*";
5. The law provides for no limitation on the share participation of foreign ownerships, thus 100% foreign ownership of companies is permitted;
6. All foreign investors are protected as Albania is part of 43 BITs.

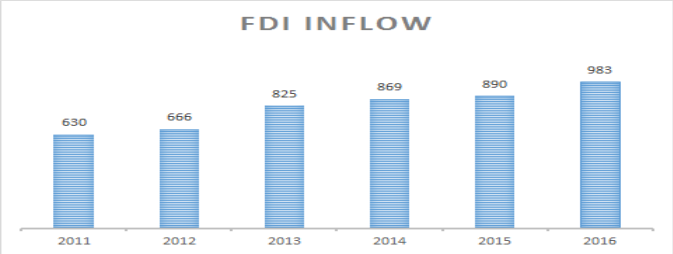

Table 11[183]

[177] Peter Fischer 'The law of the WTO' (2016) LL.M Program in European and International Business Law, University of Vienna, ch 1 14-15.
[178] Law no.7764, date 2.11.1993, later amended with the Law no.10316, date 6.10.2010.
[179] Law no.7764, date 2.11.1993, Article 2.
[180] Law no.7764, date 2.11.1993, Article 2, para.1.
[181] Law no.7764, date 2.11.1993, Article 4.
[182] Law no.7764, date 2.11.1993, Article 7.
[183] Table 11 – FDI inflow in Albania measured in million euros (INSTAT and Bank of Albania).

One of the most important benefits that this law introduced is that all the foreign investments enjoy full legal protection under the Albanian law. Therefore, all investors can resolve their disputes relying in an Albanian Court.[184] This is not the only option possible because investors can agree also to arbitration as Albania has implemented the New York Convention. Although the reforms undertaken are pushing Albania towards a further development, still the level of corruption in the juridical system remains high.[185] For this reason, foreign investors do not trust the Albanian Courts and therefore are more reluctant to choose International Arbitration as their dispute resolution.

Furthermore, the Albanian tax system in collaboration with the law "*on Entrepreneurs and Commercial companies*[186]", have created a favorable investment regime with low tax rates and low fees in establishing a business (*company*). First, corporate tax rate in Albania is levied at a rate or 15%, and this rate is one of the lowest rates compared to other countries in the Balkans. Second, the Albanian tax system creates advantages for the FDI, containing low tax rates and offering in some cases VAT reimbursement. Foreign companies can usually receive reimbursement of VAT paid for purchases, for which VAT registered businesses may claim deduction of input tax from local VAT refunds. Third, Albanian tax system does not distinguish between foreign and domestic investors, thus the same tax rates apply to both. This was the main policy of the government in 2013, arguing that foreign investments not only help the growing of the economy but also provide for new technology and capital. Thus, it is vital creating a favorable tax environment with the goal to attract them coming in Albania. In the last 20 years, these reforms brought a new era concerning foreign investments that lead to an economic growth and a lot of other benefits in the life of every Albanian citizen. In conclusion, FDIs are important because they bring new capital, raise the productivity of the economy, open new markets for trade, raise the competitiveness affecting the reduction of current deficit account, as well as increase employment and the well-being of the population. The more FDIs are, the faster and better the economy grows.

[184] Al-Tax 'Tax system and Investment climate in Albania' (2016), fiscal paper no.2016/01/01, 6 <www.scribd.com/doc/294614306/Tax-System-and-Investment-Climate-in-Albania-2016> assessed 12 June 2017. This section of this fiscal paper was mainly based on Article 8 of the Law no.7764, date 2.11.1993 (law 'on FDI').
[185] In 2017, Albania implemented the so-called "*Reform in Justice*", which was a condition for further negotiations aiming to join the European Union. The "*Process of Vetting*" will give end once forever the corruption of judges and prosecutors. This will lead Albanian and foreign citizens to trust Albanian Courts and seek their rights decisively.
[186] Law no.9901, date 14.04.2008 (Albanian Company Law).

Section 5.4 – Pros and Cons of investing in Albania

After highlighting the investment climate in Albania and the importance of the FDIs in the country's economy, as well as the way that the Albanian taxation system is affecting FDI, it is important to make a reflection considering the pros and cons of investing in Albania. When Albania entered in a SAA with EU, one of the requirements of this agreement relied on creating an open market economy, abolishing restrictions and creating a favorable environment for the free flow of goods and services. The Albanian government with its reforms created an advantageous tax system for the foreign investors that lead to a growth of the economy.

'According to *AIDA*, there are 10 top reasons of why to invest in Albania:

1. ***Liberal and reformist investment climate*** – Albania has implemented a liberal foreign investment regime with the goal of increasing FDIs. Albania is committed to developing a stable and predictable business climate by continuing the implementation of overarching reforms, fiscal consolidation aimed at reducing the national debt, improvement of regional cooperation, investments into infrastructure and reform of the educational system.
2. ***Albanian Investment Development Agency*** – Providing professional service for the investors free of charge.
3. ***Competitive labor cost*** – Albania is one of the most competitive low wage in Europe. Social security and income taxes are in line with many of EU Member States.
4. ***Young and well-educated population*** – 57% of Albania's population is under the age of 35 and each year more than 100.000 students are enrolled at Albanian Universities.
5. ***Competitive taxation and incentives*** – Albanian taxation system contains competitive tax rates and incentives for strategic investments.
6. ***Optimal geographical location*** – Albania has a strategic location in the western Balkans and enjoys a vicinity with major European markets. Furthermore, it is connected to Europe through various ports in Ionian and Adriatic seas.
7. ***Strong growth potential*** – Albania is facing one of the highest economic growth in the region. FDI annual inflows in Albania have increased significantly since 2008, averaging close to 1 billion USD per year for the period 2008-2014.

8. ***Free economic zones*** – The law on "*Free Economic Zones*[187]" has created a competitive environment for economic development areas to be developed by serious investors.
9. ***Free access to the large markets*** – Albania has signed several Free Trade Agreements (*FTAs*) with key markets offering customs free access to large market consumers.
10. ***Macroeconomic stability*** – The macroeconomic situation in Albania is characterized by stable prices, low inflation and solid exchange rates.'[188]

Regarding cons, investing in Albania could lead investors towards a great risk. The economy is still fragile even that many reforms were undertaken. The poverty rates are still on a high level and the Government must pay more attention on this layer of population. As every country in transition, the importance of personal relations between powerful citizens went beyond the law, plunging the country deep into an insecure situation.[189] This is one of the darkest sides of every evolving society that clouds the attraction of Foreign Direct Investments. The fight against corruption has started by the implementation of the so-called "*Reform on Justice*", that hopefully will bring corrupted judges and prosecutors before Courts. Regarding taxation, Albanian tax legislation offers a lot of incentives for investors, but this system needs to be improved.

CHAPTER 6 – Conclusions and recommendations

This Master Thesis aimed to give an overview of the impact of International Tax Law on the Albanian tax system under special consideration of EU membership negotiations. Albania is a country aspiring to join the EU. Hence, the integration process faced challenges and issues that were developed in the previous chapters of my thesis. The field of taxation is very complex and complicated, because humans behave in a way against the payment of taxes. For this reason, the main goal for Albania's fragile economy was to create a fair and strong taxation system. On one hand the reforms taken gave satisfying results that lead to a growth of the economy. On the other

[187] Law no.8636, date 6.07.2000.
[188] AIDA 'Why to invest in Albania?' (23 March 2017) <http://aida.gov.al/pages/why-invest-in-albania> assessed 18 April 2017.
[189] Al-Tax 'Tax system and Investment climate in Albania' (2016), fiscal paper no.2016/01/01, 12 <www.scribd.com/doc/294614306/Tax-System-and-Investment-Climate-in-Albania-2016> assessed 15 June 2017.

hand, Albania has a lot of work to do to harmonize its legislation with EU, as well as fulfill the obligations that arise after being awarded with a Candidate Status in 2014.

Related problems to the organization of the taxation system in Albania are numerous since this system has made a dramatic transitioning from a centralized economy to an open market one. The Albanian tax system reform remains one of the biggest challenges, as it is directly linked with the political performance and the well-being of every Albanian citizen. Taxes are essential in the economy of a State, being the main tool which help the collection of financial means for public expenditures. Accordingly creating a strong and fair tax administration system was obligatory.

The second chapter highlighted the economic and political factors that lead to the development of the Albanian tax system in the recent years. After the declaration of Independence in 1912, the Albanian State inherited a backward taxation system causing political instability. The economic crisis and the failure to implement the reforms needed were the main reasons that lead to the failure of implementing a new tax system. The first developments began with the establishment of the Kingdom of Albania. The Kingdom's Statute set for the first time the basic principles of taxation. During the Socialist regime, the taxation policy was based on the abolition of the private property, establishing a centralized market economy that prevented the country from further development. In my opinion, this was the darkest period of the history of Albania, which kept Albania away from the Western developed countries. The first legal acts aiming in the establishment of a new taxation system originated after the Communist System collapse. From 1992 till now, the taxation system of the Republic of Albania was subject to continuous development, creating a system based on principles like the other EU countries.

The third chapter gave an overview of the Albanian taxation system, the way it functioned and the taxes which governed into it. This study proved that this is a moderated system and the remaining goal is the further alignment with the taxation laws/directives of the EU. In my opinion, Albania has a strong and fair taxation system, subject to many reforms taken by the government in years with the intention of further improvement and harmonization with EU law. Abolishing the flat tax and introducing taxation based on progressive rates did influence in a positive way the economy of every citizen, as 85% of the Albania's population is composed of middle and low class. Furthermore, taxing the small businesses in 0 rates, relieved many people from the previous tax burdens and gave a big advantage to the economy.

According to ***EC Progress Report***: 'Regarding administrating cooperation and mutual assistance, GDT and Customs established a joint risk unit. The GDT receives support from IMF to implement the compliance risk management strategy, and from the United States for law revisions and debt/VAT collections. Concerning operational capacity and computerization, a new IT risk analysis model became operational in 2015 which helps better target tax audits'[190]. After studying the Albanian tax legislation, we conclude that the Albanian taxation system is based on fair rates of taxation compared to other countries in Balkans and Europe.

The fourth chapter emphasized Albania's status, the harmonization process being in line with the *Acquis*, as well as the impact of International tax law on the Albanian taxation system concerning the fight against the issue of double taxation. The requirements and obligations derived from the SAA between Albania and EU Member States lead to the starting of the law harmonization process. EU was created as an economic union between the Member States with the goal of generating an environment that won't affect the free movement of goods and services. Establishing a common market was a fundamental objective of the EU. In the field of indirect taxation, Albania has harmonized its laws with the respective ones in the EU, especially VAT and Excise duties. In my opinion, harmonizing these laws regarding indirect taxation was vital, because of the simple reason that these indirect taxes are precisely the ones which may affect the free movement of goods and services. Therefore, one of the obligations deriving from the SAA consisted in the alignment of the laws in the field of indirect taxation. In this context, Albania must further alight some VAT exemptions and excise rates which are not in line with the respective ones in the European Union.

Meanwhile, concerning direct taxation, there is no harmonization at all because Member States decided to treat these types of taxes at a national level. Every Member State chooses to adapt the best suitable tax system concerning their economic development, culture and tradition. Nevertheless, EC has adopted three main directives considering direct taxation which aim to remove the tax obstacles within the Internal Market. Furthermore, considering the issue of double taxation as a matter of International Law and its impact, Albania has made a huge progress signing till now 43 Double-Tax Treaties aiming the elimination of double taxation.

[190] Commission, 'Commission staff working document, Albania report 2016' COM (2016) 715 final, ch 16, 50.

The fifth chapter examines the investment climate in Albania, considering the way in which the Albanian taxation system affects the investment climate regarding Foreign Direct Investments. In the 20 years following the abolition of the centralized market economy, Albania has significantly progressed introducing as its main goal the attraction of many Foreign Investments. Many laws were adopted regarding *Strategic Investments*, *Foreign Direct Investments* that brought many legal incentives for the foreign investors. This was the main reason why the FDI inflow in the Republic of Albania grew up to 983 million Euros in 2016. The corporate tax in Albania is levied at a rate of 15%, making it one of the lowest rates compared to other neighbor countries. In some cases, the law on VAT offers reimbursement purchases. Taking in consideration the economic factors, we may finally conclude that Albania offers good opportunities for investment, as Albania is member of WTO and other important EU organizations, signing different FTAs with key markets in Europe. According to the World Bank's annual report, Albania moved up 32 positions in the overall ranking, being ranked now in the 58th position compared to the 90th of the previous year.[191]

Following the above-mentioned statements and the different problems taken in consideration in the Master Thesis, my recommendations are:

- '*Albania should implement an updated organizational structure, including clearly defined responsibilities within the tax administration and an independent appeal-mechanism*'[192];
- '*Implement actions against the informal economy to promote voluntary tax compliance*'[193]
- *Albania should further align VAT and Excise duties with the Acquis*;
- *Reconstruction of the law "on income taxes", as this law contains three different taxes, it should be better separating them in three different laws to have a better and clear idea*;
- *Member States should unify the agreements on the elimination of double taxation, as they have only implemented them from the OECD Model Convention*;
- *Harmonization in the field of direct taxation is essential in the fight against tax evasion*;
- *The laws should be written in a more explicit way, making them more understandable*;
- *Implement procedures regarding taxation of the foreign sourced income*.

[191] World Bank 'Albania Doing Business Report' (2017) <www.doingbusiness.org/data/exploreeconomies/albania> assessed 15 March 2017.
[192] See 190 50 see 'recommendations of EC in the field of taxation'.
[193] ibid 50.

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ABSTRACT

Taxation is a very complex field of law. As every country in continuous development, Albanian tax legislation faced significant changes. This was not achieved without serious difficulties, as Albania overcame many obstacles inherited from the Communist regime. The goal is to make this system more comprehensive and updated like every modern tax system in the European Union. Although many legislative reforms were undertaken, still Albania must continue to align its tax laws with the respective ones in the European Union.

The purpose of this study is to present on overview of the Albanian tax legislation and the impact of the EU tax law regarding EU membership negotiations. Harmonizing the EU tax legislation is a difficult task, but not unreachable as this is one of the main obligations to achieve the dream of joining the European family. In 2014, Albania was awarded the Candidate Status by the EU leading Albania towards the road of EU-membership. This is not anymore a dream for every Albanian citizen, as EU is offering stronger incentives for pushing Albania ahead with the reform to bring the tax system in line with EU standards.

The harmonization process is still not completed, but Albania is on a good way towards prosperity. The influence of EU-organizations on one hand, and the International aids on the other hand are accelerating this harmonization process with the hope of reaching the goal before 2022.

ABSTRACT (GERMAN)

Besteuerung ist ein sehr komplexes Rechtsgebiet. Wie in jedem Land, das sich in der kontinuierlichen Entwicklung befindet, hat die albanische Steuergesetzgebung erhebliche Veränderungen durchgemacht. Diese zu vollziehen war verbunden mit ernsthaften Schwierigkeiten, da Albanien viele Hindernisse überwinden musste, die es vom kommunistischen Regime geerbt hatte. Ziel ist es nun, dieses System ausführlicher zu machen und es auf den Stand aller modernen Steuersysteme in der Europäischen Union zu bringen. Obwohl inzwischen schon

viele Gesetzesreformen durchgeführt wurden, muss Albanien seine Steuergesetze weiterhin an die der Staaten in der Europäischen Union anpassen.

Der Zweck dieser Studie ist es, einen Überblick über die albanische Steuergesetzgebung und über die Auswirkungen der Einführung des EU-Steuerrechts auf die EU-Mitgliedschaftsverhandlungen zu verschaffen. Die Harmonisierung der EU-Steuergesetzgebung ist eine schwierige Aufgabe, aber keine unmögliche, und sie ist die Hauptverpflichtung für die Realisierung des Traums, sich der europäischen Familie anzuschließen. Im Jahr 2014 erhielt Albanien den Kandidatenstatus der EU, was das Land einen Schritt näher zur EU-Mitgliedschaft führte. Diese bleibt nun für die albanischen Staatsbürger kein Traum mehr, denn die EU bietet stärkere Anreize, Albanien mit der Reform voranzutreiben, um das Steuersystem mit den EU-Standards in Einklang zu bringen.

Der Harmonisierungsprozess ist noch nicht abgeschlossen, aber Albanien ist auf gutem Weg zum Wohlstand. Der Einfluss von EU-Organisationen einerseits und die internationalen Hilfsmittel andererseits beschleunigen diesen Harmonisierungsprozess mit der Hoffnung, das Ziel vor 2022 zu erreichen.