



FISCAL TREATMENT OF NPOs

ASSESSMENT OF NATIONAL
LEGISLATION AND PRACTICE FOR
NON-PROFIT ORGANISATIONS IN
ALBANIA

2018

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Prepared by:

Juliana Hoxha

Anora Topi

Klotilda Tavani

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Introduction

Civil society is an important factor in advancing the democratic development of Albania. It plays a key role in public education, represents an irreplaceable vehicle for public participation in decision-making and monitoring of government performance. Regardless, still civil society organizations in the country lack human and financial capacities, and face several challenges with regards to the legal and regulatory framework in their operation to fully play their role in the democratic development of the country.

In the framework of its work for the creation of an enabling environment for civil society organisations in Albania, Partners Albania for Change and Development prepared a monitoring report on the NPOs fiscal legal and regulatory framework and its implementation¹.

Although the sector has been in operations for about three decades, its regulatory framework is still in development, marking very frequent changes which in most of the cases do not go through an open and participatory consultative process. According to 2016 CSO Sustainability Index², the overall CSO sustainability in Albania remained stagnant.

The purpose of this paper is to give a general overview on fiscal legislation for non-profit organisations in Albania and its implementation, to identify gaps in the legal framework and the challenges encountered in practice, and to provide recommendations for further improvements.

The report was conducted in the framework of the project “Enabling Environment - Sustainable CSOs” supported by IBON International through the CSO Partnership for Development Efficiency (CPDE) within the “Advocacy on CSO Enabling Environment” program.

¹ The primarily law that regulates the establishment and operation of civil society organisations in the country is the Law no. 8788, dated 17,05,2001 “For the Non – Profit Organisation”. Therefore the report focuses only on NPOs. Other types of civil society organisations such as trade unions, religious organisations, chambers of commerce, and more are not subject of the analysis as they are regulated through other laws and their fiscal treatment differs from that of NPOs.

² 2016 CSO Sustainability Index for Central and Eastern Europe and Eurasia

Methodology

Partners Albania employed several methodological tools for the preparation of this report during January - April 2018, including: desk research, focus group meetings, consultations, and a small scale survey with NPOs, official requests for information and interviews with public officials.

A comprehensive review of Albanian Tax Laws applicable to non-profit organisations, and their implementation was conducted. This covered a wide range of sources: legislation, public data and reports published by public institutions and various reports written by civil society in Albania and international organisations. International sources were also consulted in order to compare the Albanian situation with other practices in the region and abroad.

A small-scale survey was conducted with non-profit organisations in order to collect and analyze first-hand information about their experiences with the tax issues. The purpose of the standardized questionnaire was to explore the issues related to fiscal treatment by getting information mainly on NPOs activity, Sources of income and Fiscal treatment. Four regional consultative meetings with local civil society organisations in Tirana, Kukës and Vlorë have also contributed to the understanding of issues faced by non-profit organisations with regards to tax treatment.

Interviews with public officials from the Ministry of Economy and Finances and Tax Administration have also been conducted. Finally, because of the lack of the published data for the sector, Partners Albania sent official requests for information to several public institutions such as, Tirana First Court of Instance, General Directorate of Taxation, Agency for the Support of Civil Society, and Ministries.

1. Understanding NPOs

1.1. Types of NPOS

The Albanian Constitution recognize the right of any citizen to collectively organize for any legitimate purpose. It also provides that the registration of organisations and associations in the court is done according to a procedure as foreseen in the law³.

The primary law that sets the rules for the establishment, registration, functioning, organization, and activity of nonprofit organisations that carries out activities in the good and interest of the public, is the Law no. 8788, dated 7.05.2001 "For the Non – Profit Organisations". It recognizes the rights of any natural or judicial person, local or foreign, to establish a non-profit organization. The law recognizes three types of non – for - profit organisations (hereinafter NPOs): (1) associations, (2) foundations and (3) centers.

According to their form of organisation, non-profit organisations are classified as:

- NPOs with membership (associations);
- NPOs without membership (foundations and centers);

According to their registration, non-profit organisations are classified as:

- Domestic organisations (established and registered under Albanian law);
- Foreign organisations (established and registered under the law of a foreign country but registered under Albanian law when exercising activity in Albania);

Non-profit organizations, subject of the Law no. 8788 acquire juridical ability after they are established and registered at the Tirana First Court of Instance, in conformity with the conditions and procedures provided for in the law. Branches of foreign nonprofit organizations are also subject to the same registration procedures. The procedures for the registration of non-profit organizations in court and the deposit of their documents into the respective Register are regulated by the Law No. 8789, dated 7.05.2001, For the Registration of NPOs.

1.2. NPOs Activity and Sources of Income

NPOs activity is conducted in an independent manner and without being influenced by the state. For the realization of the purpose and object of activity contemplated in the charter, non-profit organisations have the right to exercise any kind of lawful activity. As provided in the Law no. 8788, "For the Non – Profit Organisations", non for profit activity means any economic or non-economic activity on the condition that the income or assets of the non-profit organisations, if there are any, are used only for the fulfillment of the purposes specified in the organisation' statute.⁴

A non-profit organization may generate incomes from dues, grants and donations, as well as from economic activity and the assets owned by the organization⁵. Non-profit organisations have the right to participate, like all other legal entities, in tendering and procurement of grants, contracting and purchases and sales by state bodies of public services, goods and public property, and the transfer of public services and respective properties from the public sector to non-profit organisations.

³ The Constitution of the Republic of Albania, Article 26, Point 1 and 2

⁴ Law no. 8788, dated 7.05.2001 "For the Non – Profit Organisations", Article 2

⁵ Idem, Article 35

NPOs have the right to organise fundraising activities to accomplish the goals and object of their activity or to support the goals and activities of other non-profit organisations. Special laws determine the rules for the public collection of funds. Financial relations, mutual rights and obligations with donors are set in accordance with the relevant agreements, but respecting the requirements of the statute of the non-profit organisation and law “For the Non – Profit Organisations”.

Primary sources of funding for NPOs are from membership fees, grants and donations, and non-profit organisations are exempt from tax on revenues realized from these types of funding⁶. In addition, for these types of funding, NPOs are not considered “taxable person” as per definition in the VAT Law⁷, therefore they are exempted from profit tax and VAT.

If NPOs carry out economic activity to generate incomes to meet the goals set out in the statute and the establishment act, they are considered “taxable person”. The economic activity should NOT be the primary activity of the NPO (the non-economic activity should obviously prevail) and the annual revenues from the economic activity should not exceed 20% of the total annual income. If this amount exceeds the VAT registration limit of 2 million ALL (approx. 15,000 EUR) then the NPO, like any other taxable person must register and declare VAT, according to the Law on Tax Procedures of 2018.⁸

1.3. The size of NPO sector

The situation with the real number of NPOs in the country continues to be ambiguous, due to the lack of a unified and updated electronic register of NPOs nationwide. All newly established NPOs should be registered at the Tirana First Court of Instance. This process is assessed as problematic and has created many financial and administrative burdens for those willing to establish an NPO⁹. Furthermore, NPOs cannot enter any financial relations if they do not have a bank account, the opening of which necessarily requires the receipt of a registration document to the tax authority; therefore NPOs should be also registered at this authority.

There is a big discrepancy in data provided by Tirana First Court of Instance and the Tax Administration as regard to NPOs. While the number of the NPOs registered at the Tirana First Court of Instance is 7,383, only 4,136 are reported to be registered in the Tax Administration and out of these only 2,032 NPOs or 50% are in the active register of the taxpayers¹⁰ (see graph no.1)¹¹. As shown in Graphic 2 below, Tirana First Court of Instance also reports that there are 345 new NPOs registered in 2017 (198 Associations, 61 Foundations and 86 Centers), while only 238 are registered in Tax Administration.

Main issues as regard to the accurate data on the sector are as follows:

- Information from the Tax Administration is not accurate, due to the mixing of NPOs with other entities in their registers, as universities, political parties, etc.
- Electronic tax register has undergone several changes (from manually registration of all the data since the establishment of the institution, the IT system has changed twice), creating problems regarding classifications of the entities registered in years, especially for the NPOs.

⁶ Idem, Article 40

⁷ Law NO. 92/2014 For Value Added Tax in the Republic of Albania

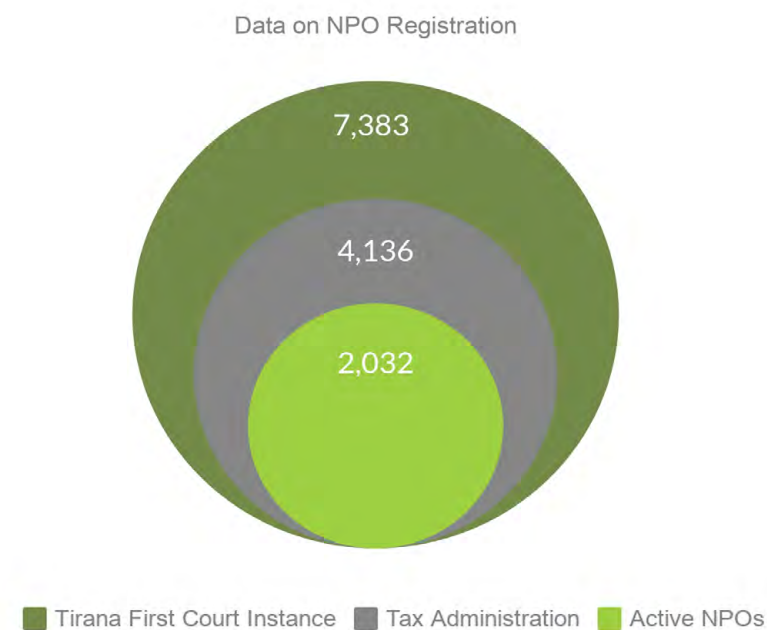
⁸ The new regulation in force was strongly opposed by the small business representatives in Albania for creating heavy compliance burden. Frequent changes in fiscal legislation and related procedures have created negative impacts on the whole system. Albania has lost a considerable position in Doing Business 2018 of paying taxes compared to the previous year. Link: <http://www.doingbusiness.org/data/exploreeconomies/albania#paying-taxes>

⁹ <http://partnersalbania.org/publication/monitoring-matrix-on-enabling-environment-for-civil-society-development-country-report-for-albania-2/>

¹⁰ According to provisions in the Law no. 9920, “On tax procedures”, “active taxpayers” are the ones that have declared at least one tax declaration within the 12 last consecutive months. In cases when the organisation: (1) does not carry out any activity for 12 consecutive months, (2) does not submit any tax declaration for a period of 12 consecutive months or (3) declares to the tax authorities’ suspension of its activities, it is automatically transferred to the passive register of the taxpayers. When in passive register, the organisation has no obligation to submit any tax declaration and no penalties are applied for non-declaration.

¹¹ All data are based on the official responses by the respective institutions to the Request for Information submitted by Partners Albania

Graph no. 1



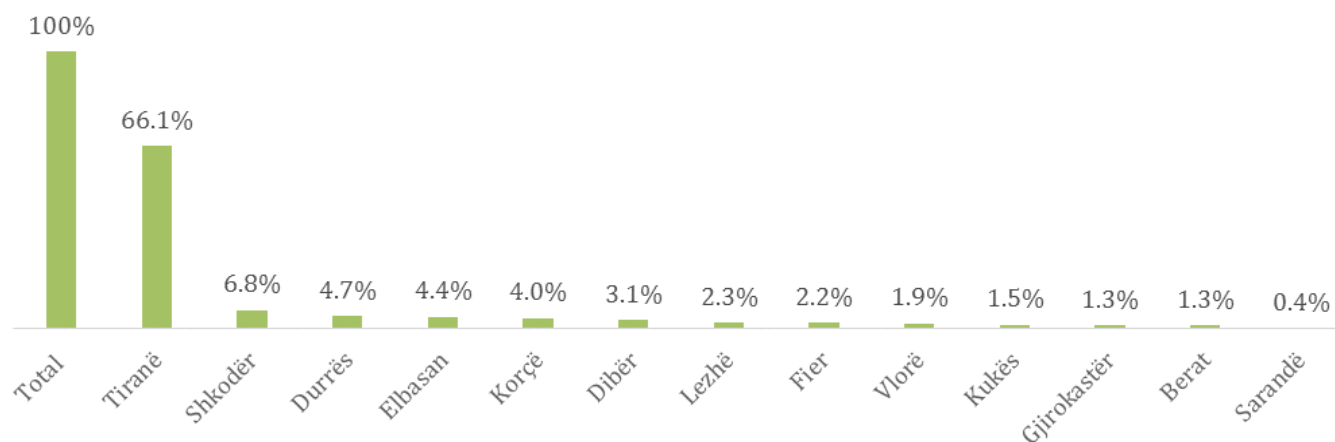
Graph no. 2



Regarding the distribution of NPOs registered to the tax authorities by cities, it is evident that the largest number of registered NPOs is located in Tirana, followed by Shkodra, Durrresi, Elbasan and Korca (see graph no. 3).

Graph no. 3

Geographic distribution of NPOs

**[Recommendations:]**

- As evidenced by the contradictions in the data provided, it is difficult to understand the sector in a situation where there is not yet a unified electronic register of NPOs applicable to all relevant institutions responsible for registration and regulation of NPOs activity. Therefore, as a first and outmost important step in the efforts for the creation of an enabling environment for CSOs development in the country, remains the preparation and publication of a comprehensive database that provides information on NPOs (the number, scope of work, geographical distribution, legal form, number of employers and volunteers, annual turnover, sources of funding, etc.).
- Creation of a special electronic register only for NPOs (as defined by the law on NPOs) within the Tax Administration. It would not only provide accurate information on the sector, but would also allow for a differentiated tax treatment of NPOs in accordance with their non-profit nature and type of activities. The register would enable the measurement of impact and contribution of the sector to the economic development of the country.

2. Fiscal treatment of NPOs and key legislative changes over the years

Fiscal treatment of NPOs remains problematic and presents a significant obstacle in the operation of NPOs, their sustainability and development.

Since 2001, when the Law on NPOs was adopted, many changes and amendments to the legal framework on fiscal treatment of NPOs have been made, in some cases without consultations with the sector, or without taking into consideration the feedback and suggestions of the experts. As a result, the fiscal regulatory framework is not properly prepared based on the nature and mission of NPOs, and its implementation in practice is unclear and misinterpreted by both tax authorities and NPOs.

In the law on NPOs adopted in 2001 it was stipulated that non-profit organizations, regardless of their form of organization, their mission and types of activities, are exempt from income tax for donations and membership fees¹², living out grants and other types of incomes generated by NPOs through their non-economic activity. The law recognized the right of NPOs to carry out economic activity to generate incomes in support of their mission, but no provision were provided in this law or other laws on the ratio of economic activity to the total activity of NPOs, leaving it evasive in terms of fiscal treatment and reporting to state authorities.

Shortcomings in the Law on NPOs and other related laws and regulations on fiscal treatment of NPOs, led to the classification of grants as taxable income in the VAT law in 2008. As a result, following an instruction issued for tax officials on the application of VAT for non-profit organisations, all NPOs were automatically registered for VAT and Tax on Profit, classifying NPOs as “large business”, in full contradiction with the nature and definition of NPOs: No profits - no tax on profits. On this base, tax authorities initiated several tax inspections to the sector.

On the other hand, there was misinterpretation by donors on this provision, and they started to request for business invoices (VAT invoices) to be issued by NPOs on the grant contracts creating so, high burden to the sector. The sector faced several negative implications, such as: closure of NPOs, increased costs of compliance, fines/penalties imposed by tax authorities for issues related to filing and declaration of taxes, extra costs in implementing donor funded projects, etc.

With the amendments to the NPO law in 2013, improvements were made with regards to clarification of “grants” and “economic activity”. The amendment provides clear definition on these terms, but still remained evasive regarding the ratio between the economic activity and the non-economic activity of an NPO (Law 92/2013 on some changes and amendments to the Law 92/2013, article 1). Another positive impact of this amendment was inclusion of “grants” and “bank interests” in the exemption from tax on incomes. Still, regardless the improvements in the NPO Law the situation with the registration of NPOs for VAT and Tax on Profit did not changed, until 2015.

The civil society, with its continuous efforts, has played a key role in improvement of the legislation for the sector. Fiscal treatment of NPOs was one of the three main pillars of the dialogue between NPOs and the Albanian Government in the National Conference “Social Partners – Time for Action”, organized by Partners Albania in December 2013. The conference was concluded with a Statement of Representatives of Civil Society in Albania, and the commitment of the government to work with the civil society expert to address the issues of the statement. As a result, the new Law on VAT in Albania enacted in 2015 and the Decision of the Council of Ministers on the implementation of the Value Added Tax no. 953, dated on 29.12.2014, finally provided clear provisions for the sector, as follows:

¹² Law no.8788, dated 7.5.2001 On Non-Profit Ogranisations, Article 40

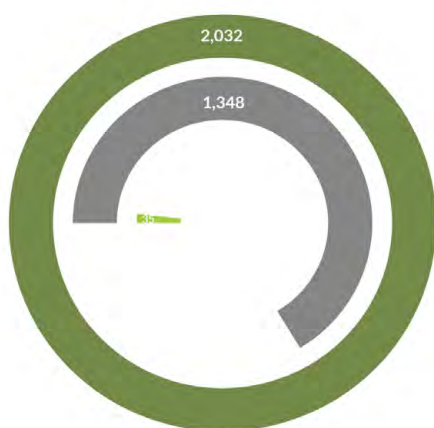
1. Grants are VAT exempted;
2. The turnover from economic activity should not exceed 20% of the total annual turnover;
3. Clear definitions on the threshold for VAT registration. The new law clarifies and confirms the exemption of the NPOs from VAT and none of them has been automatically registered from 2015 on VAT or Tax on Profits.

But, the situation remains problematic with the NPOs that have been registered for VAT in the period 2008-2014 and continues to be in the system, creating big confusion among NPOs, tax authorities, and donor community about the sector being in and out of the VAT scheme.

Based on the data from General Directorate of Taxation, there are 1,348 or 60% of NPOs registered for VAT, and most of them have never carried out any economic activity, while about 1,043 non-profit organisations are registered for profit tax in the tax register database (see graph no. 4 and 5).

Graph no. 4

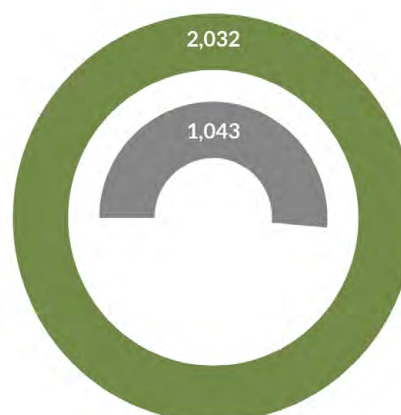
VAT Registration of NPOs



■ Active NPOs ■ Registered with VAT ■ De-registered from VAT

Graph no. 5

Data on NPOs Registered for Profit Tax



■ Active NPOs in Tax Register ■ NPOs-Registered for Profit Tax

Representing unjustified financial and administrative burden for NPOs, this has been one of the main issues of discussions between civil society experts and the Ministry of Finance at the National Conference: “Boasting towards a better enabling environment for civil society organizations in Albania”¹³, organized by Albanian Office of Regional EU project Technical Assistance for Civil Society Organizations (TACSO) on December 2016.

The representative from Ministry of Finance accepted that the registration of CSOs for VAT has not been correct, but also declared that there is an easy procedure for de-registration based on a request presented by NPOs to the tax authorities. This statement is supported by the interviews with tax administration during the preparation of this report, and the information provided in response to the request for information presented by Partners Albania on the number of NPOs de-registered from VAT. According to the information by the General Directory of Taxes, there are 35 NPOs that have been de-registered from VAT in the period 2016-2017, and the procedure for de-registration is based on the law on VAT and its guidance.¹⁴

But, what does the law provides for on de-registration process?

Firstly, article 122 of the Law no. 92/2014 on “Value Added Tax” refers to the **small business** that claim to tax authorities de-registration from VAT when its turnover in the last 12 calendar months falls below the minimum registration limit for VAT. There is no reference to NPOs in this article or others in the law.

¹³ <http://www.tacso.org/Publication/ArchiveRead/14590?title=Albania:%20National%20Conference%20on%20Enabling%20Environment%20for%20CSOs%20in%20Albania>

¹⁴ Law no. 92/2014 “On the Value Added Tax in the Republic of Albania, Art. 122 , and Guidance no. 6 /30.01.2015, Art. 6

Secondly, Article no. 6, point c) of the Guidance no. 6 /30.01.2015"On Value Added Tax", refers to the cases when a "**taxable person**" registered for VAT has never been compelled to be registered nor has voluntarily exercised the right to be registered for VAT, claim de-registration to tax authorities. As per the same article in the guidance, the entity may be de-registered after **it is found out**¹⁵ that it has neither been forced nor voluntarily exercised the right to be registered for VAT, but still **is responsible for performing any VAT liability** from the moment it is registered until the date of de-registration from VAT. This is not the case with NPOs that have been automatically (involuntary) registered by tax authorities for VAT.

Considering as above, it is evident that there is no legal bases for de-registration of NPOs from VAT, putting a question mark on the number of NPOs de-registered from VAT provided by tax administration. Therefore, there is a big number of NPOs still registered in the VAT system, even though they have never carried out economic activity.

[*Recommendations:*]

- Preparation of guidelines on the fiscal treatment of NPOs, to serve as an orientation document to tax inspectors, NPOs and any interested stakeholder on the application of the legal framework in force. This document will be useful to the tax inspectors in their work with non-profit organisations, and would also be used as an "official" material to be used with donors.
- In order to clarify the VAT de-registration issue, it is recommended that the tax administration prepares a special procedure for de-registration of all NPOs from the VAT system. The procedure should be provided within the legal framework and published, accompanied by specific guidelines for the responsible structure on its application. Trainings of NPOs representatives and tax inspectors would be necessary for the successful implementation of the procedure.

¹⁵ The tax administration has the right to audit the entity registration documentation and other related activity documents to secure the necessary proof for a final decision.

3. Fiscal treatment of economic activity of NPOs

As mentioned in the previous section, **NPOs may engage in economic activities** to generate incomes in support of their mission. And like any other entity that carries out economic activity, regardless of its form of organization, NPOs are considered “taxable person”, and are required to register for profit tax, according to the provisions of the Law no. 8438, dated 28.12.1998 “On Income Tax.” If the annual turnover from the economic activity is more than 2 million ALL (approx. 15,000 EUR) they must register for VAT¹⁶.

Pursuant to the definition on the VAT Law, **Economic Activity** is considered “any activity carried out by producers, traders, persons supplying goods or services, including extractive, agricultural and professional activities. Economic activity is also considered to be the use of embedded or intangible assets for the purpose of generating incomes of continuous character”¹⁷.

Like any other taxable person, **NPOs have the right to claim the VAT** refund for their economic activity, if they meet the criteria described in the VAT law¹⁸.

- has carried forward the deductible VAT surplus for 3 consecutive months;
- the amount of VAT claimed must exceed 400,000 ALL (approx. 3,000 EUR).

Considering the non-profit nature of CSOs and the limitations presented in the related laws on the level of economic activity carried out (the economic activity is a secondary activity of NPOs, and the annual revenues from the economic activity should not exceed 20% of the total annual income), it is evident that the economic activity of NPOs cannot have a continuous character. As a result, they cannot meet the criteria requested by the law to claim VAT refund, thus making it practically impossible for NPOs to benefit from the VAT refund.

NPOs have also the right to benefit from VAT exemption of some economic activities that are considered as “activities of general interest” by the VAT law¹⁹. In order to benefit from VAT exemption for these types of activities, NPOs must meet all three criteria as below, provided in the Council of the Ministers Decision No. 953, dated 29.12.2014 For Implementing Provisions of the Law No. 92/2014:

1. The decision-making bodies of the NPO must not have interests directly linked to the activity of the organisation,
2. The non-economic activity of the organisation must evidently prevail in relation to the rest of activities, and the revenues from the non-economic activity of NPO should prevail. Economic activity cannot exceed 20% of non-profit organisations' annual revenues.

Products or services offered by NPOs should not compete with the commercial profit sector. The amount of income from the economic activity of the organization as its secondary activity carried out by the organization for the purposes of the non-for-profit activity for which it is established, collected during the calendar year shall not exceed 20% of the total annual income of the organization²⁰.

¹⁶ Law no. 9920, dated 19.5.2008 For tax procedures in the Republic of Albania, amended

¹⁷ Law no. 92/2014 “On the Value Added Tax in the republic of Albania, Art. 4

¹⁸ Article 77, of the Law on VAT, and following the procedure prescribed in the Instruction no.6, dated 30.01.2015, “On VAT”

¹⁹ Law dated 24.07.2014 On the Value Added Tax in the Republic of Albania, Article 51

²⁰ Decision No. 953, dated 29.12.2014 For Implementing Provisions of the Law No. 92/2014, Article 2

NPOs meeting these criteria should file an application along with the list of documents requested²¹ to the Regional Tax Directory for VAT exemption. The authorization for the VAT exemption is issued by the General Director of the Tax Administration, with duration of three years, with the right for renewal.

In the framework of the preparation of this report, PA submitted a request to the Tax Administration asking for the number of NPOs submitting an application and benefiting from the VAT exemption based on the criteria and procedure of the law, but this information was not provided.

[*Recommendations:*]

- Considering that the VAT reimbursement scheme for CSOs' economic activity is not applicable for the reasons mentioned above, it is recommended the revision of the scheme and introduction of a new one specifically for CSOs that takes into consideration their non-profit nature, and the character of their economic activity.
- Revision and broadening the spectrum of the activities considered as of "general interest" and are VAT exempted by the VAT Law, including other types of activities carried out by CSOs that serve to the general public interest.

²¹ The list of documents includes: Court Decision; Statute of the organisation and establishment act; a statement listing all the products and services provided to members and/or to third parties along with prices; statement of NPO's mission and goals as well as the main programs; statement of beneficiaries or groups in need that NPO serves; sources of income, including percentage of income deriving or expected from the economic activity.

4. Reimbursement of VAT paid for goods and services supplied under EU and other foreign donors funded projects

In principle, all types of grants and donations are VAT excluded. In cases where the financial agreements ratified by the Albanian Parliament or the grant agreements approved by the Council of Ministers provide for the non-utilization of the foreign financial resources to pay taxes, including or not the value added tax, the value added tax paid is reimbursed to foreign donors from the Treasury System, within 30 days, according to the rules set by the Minister of Finance.²²

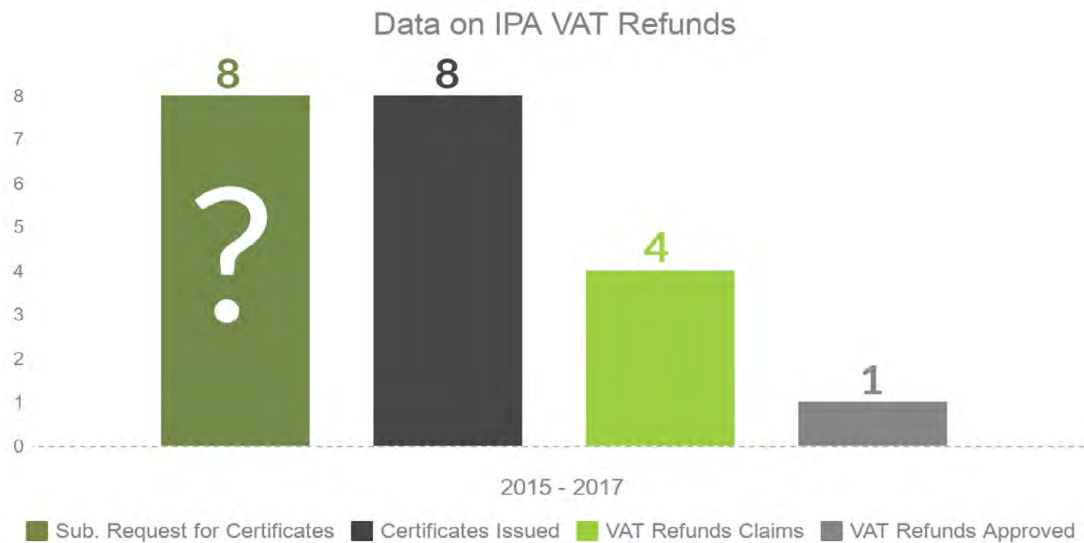
Only for the projects funded through the Instrument for Pre-Accession Assistance (IPA), there is an instruction of the Ministry of Finance issued in 2013 on the VAT reimbursement procedure²³, pursuant to Article 26 of Law No. 9840 dated 10.12.2007 "On the ratification of the Framework Agreement between the Government of the Republic of Albania and the Commission of the European Communities on the Rules for Co-Operation Concerning the EC - Financial Assistance to the Republic of Albania in the Framework of the Implementation of the Assistance under the Instrument for Pre-Accession Assistance (IPA)". Based on the instruction, contractors (non-profit organisations) of IPA-funded projects shall be reimbursed by the Regional Tax Directorate for VAT paid on goods or services supplied under such projects, following the submission of the VAT-reimbursement application and other relevant documents as provided for in this Instruction. The agreement itself and the instruction in support of its implementation have resulted non-effective, as up to date only one organization has been reimbursed, according to official data received by the General Directory of Taxes.

As shown in the graphic 6, there are **only 8 (eight) Registration certificates for IPA-funded VAT reimbursement purpose issued in the period 2015-2017** (the first step of the VAT reimbursement procedure is registration of the project within the Regional Tax Directorate and receipt of the certificate for reimbursement purpose), **only 4 (four) CSOs have applied for VAT reimbursement** (after the implementation of the project, the NPO submits to the Tax Authorities the application for VAT reimbursement concerning operations falling under the contract, along with the supporting documents as provided in the instruction). Three applications of CSOs for VAT reimbursement, out of four (4) have been refused for not meeting the legal criteria foreseen in the instruction, according to GDT.

²² Law dated 24.07.2014 On the Value Added Tax in the Republic of Albania, article 77, points 2 and 5.

²³ Instruction No. 4 dated 22.01.2013 of the Ministry of Finance "On some additions to Decision No. 17, dated 13.05.2008 "On the Value Added Tax" amended"

Graph no. 6



The main problematic issues of the agreement and the instruction that have resulted in the above situation are as below:

- a) The Agreement between the Government of the Republic of Albania and the Commission of the European Communities (Law No. 9840 dated 10.12.2007), is not inclusive and do not provide for VAT reimbursement of other EU funding mechanisms and instruments at local, regional, and international level, for which Albanian NPOs are eligible to apply and a considerable number have been / are implementing such projects. To be mentioned are: EIDHR, IPA Cross – Border, Erasmus+, etc.
- b) The non-standardized request for the foreign implementing partners of IPA funded projects that are established and operating in other countries to register for business purposes in Albania, as a condition by regional tax offices. As this provision is not clearly stated in the instruction, the registration of the project for VAT reimbursement is based on the interpretation of the tax officials. This ambiguity in the instruction has resulted in rejection of projects registration for VAT reimbursement by tax authorities. As a practical example to evidence this, is the case of Partners Albania itself. Partners Albania is implementing two IPA funded projects with partner organizations established in Italy. One project with two Italian organisations as implementing partners is registered for VAT reimbursement, while the application for the other project with one implementing partner (one of the partner organisations in the first project) is rejected only on this base.
- c) The reimbursement procedure is too long and hampers the financial viability of NPOs. They have to pay a considerable amount of VAT for goods and services purchased during the project implementation from their own sources, and apply for VAT reimbursement after the approval of the final report by the EUD, which can extend up to 18 months after the implementation of the project.
- d) Due to recent reorganization of the Tax Authority in Albania in 2016, VAT reimbursement is centralized and processed in the new dedicated VAT Reimbursement Department within the GDT, meaning that NPOs from other cities should mail all the documents to the Tax Authority Headquarters in Tirana with an estimated additional cost of 150-200 EUR.

Comparing this situation with the other Western Balkan countries, it can be easily noticed that Albania remains behind other countries with regards to the preparation and implementation of the legislative and administrative framework on the VAT treatment of foreign and UE funded projects. Almost in all other countries in the region (Serbia, Montenegro, BiH, Macedonia) is applied **VAT exemption**, while in Kosovo the VAT reimbursement is done on monthly bases during the project implementation²⁴.

²⁴ For more information on the procedure in each country please refer to Guidelines on VAT Exemption Procedures for EU Funded Projects in the IPA Countries – January 2016, published by TACSO at: http://www.tacso.org/data/dokumenti/pdf/doc_vat_report_january2016.pdf

In a situation when the biggest donors in the country, like EU and the Swiss Government through the Swiss Development Cooperation (SDC) are applying the sub-granting schemes as part of their funded projects on a large scale, apart from the positive effects in providing more support to small local NPOs through this approach, it has created additional barriers to the financial viability of these NPOs. The respective agreements with the Albanian Government for the VAT reimbursement have not foreseen this new reality, and as a result the sub-grantees are not eligible for VAT reimbursement of VAT paid on goods or services supplied under such projects.

There is no legal base for them to apply for VAT reimbursement, and as a result the VAT is an added cost that they have to pay from their own budgets.

[*Recommendations:*]

- As a first and immediate step to relief NPOs from the burden of VAT paid on goods or services supplied under EU and all foreign funded projects for which there are financial agreements ratified by the Albanian Parliament or grant agreements approved by the Council of Ministers providing that that value added tax paid is reimbursed to foreign donor, would be the drafting and approval of an Instruction of the Ministry of Finance and related documents. It should include clear provisions on the VAT reimbursement of NPOs for all projects funded through foreign donors, in support of the implementation of the Law no. 92/2014, dated 24.07.2014, "On the VAT in the Republic of Albania", article 77, points 2 and 5. The Instruction should provide for VAT reimbursement for all types of beneficiaries, being it the direct grant beneficiary, implementing partner, or a sub-grantee.
- Drafting of clear guidelines for tax inspectors and officials on the correct implementation of the new Instruction, along with trainings to ensure their unified understanding and interpretation of the Instruction and related documents.
- Wide awareness raising campaign and information sessions with NPOs to get informed, understand and apply the new procedure.
- At a further stage, as a final solution of this issue, would be the approval of the procedure for the VAT exemption for all goods and services supplied by NPOs under EU and other funded projects, for which there are financial agreements ratified by the Albanian Parliament or grant agreements approved by the Council of Ministers providing that that value added tax paid is reimbursed to foreign donor. The good experiences of the other countries from the WB region, would serve as a model for this procedure.

5. Other taxes applicable to NPOs

5.1. Social and health insurance contributions

Based on the law on social and health insurance contributions²⁵, NPOs, like any employer, must declare and pay monthly social and health insurance contributions for at least one employee. This obligation applies to all NPOs, since at the start of their operation, including organizations that run their activities based on voluntary work of their members, presenting thus a real barrier to the free initiative of individuals to establish non-profit organizations and to promote voluntarism as a human value in support of people in need. As shown in the graphic below on tax liabilities of CSOs, difficulties of CSOs to comply with this obligation have created considerable unpaid tax liabilities to the tax authorities, or have forced them to switch to passive status.

[Recommendations:]

- Proposing a differential treatment of CSOs with regards to the payment of social insurance and health insurance contributions, taking into consideration the voluntary activity on NPOs.

5.2. Local Taxes and Fees

The legal framework²⁶ on local taxes in Albania determines the rights and duties of local government units to apply local taxes, their collection and administration.

Based on an analysis of some local taxes applied by biggest municipalities in 2017 to CSOs it is noticed that generally, CSOs are treated by municipalities as businesses with regards to their local fiscal treatment. So, as shown in the table below, there is a differential treatment only for the Property tax (including tax on building and agriculture land), while for the two other taxes (signboard and environment tax) the same treatment is applied by most of the municipalities.

²⁵ Law no. 9136, dt. 11.02.2003 "For the collection of compulsory social insurance and health care contributions in the Republic of Albania" (amended with law no. 9164, dated 18.12.2003, 9329, dated 6.12.2004, no.9933, dated 26.6.2008, no. 10/2012, dated 9.2.2012, 87/2014, dated 17.7.2014, no. 143/2015, dated 17.12.2015, amended through a decision of the Constitutional Court no. 60, dated 16.9.2016, normative act no. 1, dated 25.1.2017)

²⁶ Law no. 139/2015, "On local self-government", Law no. 9632, 31.10.2006, "On local taxes", amended.

Table 1. Local taxes

Municipal- ities	NPOs			Small business		
	Property tax ALL/sq./ year	Signboard tax ALL/year	Environment ALL/year	Property tax ALL/sq./year	Signboard tax ALL/year	Environ- ment ALL/year
Tirana	50-100	35,000-45,200	10,000	200-280	35,000-45,200	3,500-10,000
Fier	60	22,500	3,000-5,000	150-300	22,500	10,000- 25,000
Shkodra	60	22,500	6,000	60-300	22,500	8,000-13,000
Korça	60	22,500	20,000 cleaning 5,000 lights 5,000 greenery Total: 30,000	150-300	22,500-45,000	5,000-15,000 cleaning 1,000-9,000 lights 4,000-5,000 greenery Total: 10,000- 29,000
Vlora	30-60	22,500-45,000	5,000	75-300	22,500-45,000	5,000-15,000
Durrës	20-100	22,500-45,000	500 cleaning 500 lights 1,500 greenery Total: 2,000	50-280	22,500-45,000	5,000-20,000 cleaning 2,000-3,000 lights 1,500 -10,000 greenery Total: 8,500- 33,000

This situation at the local level is a reflection of ambiguity and confusion in the fiscal treatment of CSOs at the national level, not treating them as a special entity with a special nature, mission, financing model, ways of operation, and beneficiaries, but rather treating them as business. This treatment is also evident in the latest changes in the Tax on Building, introduced by the government at the end of 2017²⁷. So, based on these changes, the tax rate on building will no longer be a fix rate, but will be applied as a percentage of the tax base (value of the building), based on two main categories, as follows:

- a) 0.05% for the building used for housing;
- b) 0.2% for the building used for economic activity;

As it is unclear how this tax will be calculated and applied for NPOs by the municipalities that have the authority to define subcategories and respective rates of local taxes²⁸, there is no provision in the law for the inclusion of NPOs in the list of categories exempted from this tax. While state and local government properties that are **used for a non-profit aim** are exempted from the building tax²⁹, NPOs whose mission and whole activity is **non-profit** are not included in the list.

²⁷ Law 106/2017 "On some changes and amendments of the law 9632, date 30.10.2006, On local tax", Article 22/2

²⁸ Law no. 106/2017 For some changes and additions in the Law no. 9632, dated 30.10.2006, "On the Local taxes System", amended, Article 5

²⁹ Law 106/2017 "On some changes and amendments of the law 9632, date 30.10.2006, On local tax", Article 22

[*Recommendations:*]

- Amendment of the Law on Local Taxes by introducing differential treatment for CSOs taking into consideration their non-profit nature.

6. Tax treatment for corporate and individual donations

The law on Non-Profit Organisations grants the right of NPOs to receive donations from any private or public person, Albanian or foreign, but the tax treatment of this donations is not regulated. Countries worldwide legally allow tax preferences for donations such as; tax deductions, tax credits³⁰ or other designated schemes with respect to contributions by individual or companies to non-profit organisations.

In Albania, only donations in the form of sponsorship are recognized and regulated by Law on Sponsorship³¹. The law recognizes and provides for tax benefits only for sponsorships by private companies, while individual donations are not recognized and as a result do not benefit from tax deduction.

Tax system permits donations between 3% and 5% (depending on the type of activities sponsored) of profit before tax by entities that have the quality of merchant, being physical, juridical persons, local, foreign, or joint ventures, which is not considered encouraging for private companies to increase their donations. The donation is recognized by tax authorities based on the sponsorship contract and related proofs of the sponsorship. The list of deductible activities is limited and includes only humanitarian, cultural, artistic, sport, education, environment, works of literature, science and research activities, leaving out democracy and human rights, as main activities of many CSOs for the benefit of the general public. Foreign companies might also apply for deductions under the law for sponsorship to Albanian NPOs, but only if they are legally registered in the Albanian institutions and also provide the required proofs. Another shortcoming in the law on sponsorship is that in-kind donations and gifts carried out by corporations are not recognized as deducted expenses.

Due to lack of clarity among tax inspectors on means of verifications, often donations are considered as an attempt for tax evasion. In these circumstances, many companies do not apply tax deductions provided in the law on Sponsorships.

[Recommendations:]

Creation of an enabling environment for corporate and individual donations through:

- Recognition of philanthropic activity in the legal framework to promote and regulate it as a distinct activity apart from sponsorship. In this context, it is important to increase the fiscal incentives for corporate donations and to introduce fiscal incentives for individual donations.
- Preparation of policies and introduction of incentives that encourage the partnership between NPOs and private sector, as two important actors in the development of philanthropy in the country, based on existing local models and international experience.
- On a practical level, it is necessary to increase awareness and education of the tax inspectors and officials on the philanthropic activity, in order to avoid possible barriers hindering further development of this activity in the country.

³⁰ A tax deduction reduces the tax base or a percentage of the amount of the contribution, while a credit reduces the tax due generally by a percentage of the amount of the contribution. Where the income or profits tax system has a progressive rate structure, the value of a deduction rises as the income and tax rate rise, meaning greater incentive for wealthier taxpayers.

³¹ Law no. 7892, dated 21.12.1994 " On Sponsorship", amended

7. Reporting requirements for NPOs

The accounting and financial rules and regulations for NPOs are provided by the Accounting Law³², Law on Public Financial Inspection³³, Directive on Supervision from Tax Authorities in Support of Prevention of Money Laundry and Financing of Terrorism³⁴ and the Directive of the National Accounting Standard (NAS) for Non-Profit³⁵.

In order to unify financial reporting to NPOs, the National Accounting Council has adopted the “National Accounting Standard for Non-Profit Organisations” (NSI for NPOs). This Standard applies to the financial statements starting January 1st 2016. Accordingly, the financial statements of NPOs should include the following documents: Statement of Financial Position, Activity Overview, Cash Flow Statement and Explanatory Notes.

The Standard stipulates specifications on financial statements and reporting formats of NPOs, and presents different reporting requirements for NPOs based on their annual turnover. The Standard introduces simplified reporting requirements for organisations with annual revenues below five million ALL (approx. 37,000 EUR). These organisations are required to apply cash-based accounting and to prepare and submit only the statement of cash flow with explanatory notes on the type of activity or services provided.

According to the Law on Accounting, the fiscal year is the same as the calendar year. All account books, source documents and financial statements should be stored for a period of 10 years based on the Law on Accounting, while as regard to the Law 9920 “On Tax Procedures” the financial documentation should be stored for 5 years.

While the NSI for NPOs have created facilities for NPOs with regards to reporting, problem remains its implementation by tax inspectors that are not aware or have the right information on tax treatment and reporting requirements for NPOs.

[*Recommendations:*]

- Capacity building programs for tax inspectors to be developed. Specific guidelines and manuals reflecting all changes in the legal framework on fiscal treatment of NPOs, including financial reporting and accounting rules to be prepared and shared with tax officials in all the regional tax directorates.

³² Law no. 9228, dated 29.04.2004 “On Accounting and Financial Statements”

³³ Law no. 112/2015, date 15.10.2015 “For Public Financial Inspections”, Official Gazette 186/2015

³⁴ Directive no 22, date 19.11.2014 “For the Supervision of CSOs from Tax Authorities in Support to Prevention of Money Laundry and Financing of Terrorism”.

³⁵ Directive no 62, date 17.09.2015 “For the Announcement of the National Accounting Standards for Non – Profit Organisation and for its Mandatory Application” issued by the Ministry of Finance, Official Gazette 171/2015

8. Liabilities of NPOs to tax authorities

In general, the rules applicable to NPOs and are not considered relevant to their nature and type of activity, complex and difficult to understand. As a result, in particular small and newly established NPOs find it difficult to comply.

In case of failure to meet the legal deadlines for the submission of tax declaration and payment of taxes for which the entity is liable, sanctions are generated automatically by the tax system according to the Law no. 9920, dated 19.05.2008 "On Tax Procedures in the Republic of Albania". Some sanctions applied to NPOs are as follows:

- **For late filing**, the NPO shall be penalized with 10,000 ALL (75 EUR) for each tax declaration. For late payment with a tax liability, a penalty of 0.06% of the amount of unpaid debt is payable on a daily basis during which payment has not been made. The filing of an incorrect tax declaration is punishable by a fine equal to 0.06 percent of the amount of unpaid debt on a daily basis during which payment has not been made. Penalties for late payment and incorrect disclosure are calculated for a period of up to 365 calendar days.

- **Hiding or avoiding the payment of tax liabilities** constitutes tax evasion and is punishable by a fine equal to 100 percent of the difference in the amount accrued from what it should actually be.

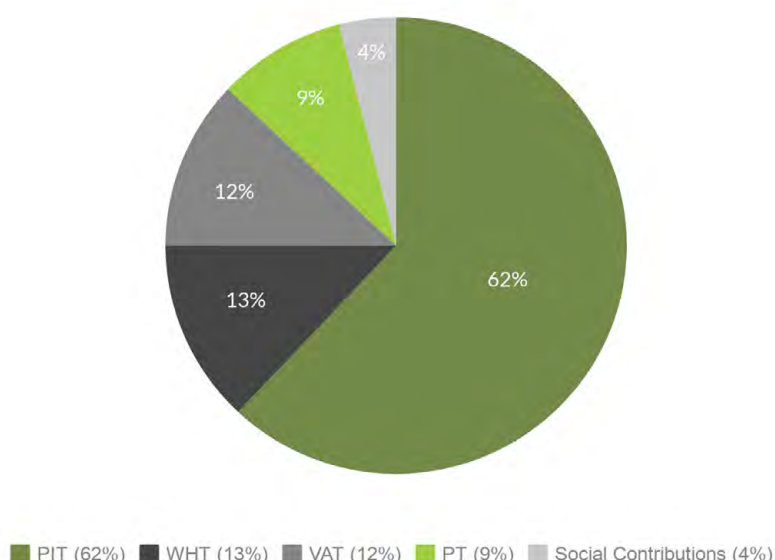
According to the official data from the Tax Administration, the total outstanding liabilities of NPOs as of March 2018 are 248,048,489 ALL (2 million EUR), out of which:

- a) 122,841,848 ALL are from tax obligation (VAT, PT, WHT and Social contributions, etc.).
- b) 125,206,641 ALL are from fines, penalties and interests.

Even here, it should be taken into consideration the fact that data from the Tax Administration are not accurate, due to the mixing of NPOs with other entities in their registers, as universities, political parties, etc. So, the amounts presented above may come from all these types of entities, and it is impossible to provide information only for NPOs, as defined by the law on NPOs.

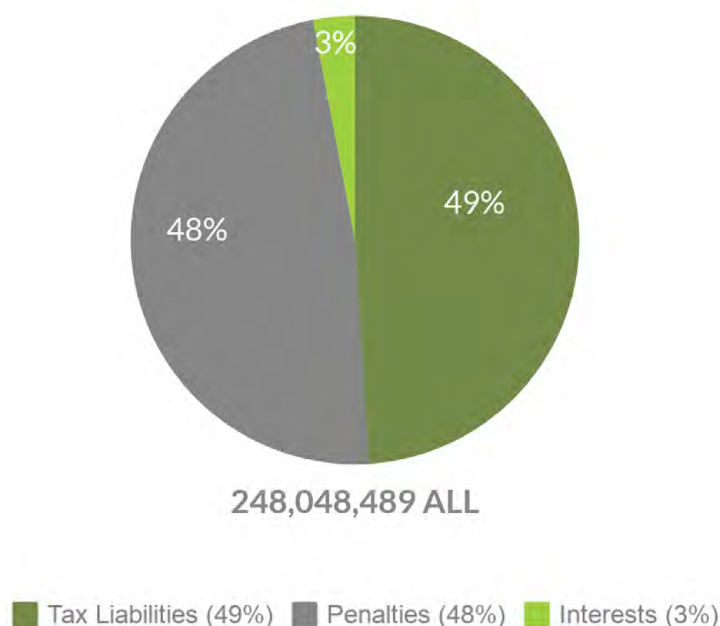
Graph no.7

Liabilities by Type of Tax



Graph no.8

NPOs Liabilities toward Tax Administration



The right to administratively appeal decisions to a superior complaint/appeal body is formally and legally³⁶ guaranteed. In case an organisation considers unjust a decision from the tax authorities, it must officially appeal the administrative act within 30 days after receiving it to the Tax Appeal Directorate that functions under the Ministry of Finances and Economy since January 2017. NPOs, same as business entities, must fulfill the preconditions stipulated in the Law on tax procedures when appealing a decision of tax authorities. The main condition is the obligation to **prepay the total amount of the tax assessed** by the regional directorate in the administrative act before the appeal, or to **have a bank guarantee** covering all the liabilities and interests. Fines and penalties may not be prepaid or secured by a bank guarantee. Tax Appeal Directorate has the right to refuse reviewing the appeal, if this condition is not fulfilled. This condition is difficult and in most cases almost impossible to be fulfilled by NPOs considering their budgets, thus preventing them from exercising the right to appeal.

[Recommendations:]

- Due to lack of financial means by NPOs to prepay the penalties imposed by tax authorities considering their non-profit nature, and very low chances that any bank will ever issue a guarantee to a non for profit organisation, revision of the preconditions for NPOs to appeal a decision of tax authorities is needed. Facilitating the procedure would allow for more appeals by NPOs and would provide for more clarity on the perception of arbitrary liabilities and fines imposed by tax officials to NPOs.

³⁶ - Articles 106 to 110 Law no.9920, dated 19.05.2008, "On Tax Procedures in the Republic of Albania"

-The Guidance of the Minister of Finance no. 24 dated 02.09.2008 "On Tax Procedures in the Republic of Albania" from paragraph 106 to paragraph 110

9. Fiscal inspections on NPOs

9.1. Operational audit inspections

Non - profit organisations are subject to “*operational audit inspections*” by tax authorities for the tax liabilities they are required to pay (personal income tax, social and health contributions, withholding tax, or other taxes applied by the legislation in force). Based on the changes introduced in 2016 in the law on tax procedures³⁷, the taxpayers must be notified at least 30 days prior to the starting of a comprehensive audit, and about 10 days prior to a short fiscal verification.

New ways of risk analysis have been also developed in the GDT since 2015. The implementation of the new IT system, has improved the selection of the taxpayers for audits, which is now risk based and calculated centrally by a designated tool in the Tax Authorities headquarters by analyzing all the information gathered from the tax declaration of the taxpayers.

Based on the information from GDT, a total number of 14 NPOs have been subject of comprehensive audit in the period 2016 – 2017. But, considering that the electronic register administered by the GDT for non-profit organisations is not accurate, the risk analysis and its results for the sector may not be accurate and the number provided may include other types of entities than NPOs. No information on the results of these audits has been provided by DGT.

9.2. Anti - Money Laundering and Financing of Terrorism inspections³⁸

This is another form of inspection conducted by Tax Authority investigation unit in cooperation with regional tax officials. In accordance with the respective legal requirements, tax officials have the right to:

A) Review the NPOs financial statements, analyze, and keep a special register on: a) Sources of funding, b) Economic activity of the NPO, (if it is applicable), c) Use of funds (transactions, documentation) and d) NPO' assets and the source of their creation.

B) Conduct a full audit³⁹, when is categorized “high risky” that includes: (1) Identification of sources of funding, agreements on grants received, donations agreements, documentation of membership fees; (2) Verification of whether the NPO carry out economic activity and if it generates income from this activity; (3) Verification of the bank account where the donations/funds are transferred; (4) Verification of whether the funds of non-profit organisations are held in bank accounts and whether the transfer or financial transactions related to these funds are carried out through the banking system, in accordance with the provisions of the legislation in force; (5) Perform duties by the highest decision-making body⁴⁰; 6. Verification if funds are used in line with the purpose of the actions and 7. If non-profit organisations that carry out economic activity and making profits from this activity, are using them for the fulfillment of the goals set out in the statute and the establishment act.

During consultations with NPOs, they have reported to have been subject of frequent audits by tax officials due to the campaigns initiated by the government during 2016 and 2017 against informality. These audits often resulted in considerable fines for organisations, mostly as a result of lack of information of tax officials on NPOs operation. While NPOs agree that the behavior and communication with tax officials has improved slightly, still there are some persisting problematic issues as follows:

³⁷ Changes on Law no 9920, “On Tax Procedures “ enacted on November 2016 with Law no. 112/2016
Link: <https://www.tatime.gov.al/c/6/69/procedurat-tatimore>

³⁸ According to the guidelines of the Minister of Finance No. 22, dated 19.11.2014 “On Inspection of NPOs by Tax Authorities in the Function of Prevention of Money Laundering and Financing of Terrorism”, article 7, “Control of Financial Statements “,

³⁹ Article 8, “Operational Audit of NPOs”,

⁴⁰ Article 20 of law no. 8788, dated 7.5.2001 “On Non-Profit Organisations”

- Tax officials provide different interpretations for the same laws and procedures in different regional tax offices;
- Frequent changes of the staff in the tax offices, lack of specific trainings and dedicated staff on non-profit sector within the regional tax offices, has impacted directly the activity of the NPOs all over the country making it difficult to understand and comply;
- There is no specific manual in place for tax inspectors related to the audits of the non-profit sector, as a result there is a lack of understanding the specific nature and related legal framework of the sector by tax inspectors.

[*Recommendations:*]

- Capacity building programs for tax inspectors and the sector to be developed. Coordination group with NPO representatives and tax authorities/line ministries to be established and joint trainings of the sector and Tax officials on fiscal matters to be offered.

Annex 1. Regional practices⁴¹ on VAT treatment for IPA projects

Kosovo:

In Kosovo⁴², organisations, which are involved in performing VAT exempted supplying, such as projects funded by the EC, and as foreseen in the IPA agreement, have the right to the reimbursement of VAT paid on purchases on a monthly basis regardless of the amount of these assets.

Organisations established in an EU Member State or in any country that are also parties to the IPA-funded projects (co-applicants), are not required to register for business purposes in Kosovo, based on Article 26, paragraph 2, point d, of the IPA Agreement for supplies that are directly funded by EU funds.

Bosnia and Herzegovina:

Supply of goods and services in Bosnia and Herzegovina within the projects funded by the European Commission through IPA are exempted from payment of VAT⁴³.

Contractors, which are IPA funded, will receive a unique Certificate control number from the European Union Delegation in BiH. A copy of the Certificate of VAT exemption is issued by the EUD in BiH, which is valid for the entire duration of the project, and also goes to the supplier/provider (through the EUD office). Each Invoice should contain the control number of the Certificate of VAT exemption.

Serbia:

National and Multi-beneficiary IPA-funded Projects are eligible for VAT exemption⁴⁴ in Serbia. Both Lead Applicants and project Partners are eligible from VAT exemption for EU-funded projects upon submission of the required documents within the legislation.

In Serbia, VAT exemption procedure for an EU-funded Project is quite simple:

The organisation submits the grant contract with the EU Commission to the EU Delegation in Serbia. (In the case of projects implemented in more than one country, the documentation needs to be sent to the EUD of each project partner country). Based on that, the EUD will deliver a list of new projects, organisations and all project contracts to the Tax Administration office once a month, on the fifth day of the month. Delegation of the European Union to the Republic of Serbia is responsible for creating and updating a list of projects and delivering the VAT Administration in the EU Delegation in Serbia.

The copy of the Project Contract, the list of names of persons responsible for submitting the VAT documentation, and the Specimen of Signatures of persons responsible for signing the VAT exemption forms should only be provided only at first- to the Tax Administration, meanwhile the copy of the Project Contract will be sent on the organisation's behalf by the EU Delegation and the VAT exemption procedure ends here.

⁴¹ Guidelines on VAT Exemption Procedures for EU Funded Projects in the IPA Countries – January 2016

⁴² <http://www.atk-ks.org/wp-content/uploads/2017/08/Rregullore-e-Brendshme-per-Procedurat-e-rimbursimit-te-TVSH-se2c-TAP-dhe-TAK-1.pdf>

⁴³ <http://www.uino.gov.ba/download/Dokumenti/Dokumenti/eng/Porezi/PDV/Instruction%20IPA.pdf>

⁴⁴ <http://www.poreskauprava.gov.rs/en.html>

