Tax Alert

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Contacts:

Loreta Peçi
Country Managing Partner
Albania & Kosovo
E-mail: loreta.peci@pwc.com

Gresë Rexhepi
Manager
Tel: +386 49 714 666
E-mail: grese.rexhepi@pwc.com

Str. Mujo Ulqinaku, No. 5,
Apt. 10, 5th floor
Qyteza Pejton
Prishtinë, Kosovo
Tel: +381 (0) 38 722 555
www.pwc.com/ks

In this publication, we cover recent tax developments in Kosovo on transfer pricing reporting requirements for FY2016, new Double Tax Treaties signed by the Republic of Kosovo, new tax refund procedures, a public ruling on the application of VAT reverse charge mechanism, and online VAT registration.

1. Transfer Pricing Reporting Requirement for FY2016

Following the entry into force of Administrative Instruction 2/2017 on Transfer Pricing, Tax Administration of Kosovo (TAK) has recently published a notice requesting taxpayers to submit the "Annual Controlled Transactions Notice" for FY2016 by November 30th, 2017. The format of this Notice has been made available by TAK and must be completed and submitted to TAK HQ – Transfer Pricing Office within the above deadline.

2. Kosovo ratifies new Double Tax Treaties

The President of the Republic of Kosovo has ratified three double tax treaties (DTT) in recent months. These include agreements on the avoidance of double taxation with the Swiss Confederation (Aug 2017), the Republic of Croatia (May 2017), and the United Arab Emirates (Oct 2016). The above DTTs will enter into force once ratification procedures are completed by each of the signatory countries respectively.

Kosovo is currently in the process of negotiating double tax treaties with the Republic of Ireland and the Kingdom of Luxembourg.

2.1. Switzerland

Permanent establishment: The DTT between Kosovo and Switzerland provides that building or construction sites constitute a permanent establishment only if they last for more than 12 months.

Dividends: Dividends may be taxed both in the state of residence of the recipient and in the state of source. In the case of the latter, the tax charged shall not exceed 5% if the resident holds at least 25% of the shares of the company for 365 days, and 15% in all other cases. Exemptions apply if the beneficiary is a pension fund or the central bank.

Interest: Interest may be taxed both in the state of residence of the recipient and in the state of source. In the case of the latter, the tax charged shall not exceed 5%. In certain circumstances interest may be subject to taxation only in the state of residence of the recipient.

Royalties: Royalties are taxed only in the state of residence of the recipient.

The method for the elimination of double taxation differs between the countries. Kosovo will apply the credit method; whereas Switzerland may apply either the credit or exemption method depending on the type of income.

2.2. Croatia

Permanent establishment: The DTT between Kosovo and Croatia provides that building or construction sites constitute a permanent establishment only if they last for more than 12 months.

Dividends: Dividends may be taxed both in the state of residence of the recipient and in the state of source. In the case of the latter, the tax charged shall not exceed 5% if the resident holds at least 25% of the shares of the company, and 10% in all other cases.

Interest: Interest may be taxed both in the state of residence of the recipient and in the state of source. In the case of the latter, the tax charged shall not exceed 5%.

Royalties: Royalties may be taxed both in the state of residence of the recipient and in the state of source. In the case of the latter, the tax charged shall not exceed 5%.

Both Kosovo and Croatia shall apply the credit method to eliminate double taxation.

2.3. United Arab Emirates

Permanent establishment: The DTT between Kosovo and UAE provides that building or construction sites constitute a permanent establishment only if they last for more than 6 months. Furthermore, the furnishing of services through employees or personnel will constitute a permanent establishment if such activities last for a period or periods exceeding 6 months.

Dividends: Dividends may be taxed both in the state of residence of the recipient and in the state of source. In the case of the latter, the tax charged shall not exceed 5%. Exemptions apply where the recipients are government institutions.

Interest: Interest may be taxed both in the state of residence of the recipient and in the state of source. In the case of the latter, the tax charged shall not exceed 5%. Exemptions apply where the recipients are government institutions.

Royalties: Royalties are taxed only in the state of residence of the recipient.

Both countries shall apply the credit method for the elimination of double taxation.

3. *Internal Document on Tax Refund Procedures*

In February 2017, TAK issued an internal document outlining a new tax refund process and procedure. Although tax laws determine the period to make a decision on refund requests at 60 days, TAK has decided to reduce this period to a maximum of 30 days.

The new rules categorize taxpayers into three groups depending on their tax compliance history.

Category A includes taxpayers who have a good history of tax compliance. This category includes taxpayers who have submitted all tax declarations (and have not subsequently corrected them) for the period under review, paid all due taxes on time, and have had previous refund requests approved successfully.

Refund requests for such taxpayers shall be fast-tracked, whereby information provided by them is verified but a tax audit is not initiated. The time taken to review Category A refund requests will be maximum 7 calendar days.

Category B includes taxpayers who have a less favourable tax compliance history. Refund requests for this category shall be reviewed in the following manner:

a) If tax officials, by way of verification of data and evidence, assess that the refund request is reliable and the initiation of a tax audit procedure is not necessary, they may recommend fast-tracking the refund process to a maximum duration of 7 calendar days;

b) If tax officials, by way of verification of data and evidence, assess that they must be cross-checked by third parties, they may recommend an initiation of a tax audit procedure. Such procedure shall in any case not exceed 20 calendar days.

Category C includes all other taxpayers, including those who have submitted their first refund request. The duration of the refund request review and tax audit shall in any case not exceed 30 calendar days.

4. *Public Ruling on the Application of the VAT Reverse Charge Mechanism*

In August 2017, Tax Administration of Kosovo (TAK) published a Public Explanatory Decision on the Application of the VAT Reverse Charge Mechanism for Non-Domestic Purchases, with reference to the ECJ rulings C-95/07 and C-96/07 in respect of the time limitation for VAT deduction.

In this Public Ruling, TAK has stated that it will not assess VAT liabilities in cases where the reverse charge is not applied correctly and the time limitation for the deduction of input VAT has expired. It has, however, distinguished between two cases:

1) Where a taxpayer has incorrectly reported purchases subject to reverse charge in their VAT books, and as a result has not applied the reverse charge mechanism, they will only be subject to administrative

penalties while the right of VAT deduction for reverse charge purchases can be exercised regardless of the 2-year limitation provided in the VAT law. In such cases, TAK will assess both output & input VAT and there will be no VAT liability borne (only fines for VAT non-compliance/misreporting).

2) On the other hand, where a taxpayer has not reported such purchases in their VAT books, and as a result has not applied the reverse charge mechanism, they will not only be subject to administrative penalties, but will also lose of the right of deduction if the time limitation has expired. As a result, in cases where the purchases subject to reverse charge are not reported in the VAT books at all, the right to deduct is limited as per the VAT law whereas output VAT can still be assessed by tax authorities, thereby resulting in VAT liabilities.

5. Online VAT registration

TAK has announced that starting from 28 September 2017, taxpayers can register for VAT and generate their VAT number electronically through the online tax reporting platform (EDI). They will be notified electronically upon the completion of the VAT registration procedure, and will be able to collect the physical copy of their VAT certificate at local TAK offices.

How can we help?

PwC is the leading provider of tax services worldwide both in terms of the size and scope of our tax practice and our reputation.

Clients engage us because we combine a strong understanding of their business and economic environments with specialist tax knowledge in hundreds of national and local jurisdictions across the globe.

As tax codes become increasingly complex and tax planning more controversial, we help companies to:

- identify and reduce tax risks,
- understand and meet their compliance obligations,
- implement tax strategies that complement their business and operational objectives,
- resolve disagreements with tax authorities when they arise, and
- manage tax accounting and reporting issues and design of best in class tax functions

PwC Kosovo draws upon its local tax knowledge and experience, together with the know-how and expertise of its global and regional network, to provide clients with comprehensive tax services across industries.

For more detailed information regarding these legislative changes and how PwC can help you comply with tax rules in Kosovo, please contact us to discuss further.

This Tax Newsflash publication has been prepared by PwC Kosovo's Tax and Legal Department.