

TAX AND FISCAL REGIMES: INCENTIVES FOR BUSINESSES

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Doing Business: Key Factors

- Infrastructure
- Permitting (New Law on Licenses and Permits Effective June 2016)
- Taxation
- Applicable Law and Courts (Enforcement)

Azerbaijani Taxes

- Overview
 - Tax Code
 - Special Tax Regimes
 - Commercial Agreements Approved into Law
 - Promotion of Exports
 - “Post-Oil” Era
 - Role of Taxes in Azerbaijani Economy
- Double Taxation Avoidance and Other Tax Treaties
 - Status
 - Preferences Granted
 - Summary
- Trade in Goods
 - Forms of Foreign Supplies in Azerbaijan
 - Taxable Permanent Establishments
 - Sales Structures
 - Commissionaire Structure
 - VAT

Tax Code

- Tax Code effective 2001
- Post 2001: substantive refining tax system
- Adoption of 2005-2007 State Program for Improvement of Tax Administration: emphasis shifts on streamlining tax compliance and control procedures
- Improvements continue as part of e-government formation program and initiative
- “Post-Oil” Era

Tax Code

- State, Autonomous Republic, and Local Taxes
- All taxes are those listed in Tax Code
- Profits Tax (CIT, Corporate Income Tax) – 20%
- Individual Income Tax – progressive taxation, three brackets: 0%, 14%, and 25%
- VAT – 18% or 0% (or exemption)
- Withholding Taxes (mostly, 10%)
- Excise Tax
- Simplified Tax (4% or 2% on gross proceeds)
- Subsoil Use Taxes/Mining Tax
- Property Tax – 1% (if paid by entities)
- Land Tax
- Highway Tax
- Social Security Charge – 22% payable by employer, 3% payable by employee

Tax Code Taxes

- Profits Tax
 - Azerbaijani entities (residents) are subject to tax on worldwide income
 - foreign entities operating in Azerbaijan are subject to tax on profits earned through their PEs in Azerbaijan
 - tax base for residents and PEs is gross annual income less allowable deductions
 - aggregate income of resident taxpayer includes all income irrespective of source, income of nonresident taxpayer consists only of Azerbaijani source income

Tax Code Taxes (Cont'd)

- Personal Income Tax
 - residents are obliged to pay income tax on worldwide income, nonresidents are taxed only on income originating from sources in Azerbaijan
- VAT
 - imposed on turnover of most goods, work, and services and importation
 - charged by seller of goods, provider of services or, in case of imported goods, by customs
 - input VAT representing business expense can be offset against output VAT collectable by business

Tax Code Taxes (Cont'd)

- Withholding Taxes
 - branch remittance at 10% tax applies to net profits remitted outside Azerbaijan by PEs of nonresidents (therefore, bringing overall effective rate of taxation of nonresidents to 28%)
 - personal income tax discussed above can be withheld from income payable to individuals by persons who are required to withhold (principally, employers)
 - dividends paid by resident enterprises and interest payable by resident or PE or on behalf of PE
- Excise
 - imposed on consumption basis and is applied upon departure of excisable goods from production sites or from importation of excisable goods
 - rates vary according to goods produced or imported and are subject to frequent changes
 - excise paid for goods used for production of other excisable goods can be offset against excise charged for finished products; alternatively, such excise can be reclaimed from state budget
 - export of excisable goods is subject to rate of 0%

Tax Code Taxes (Cont'd)

- Simplified Tax
 - enterprises not required to register for VAT
- Subsoil Use Taxes
 - entities engaged in extraction of subsoil resources
 - rate on mineral extracted
 - additionally (or, in some cases, alternatively), subsoil users are subject to various payments, including bonuses and fees, method of calculation and application of which are stipulated by contract with resource-owner

Tax Code Taxes (Cont'd)

- Property Tax
 - assessed annually on book value of fixed assets maintained by resident or nonresident enterprises
 - also payable by resident and nonresident individuals owning properties in Azerbaijan
- Land Tax
 - imposed on owners and users of land in an amount dependent on location, quality, and size of plot
 - payable by resident and nonresident individuals, and resident and nonresident enterprises
- Highway Tax
 - imposed on vehicles operated by nonresidents entering Azerbaijan for transportation of passengers and cargo and departing it as well as gasoline, diesel fuel, and liquid gas produced in Azerbaijan for internal consumption (wholesales) and imported into Azerbaijan

Taxes

- Social Tax (Charge)
 - employers make contributions to State Social Protection Fund with respect to salaries and other qualifying income of their employees (including, as of 2006, foreign employees)
 - based on qualifying gross income amount

Special Tax Regimes

- Commercial Agreements Approved into Law
- PSAs (most notably, in oil and gas) and Host Government Agreements
 - exemptions differ between contractors and subcontractors:
 - contractors are subject to:
 - the profits tax
 - profits tax is typically included in government's take of profit oil
 - bonus payments
 - acreage fees
 - subcontractors (except under major pipeline agreements) are subject to:
 - the withholding tax
 - VAT at 0%
 - only resident employees are subject to income tax

Special Tax Regimes

- Export of Oil and Gas infrastructure
 - Azerbaijani businesses have an option to be taxed under 5% tax on gross proceeds with no withholding taxes applicable to dividends, interest, or PE net profit, exempt from property and land taxes
 - as with other exports from Azerbaijan, export of oil and gas infrastructure from Azerbaijan is subject to VAT at 0%
- Agriculture
 - income of individuals is exempt from personal income tax
 - termed exemption (2014 through 2018) to agricultural sector from profits tax, simplified tax, VAT, and property tax
 - reduced rate of social charge applies to personal income from agriculture

“Post-Oil” Era

- Generally, End of 2014 – Beginning 2015
 - increase of threshold for mandatory VAT registration
 - VAT-free imports of fixed assets objects of [financial] leasing agreement
 - increase of mining tax rates
 - extension of tax base of individuals disposing of assets
 - incentives include extension of exemptions to residents of industrial parks from customs duties and VAT for all their imports (as opposed to previous exemptions applicable to certain imports (e.g., technologies)) for 5-year period with effect from 1 May 2016
 - starting May 2016, any supplies by contractors and subcontractors directly engaged in activities in industrial parks are subject to VAT at 0% for five years

“Post-Oil” Era (Cont’d)

- foreigners engaged by residents and their immediate contractors and subcontractors in activities in industrial parks are excluded from persons covered by mandatory state social insurance for term of 5 years starting also 1 May 2016
- income of resident legal entities is exempt from profits (corporate income) tax for seven years after registration in industrial and technological park
- import of technological equipment and installations with production purpose is exempt from VAT for seven years after registration in industrial and technological park
- resident legal entities are exempt from property and land taxes for seven years after registration in industrial and technological park

“Post-Oil” Era (Cont’d)

- Instructive Order No 2257, dated 4 August 2016, of President approved guidelines for reforms of taxation during 2016
 - “tax free” system introduced in July 2016 at airports will be implemented at other border checkpoints
 - rules of advance tax determination (“advance tax ruling”) planned to be implemented
 - implementation of “whistleblow” (“public awareness to prevent cases of tax evasion”) mechanism: persons informing tax authorities of tax evaders to be awarded
 - implementation of system of “voluntary tax disclosure”: no additional measures, interest, or financial sanctions are implemented against taxpayers who voluntarily inform tax authorities of cases of tax evasion

“Post-Oil” Era (Cont’d)

- agricultural production separated from sale (whereas Decree suggested differentiating production from processing)
- simplification of procedures for administration of international treaties on avoidance of double taxation
- expanding base of taxation to digital economy
- implementation of electronic invoicing system
- conclusion of intergovernmental agreements for automatic exchange of financial information
- implementation of “common reporting standard” (CRS): Azerbaijan is now signatory of Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information (CRS MCAA) (first exchange of information by Azerbaijan pursuant to it is due by September 2018)

Role of Taxes in Economy, 2017

- Share of taxes in GDP: 7.3% (compare to countries where tax revenues are as high as 60% or OECD “unweighted” average of roughly 34%; however, average tax burden in oil-producing countries can be as low as 1%)
- Share of taxes in budget revenues: 58.9% (41.1% out of non-tax sources)
 - VAT accounted for 22.9%
 - profits (corporate income) tax for 14.9%
 - personal income tax for 6.5%
 - excise for 3.8%
 - remaining taxes for 10.8%

Share of Sectors in GDP, 2017

- Oil: 37.2%
- Non-Oil: 62.8%
- Added Value:
 - industry: 40.1% (69.9% extractive industry)
 - trade: 10.4%
 - agriculture, forestry, fishery: 5.6%
 - placement of tourists and public catering: 2.3%

Role of Taxes in Economy, 2014

- Share of taxes in GDP: 7.3%
- Share of taxes in budget revenues: 45.2% (54.8% out of non-tax sources)
 - VAT accounted for 16.3%
 - profits (corporate income) tax for 12.9%
 - personal income tax for 5.1%
 - excise for 4.4%
 - taxes in relation to foreign trade for 3.8%
 - remaining taxes for 2.7%

Share of Sectors in GDP, 2014

- Oil: 39.1%
- Non-Oil: 60.9%
- Added Value:
 - industry: 41.5% (69.6% extractive industry)
 - trade and paid services: 9.9%
 - agriculture: 5.3%
 - placement of tourists and public catering: ?

Role of Taxes in Economy, 2012

- Share of taxes in GDP: 6.2%
- Share of taxes in budget revenues: 41% (59% out of non-tax sources)
 - VAT accounted for 13.6%
 - profits (corporate income) tax for 13.7%
 - personal income tax for 4.7%
 - excise for 3.1%
 - taxes in relation to foreign trade for 3.5%
 - remaining taxes for 2.4%

Share of Sectors in GDP, 2012

- Oil: 47.3%
- Non-Oil: 52.7%
- Added Value:
 - industry: 50%
 - trade and paid services: 8.4%
 - agriculture, hunting, forestry: 5.2%
 - placement of tourists and public catering: ?

Double Taxation Avoidance Treaties

- 47 Effective Treaties (40 in 2013)
- USSR Treaties Not Recognized Except Specifically Agreed
- Treaties with Most Popular “Onshore” Jurisdictions
- Treaty with UAE by Far Most Favorable
- Implementation Procedures
 - Advance Clearance
 - Refund

Double Taxation Avoidance Treaties

- Residents
- PE
- Exemption from Withholding Tax Except for
 - Dividends
 - Interest
 - Royalties
- Possibly, Exemption from Branch Profits Tax
- Procedural Matters

Other Agreements

- Tax Compliance Cooperation and Mutual Assistance Agreements (also, multilateral within CIS)
- Agreement on Cooperation and Information Exchange in Combatting Tax Evasion
- Agreements on Principles of Indirect Taxation upon Export and Import of Goods (Works and Services)/Bilateral Trade
- Cooperation Agreement between Tax Authorities

Trade in Goods

- Forms of Foreign Supplies in Azerbaijan
 - No Presence
 - Presence through Intermediaries (Dealerships and Similar), Various Sales Structures
 - Commissionaire Structure – Ownership Remains with Principal
 - For VAT Purposes, Owner is Commissionaire – Removes Complexities where Principal is Non-Resident
 - “Self”-Presence – PE
 - Full Presence – Subsidiary

Questions & Comments?

Thank you!