

### **TAX DEVELOPMENTS**

Law No 1356-VQD, dated 30 November 2018, introducing amendments to the Tax Code of the Republic of Azerbaijan is passed. The Law, coming into effect 1 January 2019, makes substantial revisions to the Tax Code:

#### **SMEs and Start-ups**

A new concept introduced into the Code concerns definitions of an SME cluster company and SME cluster participant. An SME cluster company is a legal entity that, having met the criteria established by the Ministry of Taxes, obtained from the Agency of the Republic of Azerbaijan for Developing Small and Medium Enterprise a certificate of an SME cluster company. A participant of an SME cluster is an entity or individual that entered with an SME cluster company into an agreement to operate in an SME cluster and obtained from the Agency for Developing Small and Medium Enterprise a certificate of an SME cluster participant.

From the time of having been entered into an SME cluster company register, SME cluster companies enjoy exemptions for seven years (i) from the profits tax of a portion of revenues from a supply of goods (work and services) in an SME cluster operations directed for capital expenditure, (ii) from the property tax for assets used in the cluster operations, (iii) from the land tax for land used in a cluster operation, and (iv) from the VAT upon importation of production and processing plant, technological equipment, and machinery. Some of these are available to SME cluster participants.

Another novelty concerns introduction of a Start-up certificate. A start-up is a business activity of persons run on the basis on an innovation meeting the requirements to be determined by the Cabinet of Ministers and having been issued a Start-up certificate by the Agency for Developing Small and Medium Enterprise. Revenues from innovative operations of a subject of a micro- or small enterprise is exempt from the income or profits tax for three years from the date of obtaining the Start-up certificate.

#### **Income and Profits Taxes, in Detail**

An amendment made to the Tax Code concerns tax amounts from a monthly income of employed individuals. Monthly income of individuals employed by taxpayers in a private sector not engaging in oil and gas shall for seven years starting 1 January 2019 be taxed in the following amounts:

<b>Monthly Income Amount</b>	<b>Tax Rate</b>
Up to 8,000 Manats	Zero per cent
Above 8,000 Manats	14 per cent of portion above 8,000 Manats

Before another amendment to the Tax Code, an annual income amount up to 30,000 Manats from a non-business activity was subject to the personal income tax rate at 14 per cent and 4,200 Manats and 25 per cent of the amount exceeding 30,000 Manats. Following the amendment, an annual income from a non-business activity is subject to the income tax at a flat rate of 14 per cent.

Upon disposition of interest/shares in an entity, the personal income tax amount is determined with reference to a net asset value of the entity. The same rule applies to the profits tax of a corporate seller.

Under a newly introduced amendment, the following income streams of individuals (in addition to exemptions for SMEs and Start-ups) are exempt from the income tax:

- the income tax amount of sole proprietors engaged in trading by retail sale of goods and/or public catering is reduced by 25 per cent for three years starting 1 January 2019 in relation to cashless proceeds through POS terminals;
- income received from a lawful cancellation of a tax debt (to the state budget);
- the first ten Manats of a cash prize of a lottery registered by an organ controlling financial markets;
- 50 per cent of income received by a taxpayer from a disposition of a participatory interest or share that the taxpayer held for at least three years;
- welfare assistance (support) paid by the Foundation for Propagating Moral Values;
- income received as a result of payments by borrowers of dues where a payment for a guaranteed loan is made by the Fund of Guaranteeing Hypothec and Credit;
- 75 per cent of income from business of sole proprietors subject of micro-business; and
- income of labourers engaged for public works by the Ministry of Labour and Social Protection of Populace.

### **Insurance**

Where a monthly income amount is up to 200 Manats, the compulsory state social insurance premia shall be paid in relation to private sector insurers not engaging in oil and gas at the rates of three per cent payable by (withheld from) employees and 22 per cent payable by the employer and, where monthly income amount is in excess of 200 Manats, at the rates of six Manats and ten per cent of an amount in excess of 200 Manats payable by (withheld from) the employee and 44 Manats and 15 per cent of an amount in excess of 200 Manats payable by the employer.

Starting 2019, insurers and reinsurers must file reports for insured (reinsured) fixed assets of business subjects with the Ministry of Taxes by the 20<sup>th</sup> of the month following a quarter.

### **Simplified Tax**

Pursuant to the amendments, the following can no longer be simplified taxpayers:

- persons engaged in production employing more than ten people;
- persons supplying goods in wholesale trading;
- persons supplying services except for services to persons (populace) not registered with a tax authority as taxpayers;
- persons selling gold, jewellery made of gold and goldware, as well as diamond (processed, sorted, cut, and hardened as well as not processed, sorted, cut, or hardened);
- persons engaged in sale of items made of fur and leather; and

- persons engaged in licensable activity except those engaged in construction and providing mandatory insurance services.

With the exception of activities above, the simplified tax is calculated at a single rate of two per cent applicable to the amount of revenues from the supply of goods, discharge of work, and provision of services as well as out-of-sale revenues of persons subject to this tax. Prior to the amendment, the simplified tax applied at the rate of two per cent where a business was run solely in the regions and four per cent applicable to businesses run in Baku.

### **Financial Sanctions**

New financial sanctions apply to violations of the tax law. A person, supplying goods without an electronic waybill or electronic tax invoice where the person should have issued such waybill or invoice, is subject to a financial sanction at ten per cent of the sale price of the supplied goods for the first, 20 per cent of the price for the second, and 40 per cent of the price for each subsequent violation during a calendar year.

Sale, storage with the purpose to sell, and release outside a production facility of goods subject to excise marks or mandatory marking without such excise mark or mandatory marking is subject to a financial sanction at one time the market value of the goods for the first and two times the value of the goods for each subsequent violation during a calendar year.

The following are considered excisable goods subject to the respective rates:

- alcoholic energetic drinks – 2 Manats per litre;
- non-alcoholic energetic drinks – 3 Manats per litre;
- cigars, including cut cigars – 1 Manat a piece; and
- liquid for electronic cigarettes – 20 Manats per litre.

Persons that obtained tax concessions and exemptions set out in the Tax Code are subject to a financial sanction at six per cent of the non-reported or reduced income (inclusive of expenses) for a failure to report or reducing a tax-exempt income.

Before these amendments to the Tax Code, allowing concealment (reduction) of income by employer employing individuals to discharge a work (perform services) without entering with them into an employment agreement (contract) in a manner required under the Labour Code, was subject to a financial sanction imposed on the employer at 1,000 Manats per an individual. Pursuant to the amendments, the sanction amount is doubled for the first, is 4,000 Manats for the second, and 6,000 Manats for each subsequent violation during a calendar year.

The following sanctions are imposed for having monetary funds of a taxpayer evade recordation during field tax audits and operative tax control, failing to record income and expenses in a manner required under the Tax Code, and failing to present any of the electronic waybill or electronic tax invoice and acts of purchase for goods in possession of a taxpayer and, in relation to imported goods, import customs declarations, and, where such goods are manufactured by the taxpayer, documents prepared based on the rules of tax accounting of income and expenses by the areas of economic operations:

- ten per cent of monetary funds in excess of 1,000 Manats for evading or failing to record funds in excess of 1,000 Manats; and
- 20 per cent of the part in excess of 1,000 Manats for a repeated violation during a calendar year.

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