

AMENDMENTS TO TAX CODE EFFECTIVE 2017

The legislature in Azerbaijan came up recently with extensive amendments to the Tax Code of the Republic of Azerbaijan that intend to enforce compliance with the tax laws (by augmenting/modifying sanctions and expanding powers of tax authorities), provide benefits concerning certain taxes on the one hand and increase some taxes on the other. The amendments are effective from 1 January 2017.

The amendments introduced numerous new terms to the Tax Code, amongst which are “income”, “transfer price”, “tax ruling”, “retail sale”, “wholesale”, “financial institution”, “electronic audit”, “tax preference”, and “tax avoidance scheme”.

The term “income”, which was absent in the Tax Code, has been introduced and covers the total value of operations in connection with the sale of goods, provision of services, and performance of works, as well as extraordinary (out-of-sale) gain.

One of the key amendments to the Tax Code is the introduction of “transfer price”. Before, the value of goods was determined based on the market price (*when the offered price was below more than 30 per cent of the market price*) or the actual sale price (*when the value was more than 30 per cent of the market price*). The concept of “transfer price” has been designated to apply to operations between certain persons when no information is available about the actual sale price from official or open sources.

These are the operations between (i) a resident of the Republic of Azerbaijan and non-residents who are related to the former; (ii) a non-resident or its representative office, branch or other department and the non-resident’s permanent establishment in the Republic of Azerbaijan; or (iii) a resident of the Republic of Azerbaijan or a permanent establishment of a non-resident in the Republic of Azerbaijan and subjects established in countries with preferential tax regimes.

Transfer price is used for the purposes of profits tax and applies to operations, the value of which exceeds AZN500,000. There are several methods to determine the transfer price, namely, a resale method, accrual method, viability method, and profits division method.

Newly-introduced Sub-Section 15.1.2-1 broadened the rights of taxpayers by entitling them to obtain tax rulings from the tax authorities. Although the concept of tax ruling has existed in practice for some time, its introduction to the Tax Code is new. Sub-Section 77-1 of the Tax Code sets the tax ruling procedure in more detail.

Pursuant to Sub-Section 77-1.1 of the Tax Code, a taxpayer has the right to submit an application to the tax authority for the purposes of determining the former’s tax obligations in advance. Tax ruling is issued with respect to each taxpayer and each taxable transaction and is binding for a three-year term. A tax ruling can be appealed to an upper body and court.

Another benefit conferred on taxpayers is the mitigation of tax burden (elimination of sanctions and penalty) in the case of a voluntary tax disclosure, *i.e.*, a voluntary declaration of a tax obligation not revealed to the tax authorities during an on-site tax audit. Such disclosure obligates the taxpayer to pay only the main tax and exempts him from the payment of the applicable sanctions/penalties.

In furtherance of the FATCA implementation, Sub-Sections 16.1.11-3, 16.1.11-4, 35.2-1, 36.7 and 76-1 have been added to the Tax Code imposing an obligation on financial institutions to present documents and

information about financial transactions to tax authorities and their officials upon their request in accordance with international treaties, to which the Republic of Azerbaijan is a party.

Sanctions for breaches of tax laws have been harshened. The amendments established financial sanctions with respect to taxpayers who breach the requirements of non-cash transactions. For the first-time breach, the sanction will be in the amount of ten per cent applicable to the transaction value in one calendar year. When the breach is repeated, the sanction doubles. For three or more breaches, the sanction amounting to 40 per cent applicable to the transaction value applies. Moreover, absence of an import tax return, invoice, or electronic invoice is subject to various sanctions depending on the amount of the tax evaded.

Sub-Section 71-1 introduced electronic invoices, which must be presented to individual entrepreneurs and legal entities by sellers of goods, provider of services, and performer of works. The form, application, registration and rules of usage of electronic invoices are determined by the Cabinet of Ministers of the Republic of Azerbaijan.

The amendments also touch upon the withholding tax (WHT), the value added tax (VAT), excise tax, and simplified tax.

Pursuant to Sub-Section 101.5 of the Tax Code, income from bets in connection with sport games, lotteries, as well as other contests is subject to a ten per cent tax after deducting the amount spent on participation. Besides this, the electronic trade is subject to the ten per cent WHT to be withheld by a local bank, branch of a foreign bank in the Republic of Azerbaijan, or a postal office.

The term of exemption from tax of income received from deposit payments, dividends, and discounts has been extended to seven years starting 1 January 2017.

Import and production of certain food products (wheat, bread) have been exempted from the VAT for the period of three years. To stimulate growth of agriculture, the VAT on the retail sale of agricultural products will be calculated from the trade margin (defined as difference between the retail sale price and price paid to supplier (the purchase price)).

Moreover, with the intention to restructure and rehabilitate the banks with low liquidity ratios, disposition of toxic assets will be exempt from the VAT starting from 1 January 2017 for the period of three years.

On the other hand, provision of services and performance of works electronically (with the exception of hotel services and services connected with ordering airline tickets) will be subject to the VAT.

The amendments touching upon the excise tax include the addition of leather products among the excisable goods and the increase of the rates of excises.

Finally, the newly-added Sub-Section 220.12 subjects legal entities and individual entrepreneurs to one per cent simplified tax for withdrawing cash from their bank accounts.

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