



Doing Business in Azerbaijan



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1 Country overview



According to the Constitution adopted on 12 November 1995, Azerbaijan is a democratic, secular, unitary republic based on the rule of law. The country is governed by the president, who is directly elected for a seven-year term by popular vote.

Currently, the President of Azerbaijan is Ilham Aliyev. The First Vice-President of Azerbaijan is appointed by and subordinate to the President. This position is currently held by Mehriban Aliyeva. The Government (Cabinet of Ministers) is subordinate to the President, who appoints the Prime Minister and other ministers subject to the approval of the legislature. The highest legislative body is the 125-member single-chamber parliament, known as Milli Majlis, which is elected for a five-year term by popular vote. Milli Majlis may not be dissolved by the President; however, the President is able to veto its decisions.

The Republic of Azerbaijan gained its independence from the Soviet Union in 1991. It joined 11 other former Soviet republics to form the Commonwealth of Independent States (CIS) in 1993.

General statistics*

Population	Approx. 10 million
Territory	86,600 square kilometers (approx. 33,400 sq. miles)
Neighboring countries	Russia, Iran, Armenia, Georgia, Turkmenistan, Kazakhstan, Turkey
Main ethnic group	Azerbaijani (91.6%)
Ethnic minorities	Russian, Lezghi, Talysh, Tatar
Capital	Baku (pop. 2,277,500)
Other populous cities	Gandja (pop. 334,00) Sumgait (pop. 343,100)
Autonomous Republic	Nakhchivan Autonomous Republic (pop. 456,100)

*Source: <https://www.stat.gov.az/>



2 Economy



Azerbaijan's vast oil reserves attract foreign investment into the country's economy. Several major oil contracts have been signed since 1994.

According to the 2019 Azerbaijani State Statistics Committee report, foreign investments in the oil & gas sector comprised 54% (US\$ 4,900.8 m) of all foreign investments.

Following the success of oil & gas projects, the Government declared a policy calling for the development of the non-oil sector. Owing to the rapid development of the non-oil sector, the share of oil & gas investments in total foreign investments has gradually decreased compared with earlier years.

On 26 May 2000, the President of Azerbaijan signed the Law on the Main Export Pipeline ("MEP"). The MEP, which connects Baku with the Turkish oil terminal in Ceyhan via Georgia, is the main route for the transportation of Azerbaijani crude to the world oil market. On 26 October 2001 Milli Majlis also passed a law ratifying the Agreement on the South Caucasus Pipeline ("SCP"). The SCP is the main route for the transportation of Azerbaijani gas to the world market. In particular, the SCP pipeline is used to ship natural gas from the offshore Shah-Deniz gas field to Turkey.

The country has one state-owned oil refinery. Large petrochemical and metallurgical plants are located in Sumgait, 28 kilometers from Baku.

In addition, there are 5 so-called industrial parks and 3 high-tech parks in Azerbaijan. These provide a 7-year tax holiday for entrepreneurs operating within these clusters.

The President of Azerbaijan signed a decree on additional measures to improve the business environment and strengthen the country's position in international rankings on 13 July 2016.

That decree set up a special body (Commission) tasked with generating proposals for the establishment of a favorable business environment, developing an appropriate legal and institutional framework and preparing an action plan to achieve the goals set.



3 Business overview



Licensing of entrepreneurial activity

The Law on Licenses and Permits, adopted on 15 March 2016, stipulates a “one-stop-shop” principle for issuing licenses. The Ministry of Economy of Azerbaijan maintains the Registry of Licenses and Permits.

It should also be noted that licenses to conduct business activity are normally granted for an indefinite term, save for specific exceptions.

Labor licensing requirements

Foreign employees are required to have individual work permits issued by the State Migration Service of Azerbaijan. The legislation prescribes severe penalties for employers that fail to obtain a work permit: AZN 3,000 to AZN 4,000 for executive officers and AZN 15,000 to AZN 20,000 for legal entities. The penalty increases to AZN 35,000 if the violation is committed in relation to three or more foreign employees. Heads and deputy heads of branches/representative offices of foreign companies and foreign entrepreneurs are exempt from the requirement to obtain work permits. The same rule applies to heads and deputy heads of legal entities established in Azerbaijan that have at least one foreign (corporate or individual) founder.

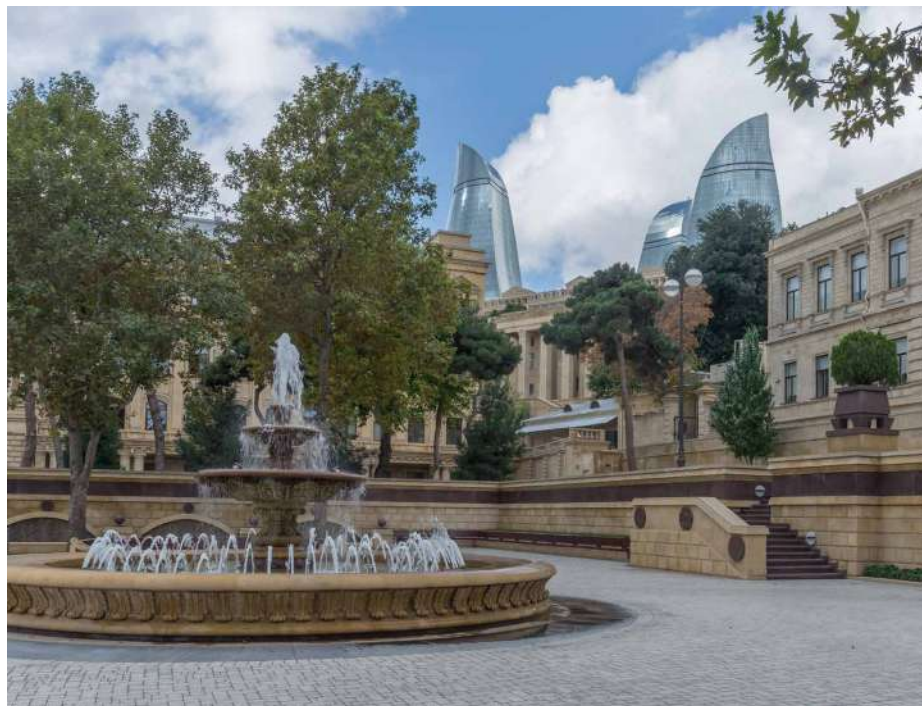
Furthermore, a foreigner or stateless person has the right to work in the Republic of Azerbaijan without obtaining a work permit provided that he/she is on a business trip in an area of business specifically permitted by the Cabinet of Ministers of Azerbaijan and the period of the business trip does not exceed a cumulative total of 90 days in a year.

Foreign citizens coming to Azerbaijan for more than fifteen days must register with the State Migration Service within fifteen days, based on an application made by the landlord (owner) of the premises where the visitor is residing.

Foreign citizens wishing to live in Azerbaijan are required to obtain a temporary residence permit before their

visas expire (those entering Azerbaijan under the non-visa regime must apply for a residence permit for stays of more than 30 days). Temporary residence and work permits are issued under the one-stop-shop principle. State duty for a temporary residence permit or for a work permit varies depending on the period of validity (e.g., AZN 120-160 for a one-year temporary residence permit and AZN 1,000-1,400 for a one-year work permit).

The employer must register the conclusion, amendment and termination of employment contracts electronically in the E-government web-based information system using an enhanced electronic signature to authenticate entries made.





Profit repatriation

Under the Law on the Protection of Foreign Investment (adopted on 15 January 1992) and the Law on Investment Activity (adopted on 13 January 1995) (collectively the “Foreign Investment Laws”), foreign investors are entitled to repatriate profit in convertible currency after the payment of all taxes and other fees that are due.

Currency regulations

The official currency of Azerbaijan is the Manat (AZN). Foreign companies and individuals may have both AZN and foreign currency accounts at local banks. All settlements within Azerbaijan, including the payment of salaries, must be made in AZN, save for certain specific exceptions.

Land ownership

Land ownership in Azerbaijan is governed by a set of legal acts, including the Law on Land Reform, the Law on the Land Market, the Civil Code of Azerbaijan and the Land Code. Azerbaijani citizens and legal entities are permitted to own land.

Foreign individuals and legal entities cannot acquire land in Azerbaijan, but they have the right to lease land. Foreign individuals and legal entities may purchase dwellings. In such instances, the land on which the acquired dwellings are situated is rented to those foreign individuals and legal entities.

Establishing a business

The Foreign Investment Laws provide the legal framework for foreign investment in Azerbaijan. They stipulate the types of entity foreign companies can invest in, the rules governing the repatriation of profit, and the general rights and guarantees provided to foreign investors. Foreigners can invest in a business venture in Azerbaijan in a number of ways, such as:

- ▶ Establishing a fully owned subsidiary;
- ▶ Acquiring shares in an existing company;
- ▶ Establishing a joint venture with Azerbaijani companies and individuals;
- ▶ Entering into other acceptable forms of investment agreement.

Various registration requirements apply to foreign companies establishing a business presence in Azerbaijan. A special license to conduct business is required for companies operating in telecommunications, sea and air transportation, insurance and other regulated industries. The Ministry of Taxes of Azerbaijan is charged with registering the business presence of commercial legal entities based on a one-stop-shop principle.

Types of business presence

The following forms of commercial legal entity exist in Azerbaijan:

- ▶ Open and closed joint-stock companies;
- ▶ Additional and limited liability companies;
- ▶ General and limited partnerships.

Foreign investors wishing to establish a presence in Azerbaijan may opt for any of the above forms. Foreign entities may also operate in Azerbaijan through a branch or a representative office.

Joint-stock companies (JSCs)

A JSC is governed by the Civil Code. A JSC is established by at least one legal entity or individual. The liability of a JSC shareholder is limited to the value of his shares. JSCs fall into two categories – “closed” and “open” JSCs. The shares of closed JSCs are not freely transferable and the company must have a minimum capital of AZN 2,000. The shares of open JSCs are not subject to the transfer restriction, but the company must have a minimum capital of AZN 4,000.

Limited liability companies (LLCs)

LLCs may be founded by one or more legal entities and/or individuals with the founding members having a participating interest in the LLC proportional to the amount paid into the charter capital. Each owner’s liability is limited to the amount invested in the LLC. LLCs do not issue shares.

A participating interest in an LLC is freely transferable to third parties.

Partnerships

General and limited partnerships are governed by the Civil Code. A general partnership is established by at least two legal entities or individual entrepreneurs with all partners having unlimited liability. A limited partnership is established by at least two legal entities and/or individual entrepreneurs with at least one partner having unlimited liability.

Branch or Representative Office

Foreign companies may operate in Azerbaijan without establishing a local legal entity if they instead register a branch or representative office with the Ministry of Taxes of Azerbaijan. Branches and representative offices are allowed to conduct commercial activities in Azerbaijan. The state duty for the registration of a branch or representative office is AZN 220.

Other forms of legal entity

As well as commercial entities, Azerbaijani legislation also provides for non-commercial legal entities and public legal entities.

A non-commercial legal entity is an entity that neither generates profit as its main purpose nor distributes profit among its members. Non-commercial legal entities may be created in the form of public associations, funds or unions of legal entities.

Public legal entities engage in activities of state and public significance. They may be founded by executive authorities designated by the President of Azerbaijan on behalf of the government or by municipal bodies on behalf of municipalities. They may also be founded by other public legal entities if the charters of the latter authorize this.

4 Taxation



Introduction

There are currently two separate and distinct tax regimes in operation in Azerbaijan. These are the statutory profit tax regime and the special tax regime. The latter is applicable in limited cases, in particular to oil & gas and mining companies operating under Production Sharing Agreements (“PSAs”) and/or Host Government Agreements (“HGAs”), as well as companies operating in special areas (e.g., ports and high-tech parks). The statutory (general) profit tax regime is applicable to all other entities operating in Azerbaijan.

Foreign companies that are deemed to have a permanent establishment (“PE”) in Azerbaijan are taxed on income derived from the commercial activities of the PE in the country. Foreign companies receiving income from Azerbaijani sources other than through a PE are subject to withholding tax on the amount of such income.

The PSA regime is a set of rules covering 20+ production-sharing agreements that have been ratified by the Milli Majlis. The PSA regime generally applies to all contractor parties under the PSAs and their direct and indirect foreign subcontractors. The HGA tax regime applies to entities working on the Baku-Tbilisi-Ceyhan oil export pipeline and the South Caucasus Pipeline. For a complete summary of the PSA and HGA regimes mentioned in this paragraph, please refer to our separate Azerbaijan oil & gas tax guide.

Statutory tax regime

The tax regime outlined below is based on the Tax Code enacted on 1 January 2001, as amended up to November 2019. The main taxes and payments affecting foreign investors operating under the statutory regime are as follows:

- ▶ Corporate profit tax;
- ▶ Personal income tax;
- ▶ Value added tax.

In addition to the above, the legislation envisages social fund contributions and other taxes and charges (e.g., excise tax, property tax, road tax and land tax).

Corporate Taxation

Profit tax

The following entities are subject to profit tax in Azerbaijan:

- ▶ Azerbaijani legal entities, with or without foreign ownership;
- ▶ Permanent establishments of foreign legal entities;
- ▶ Representative offices of foreign legal entities engaged in commercial activities in Azerbaijan;
- ▶ Non-commercial organizations deriving income from commercial activities.

Taxable profit includes trading profit, capital gains, profit from financial activities and other profit sources. Residents, including entities with foreign investments, are taxed on worldwide profit. Non-residents are taxed only on profit from business carried on in Azerbaijan.

Permanent Establishments (PEs)

The Tax Code defines a PE as a non-resident foreign legal entity or natural person that carries on commercial activities for no less than 90 cumulative days in any twelve-month period.

However, the Tax Code also provides that entities that carry on exclusively any or any combination of the following activities do not create a PE in Azerbaijan:

- ▶ The storage and display of goods;
- ▶ The storage of goods for processing by another entity and subsequent export from Azerbaijan;
- ▶ The purchase of goods for proprietary use and the collection of information;
- ▶ Any other preparatory or auxiliary activities for proprietary purposes.

Foreign companies that do not operate in Azerbaijan through a PE situated therein are subject to withholding tax (see below) on any taxable income received from Azerbaijani sources.

It should be noted that the provisions of double tax treaties (see the list of effective double tax treaties below) prevail over those in the Tax Code.

Tax rates

The general profit tax rate is 20%. An additional branch remittance tax of 10% applies to profit remittances from the branch to the head office. The taxable base is net profit after taxes.

Determination of taxable profit

Annual income disclosed in a company’s Azerbaijani statutory accounts is reduced by all business expenses except for those specifically disallowed by the Tax Code. The most significant items of non-deductible expenditures for tax purposes are:

- ▶ Depreciation and repair expenses in excess of the established limits (to be capitalized and expensed through depreciation);
- ▶ Entertainment, accommodation and meal expenses (except for meal expenses for the provision of “therapeutic nourishment”, milk and similar foodstuffs to employees, which are deductible up to certain limits);
- ▶ Business travel expenses in excess of the statutory limits.

Capital gains

There is no separate capital gains tax in Azerbaijan. Capital gains are subject to profit tax in Azerbaijan only when an asset is alienated. Gains arising from the disposal of assets are calculated as the difference between the sale price and the net book value of an asset (excluding VAT).

Gains arising from the alienation of shares or other participating interests in resident enterprises are also subject to general profit tax. Such gains are calculated as the difference between the actual sale price and the nominal value of sold shares if the shares/participating interests are sold for a price exceeding the proportional value of net assets of the company corresponding to the alienated shares/participating interest. If the sale price is lower than the proportional value of net assets, the gain is calculated as the difference between the proportional value of net assets as at the date of sale and the nominal value of the alienated shares.

50% of a taxpayer’s income from the sale of shares/participating interests owned by the taxpayer for at least 3 (three) years is exempt from profit tax.

Interest and dividends

Interest (except for interest on loans paid to local banks or non-resident banks with PEs in Azerbaijan) and dividend income received from Azerbaijani companies and PEs of foreign companies are subject to 10% withholding tax.

Depreciation charges

All assets with a net book value of more than AZN 500 and a useful life of more than one year must be capitalized and expensed through depreciation. The applicable depreciation rates depend on the category to which the assets belong. The following are the maximum depreciation rates by category for the most common groups of assets:

Type of assets	Rate of depreciation (%)
Capitalized land improvements and buildings	up to 7
Machinery and equipment	up to 20
High technology equipment	up to 25
Means of transport	up to 25
Livestock	up to 20
Intangibles	10 (for those with an indeterminate period of use)
All other assets	up to 20

Micro-enterprises are entitled to make depreciation deductions for fixed assets used in their entrepreneurial activities at 2x the depreciation rates shown above, while small enterprises may make deductions at 1.5x the rates shown above.

Depreciation rates are applied to the net book value of assets. Depreciation may be applied at a lower rate than the maximum rate. The balance resulting from using the lower rate may be claimed in future periods.

Losses and bad debts

Entities that have deductible expenses in excess of their annual income may carry the resulting losses forward for a period of up to five years and offset them against profits for those years without any limitation. Bad debts may be deducted from taxable income only if they are recognized as having no value

in the company's accounts and were reflected as income in previous periods. Losses and bad debts recovered in future periods are recognized as income in the period of their recovery.

Transfer pricing rules

The Regulations on the Calculation and Application of Transfer Prices ("Regulations") were adopted by the Ministry of Taxes in 2017. They are used for profit tax purposes. Transfer prices calculated under the Regulations may be used to recalculate profit tax in respect of controlled transactions between the following persons:

- ▶ A resident of Azerbaijan and a related non-resident;
- ▶ A PE of a non-resident in Azerbaijan and the non-resident itself or any of its representative offices, branches or divisions located in other countries or any other person located in another country that is a related person of the non-resident;
- ▶ A resident of Azerbaijan and/or a PE of a non-resident in Azerbaijan and entities incorporated (registered) in jurisdictions identified as having preferential tax regimes.

As a rule, where the prices or margins in controlled transactions involving supplies of goods (works, services) are not consistent with those of comparable transactions carried out between unrelated parties under the same or similar conditions at arm's length, the tax base of the transaction may be recalculated based on transfer prices.



The Regulations also lay down certain contingent methods for determining transfer prices if no information is available on comparable transactions.

Taxpayers must submit a notification to the tax authorities in respect of controlled transactions exceeding AZN 500,000 during the reporting period. The deadline for submitting the notification is 31 March of the year following the reporting year.

Market prices

In the case of import and export operations, barter transactions, transactions between related parties and transactions in which the price differs by more than 30% from prices in transactions for the same (similar) goods (works, services) on the market during the preceding 30 days, or where property is insured for amounts exceeding its net book value, or where the minimum amount of monthly rent for real estate (other than housing) is required to be established for tax purposes, taxes may be recalculated based on the market price.

Declarations and payments

Profit tax is calculated on a calendar year basis. All taxpayers must submit their profit tax returns no later than 31 March of the year following the reporting year. The deadline may be extended by three months provided that tax is paid in full by the original due date. Tax installments are due quarterly by the 15th of the month following each

quarter. Tax installments are estimated as one quarter of the tax payable for the previous calendar year or may be calculated by multiplying income for the latest quarter by the ratio of tax to annual income for the previous year.

The final payment of the balance due must be made no later than 31 March of the following year. Failure to comply may result in penalties (for details of these, see the Interest and penalties section below).

Individual tax

Residency rules/scope

A resident is defined as an individual who is physically present in the Republic of Azerbaijan for a period of 183 days or more in a calendar year. Individuals not meeting this requirement are considered to be non-residents unless otherwise determined by the application of tie-breaker rules.

Residents are taxed on their worldwide income, while non-residents are taxed only on their Azerbaijani source income. Tax on Azerbaijani source income is normally paid by withholding tax at source at progressive rates. Income from overseas sources is assessed on a current year basis for residents. An Azerbaijani source of income is defined as any income from commercial activities and sources in Azerbaijan, and specifically includes dividends received from Azerbaijani companies, income from the sale of shares and participating interests in Azerbaijani companies,

income from employment in Azerbaijan, etc. The place of payment is irrelevant in determining the source of income.

Rates

Income earned from employment in the oil and gas or public sectors is subject to the following tax rates:

Monthly taxable income	Tax rates
Up to AZN 2,500	14%
Over AZN 2,500	AZN 350 + 25% of the amount exceeding AZN 2,500

Starting from 1 January 2019, individuals whose monthly income is less than AZN 2,500 are exempt from tax on the first AZN 200 of their income. Annual income of individuals engaged in non-entrepreneurial activity is taxed at the rate of 14%. Individuals whose annual income is less than AZN 30,000 are exempt from tax on the first AZN 2,400 of their income. Individuals who derive income from business activities without forming a legal entity are liable to personal income tax at the rate of 20%. Effective from 1 January 2019, employees not working in the oil and gas and public sectors are eligible for reduced PIT rates as follows for a period of 7 years:

Monthly taxable income	Tax rates
Up to AZN 8,000	0%
Over AZN 8,000	14% of the amount exceeding AZN 8,000

Determination of taxable income

Virtually all forms of compensation to an employee are taxable, including hardship and cost of living allowances, payments by an employer for the education of an employee's child and payment of taxes on behalf of an employee, unless they are specifically exempted. One such exemption is accommodation and meal expenses incurred by an employer on behalf of employees, provided that no tax deduction is made for these expenses on the profit tax return.

Social Insurance Fund contributions payable by employees

Subject to the exception below, both Azerbaijani and foreign nationals earning employment income in Azerbaijan must contribute 3% of their gross salary to the Social Insurance Fund of Azerbaijan ("Fund").

For individuals engaged in employment activities in neither the oil and gas sector nor the public sector, the following amounts must be withheld from the employee for a period of 7 years starting from 1 January 2019:

Gross taxable monthly income of:

- ▶ below AZN 200 - 3% of the amount;
- ▶ above AZN 200 - 10% of the amount exceeding AZN 200 plus AZN 6.

Contributions are to be withheld at source and remitted to the Fund by the employer. Fund contributions are not applicable to foreign employees who are employed under PSA-related contracts.

In addition, effective from 1 January 2018, employers must withhold 0.5% from the employee's monthly wage and contribute it to the Unemployment Fund as an unemployment insurance premium.

Capital gains and investment income

Sales of movable assets are not generally subject to income tax unless the disposal relates to business or other entrepreneurial activities. The sale of an immovable asset is not subject to tax if it has been the place of residence of the seller for at least five years. Except for these two exemptions, all other gains resulting from the sale of property are taxable based on the annual income tax rates for individuals and the profit tax rate for legal entities.

Gains arising from the alienation of shares or other participating interests in resident enterprises are also subject to general income tax. Such gains must be calculated as the difference between the actual sale price and the nominal value of the sold shares if the shares/participating interests are sold for a price exceeding the proportional value of net assets of the company corresponding to the alienated shares/participating interest. If the sale price is lower than the proportional value of net assets, the gain is calculated as the difference between the proportional value of net assets as at the date of sale and the nominal value of the alienated shares.

50% of a taxpayer's income from the sale of shares/participating interests owned by the taxpayer for at least 3 (three) years is exempt from income tax.

Interest on deposits of individuals and dividends received by individual shareholders of JSCs are exempt from taxes until 1 February 2023.

Declarations and payments

Both residents and non-residents must complete and file their income tax declarations no later than 31 March of the following tax year. Tax must be paid before the filing deadline. Where a taxpayer only has Azerbaijani source income, which is subject to withholding tax at source, the individual is not required to submit an income tax declaration.

The deadline for filing declarations may be extended by three months provided that tax is paid in full by the original due date. Failure to comply may result in penalties (for details of these, see the Interest and penalties section below).

Value added tax (VAT)

Scope

All companies that do business and/or import goods and services into Azerbaijan are subject to VAT. Effective from 1 January 2017, the trade-markup applied to retail sales of agricultural produce is also subject to VAT.

Rate

The standard VAT rate is 18%.



VAT registration

There are detailed requirements for VAT registration and accounting, with set penalties for non-compliance. Legal entities and individuals with taxable turnover exceeding AZN 200,000 over twelve consecutive months, excluding those involved in trade and public catering services, must register as VAT payers.

Other companies doing business in Azerbaijan may register voluntarily. Only registered VAT payers may charge VAT or claim credit for input VAT that they pay.

Determination of the taxable base

VAT is levied on turnover from supplies of all goods and services, including imports, unless they are zero rated or specifically exempt. Barter and free supplies of goods and services are specifically included in the taxable base. All excise taxes and customs duties paid are also included in the taxable base for VAT purposes.

Zero-rated goods and services include exports, transit and international transportation, purchases of goods and services for projects funded by international loans, and imports paid

for with foreign financial donations. Exempted goods and services include:

- Financial services;
- Currency and securities transactions;
- Publications.

Generally, goods are deemed to be imported or exported if they undergo customs clearance.

There are detailed place of supply rules for determining the treatment of exported and imported services. Azerbaijani tax legislation generally allows credit for input VAT on commercial goods or services.

However, credit is allowed only if VAT is paid to suppliers through a designated VAT deposit account (see below for additional information). Credit is not allowed for input VAT in relation to VAT exempt goods or services (such input VAT can only be claimed as a deduction for profit tax purposes). If input VAT exceeds output VAT, the excess input VAT may be carried forward or offset against certain VAT or other tax liabilities. Taxpayers may also apply to the tax authorities for a refund of excess input VAT. VAT on purchases of fixed and intangible assets is not capitalized as part of the asset's cost, but offset against output VAT.

Reverse charge of VAT

Foreign companies that provide services in Azerbaijan without establishing a PE must pay VAT on taxable sales in Azerbaijan. In such cases, VAT is applied through the reverse charge mechanism. In other words, it is self-assessed by the recipient of the services and remitted to the state budget.

VAT deposit accounts

All VAT payers are required to remit VAT amounts through designated bank accounts known as VAT deposit accounts. Only VAT payments made through these accounts may be credited against output VAT. The VAT is then claimed by the payer.

Declarations and payments

Declarations must be filed and VAT must be remitted monthly by the 20th of the following month. Whereas before 1 January 2020, output VAT was generally accounted for on both accrual and cash bases and input VAT was accounted for on a cash basis, starting from 1 January 2020 both output and input VAT is accounted for on a cash basis. VAT on imported goods is paid separately at the point of customs clearance.

Timing of transactions for VAT purposes

In accordance with amendments made to the Tax Code which are effective from 1 January 2020, for VAT purposes transactions are recognized based on the date of payment. "Payment" in this context means the receipt of the principal amount due (exclusive of VAT) for goods (works, services) supplied.

Provisions have been introduced to clarify the concept of payment in specific cases. Specifically, the date of payment is defined as:

- ▶ The date on which money is received by the taxpayer in cash or as a transfer to an account held by or otherwise at the disposal of the taxpayer;
- ▶ In the case of mutual settlements – the date of the discharge or settlement of an obligation;

- ▶ In the case of accounts receivable – the date of the expiration of the recovery period;
- ▶ In the case of in-kind and barter transactions – the date of the alienation of assets;
- ▶ In the case of alienation without consideration – the actual date of such alienation;
- ▶ In the case of the assignment of a claim – the actual date of such assignment.

Where a purchaser does not pay for goods or services received from a supplier, but grants a loan to the supplier, a taxable transaction is deemed to have occurred:

- ▶ On the date of the supply if the loan was granted before the supply was made;
- ▶ On the date of the loan if the loan was granted after the supply was made.

Where payment for goods or services supplied is made in installments, each installment is considered as a separate taxable transaction.

Electronic Delivery Notes

Effective from 1 January 2017, an electronic delivery note is defined as a primary accounting document prepared in electronic format that is issued by a person supplying goods, services or works to individual entrepreneurs and legal entities. As from 1 January 2020, electronic VAT invoices have been abolished and electronic delivery notes

are the only documents required to be issued by suppliers to their customers when selling goods or providing services or works. Electronic delivery notes issued by the supplier suffice for a transaction to be recognized and for input VAT to be reclaimed.

Electronic delivery notes must be provided for supplies of goods (services, works) to legal entities and individuals engaged in entrepreneurial activities.

The general format and content of electronic delivery notes and the procedures for their issue, amendment and cancellation are laid down in the Regulations on Electronic Delivery Notes approved by a Resolution of the Cabinet of Ministers.

Other taxes and fees

Excise tax

Excise taxes range from 3% to 72% for domestically produced hydrocarbon products and from AZN 0.2 to AZN 3.2 per liter for alcoholic beverages. The rate for tobacco products is AZN 31 per 1,000 units. Excise tax and VAT are not included in the taxable base. Imported automobiles, yachts, platinum, gold, and diamonds are also subject to excise taxes.

Excise tax for platinum is AZN 4 per gram; for gold it varies from AZN 1.5 to AZN 6 per gram depending on the amount of gold in a thousand weight units; for diamonds it is AZN 400 per carat, but the calculation may differ depending on the diamond's size.

Where excisable goods are produced from excisable supplies, any excise tax paid on the supplies may be deducted from the excise tax due on the finished product.

Declarations must be filed and payment must be made monthly by the 20th of the following month. Excise tax is deductible for profit tax purposes.

Property tax

Property tax is levied at the rate of 1% of the average annual net book value of fixed assets, including buildings, machinery and equipment (excluding vehicles). The taxable base is calculated as the average of the values at the beginning and end of the year. If property of an enterprise is insured for an amount exceeding its residual value, property tax is calculated at the rate of 1% of its market price. Property tax is deductible for profit tax purposes. The following are exempt from property tax:

- ▶ Facilities that are used for environmental protection, fire safety or civil defense purposes;
- ▶ Product pipelines, railways and motorways, communication and power transmission lines, irrigation facilities, satellite and other aerospace assets;
- ▶ Vehicles;
- ▶ Property of educational, health, sport and cultural institutions used only for officially designated purposes.

Taxpayers are expected to submit their declarations no later than 31 March of

the following year. Tax due is payable in quarterly installments by the 15th of the second month of the calendar quarter in the amount of 20% of the property tax due for the previous year.

Road tax

Non-resident owners of vehicles entering the territory of Azerbaijan to transport passengers or cargo must pay road tax. The road tax payable by such non-resident owners is collected by the customs authorities at rates depending on the engine volume and weight of the vehicle, the period of stay in Azerbaijan, the number of seats, the axle load and the nature of imported products.

Tax is also indirectly applicable to vehicles used locally through the taxation of automobile gasoline, diesel fuel and liquid gas producers and importers. Specifically, AZN 0.02 is added to the wholesale price per liter of automobile gasoline, diesel fuel and liquid gas produced for local consumption or imported into Azerbaijan.

Land tax

Companies using land are generally subject to land tax calculated at AZN 2 to AZN 20 per 100 square meters, depending on location. Land tax is deductible for profit tax purposes.

Taxpayers are required to submit their declarations annually by 15 May. The tax is payable twice a year, no later than 15 August and 15 November.

Social Insurance Fund employer contributions

Employers in the oil and gas sector and the public sector are required to make contributions to the Fund amounting to 22% of the gross payroll for both local and foreign employees.

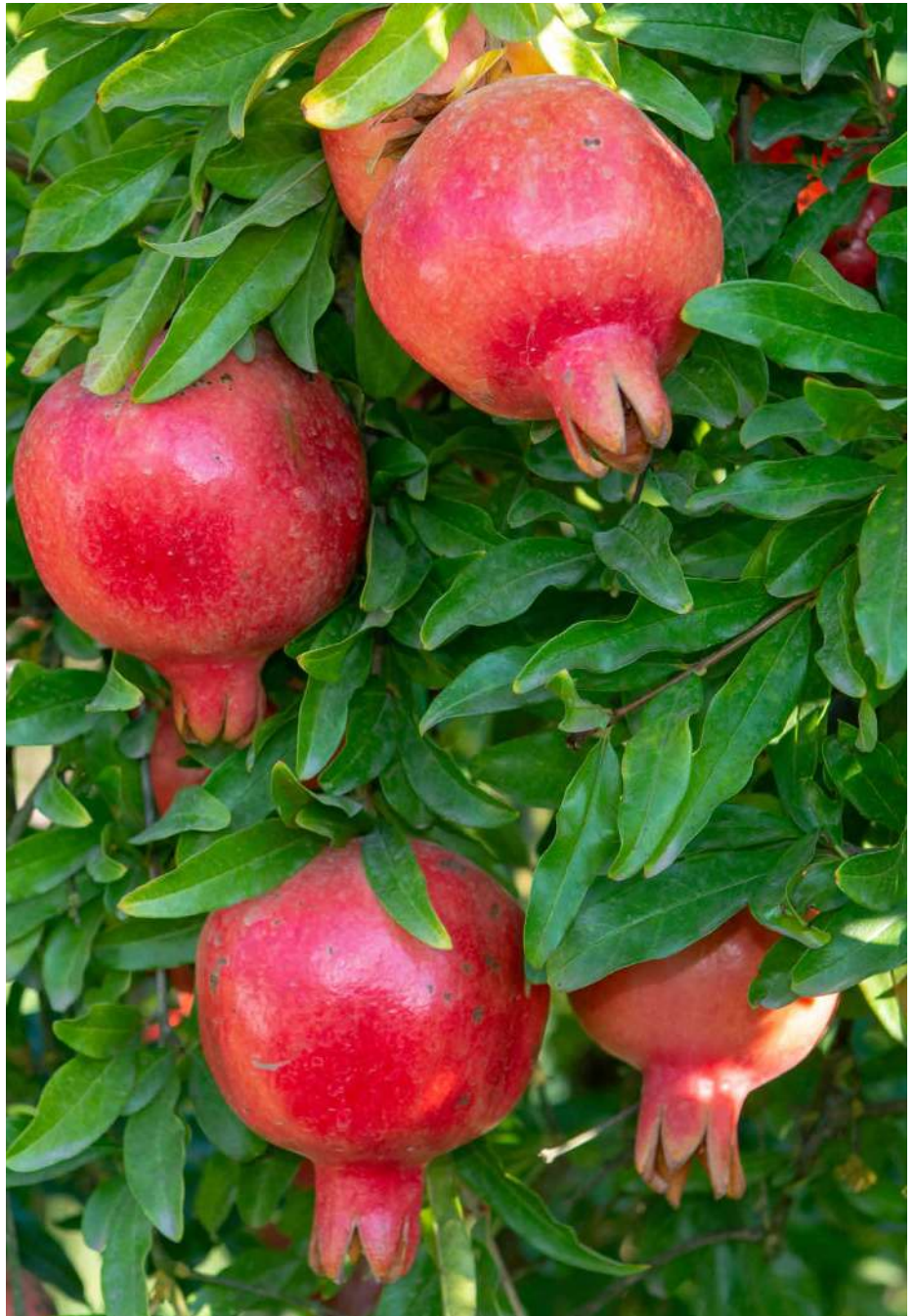
Effective from 1 January 2019, employers other than those operating in the oil and gas and public sectors are required to make Fund contributions amounting to 22% of the gross taxable monthly income of both local and foreign employees if their gross taxable monthly income is below AZN 200, and 15% of the amount exceeding AZN 200 plus AZN 44 if their gross taxable monthly income is above AZN 200, for a period of 7 years.

These contributions are made at the expense of the employer and are deductible for profit tax purposes. Relevant reports must be filed quarterly by the 20th of the following month. Fund contributions do not have to be made in relation to foreign employees employed under PSA-related contracts.

In addition, effective from 1 January 2018, employers contribute 0.5% to the Unemployment Fund as an unemployment insurance premium.

Mining tax

All companies and individuals engaged in extracting mineral resources are subject to mining tax at the appropriate rate in addition to any land tax due.



Mining tax is deductible for profit tax purposes. The tax is applied to the wholesale price of oil, natural gas and all types of metals at rates ranging from 3% to 26%. For all other taxable mineral resources, the rates range from AZN 1 to AZN 10 per cubic meter. Taxpayers are required to submit their declarations monthly by the 20th of the following month. The tax is payable monthly by the 20th of the following month.

Simplified taxation system

Legal entities and individual entrepreneurs that are not required to register for VAT purposes in Azerbaijan are eligible to be registered as payers of simplified tax, which is generally levied at 2%. The taxable base is gross income received from sales of goods, works and services, except for income subject to withholding tax.

Persons engaged in public catering activities with a taxable turnover exceeding AZN 200,000 in any month(s) over a period of 12 consecutive months are also entitled to register as payers of simplified tax. The tax rate in such cases is 8%.

Special simplified tax rates are established for taxpayers engaged in certain activities (the list below is non-exhaustive):

- ▶ Persons engaged in the provision of their own residential and non-residential premises – AZN 15 multiplied by the location zone rate, varying from 1.2 to 4.0 per square meter;

- ▶ Alienation of land – taxation depends on the location and purpose of use. Agricultural land is subject to tax calculated at AZN 0.5 per square meter, while for other types of land tax is calculated at AZN 0.5 per square meter and multiplied by the appropriate location coefficient specified in the Tax Code.

Legal entities operating under the simplified tax regime do not pay VAT or profit tax.

Any taxpayer whose business is transporting passengers or cargo (except for international transportation) is liable to pay a fixed amount of simplified tax and is required to obtain what is referred to as a “distinguishing license plate”. Taxpayers who are not involved in a local transportation business and own vehicles for the transportation of their own cargo and employees must obtain a “special distinguishing license plate” to differentiate themselves from simplified taxpayers. Both distinguishing license plates and special distinguishing license plates are issued by the Ministry of Transport of Azerbaijan at no cost within two and five days respectively.

Taxpayers under the simplified tax regime must submit their declarations quarterly by the 20th of the following month. The tax is payable quarterly by the 20th of the following month.

Persons who do not have the right to become simplified taxpayers include:

- ▶ Persons engaged in trading activities for whom the volume of taxable transactions in any month (months) during a period of 12 consecutive months exceeds AZN 200,000;

- ▶ Persons who provide services other than services rendered to persons not registered as taxpayers (except for persons who pay fixed amounts of simplified tax);
- ▶ Persons engaged in the production of goods that are excisable and subject to mandatory labeling;
- ▶ Persons engaged in production activities that have more than 10 employees;
- ▶ Persons engaged in the provision of their own residential and non-residential premises – AZN 15 multiplied by the location zone rate, varying from 1.2 to 4.0 per square meter;
- ▶ Persons engaged in wholesale activities;
- ▶ Credit organizations, professional participants in the insurance market (other than insurance agents providing services relating to compulsory insurance agreements), investment funds and managers of such funds, persons licensed in the securities market, and pawnshops.

Import tax

The maximum rate of import tax is currently 15%. There are certain import tax exemptions.

Customs processing fees are payable on imported goods in amounts ranging from AZN 10 to AZN 550 (depending on the value of the goods declared and whether customs clearance takes place within or outside regular working hours and within or outside the customs territory).

Export tax

Most goods are exempt from export tax.

Interest and penalties

Interest and penalties are applied for non-compliance with tax legislation. For example, interest is charged on outstanding tax liabilities at the rate of 0.1% per day.

The following is a non-exhaustive list of penalties that may be applied for non-compliance with tax legislation:

Nature of payment	Rate of withholding tax (%)
Insurance premiums	4%
Fees for international communication and freight services	6%
Dividends and interest, including the interest element of financial lease payments	10%
Management fees and fees for other services performed or deemed to be performed in the territory of Azerbaijan but not connected with an Azerbaijani PE	10%
Rents and royalties	14%
Branch remittance tax – for the remittance of profit derived from a permanent establishment in Azerbaijan to the head office	10%
Payments to countries with a favorable tax regime*	10%

* The list of countries with a favorable tax regime is approved by the President of the Republic of Azerbaijan.

Withholding tax

Scope

Withholding tax is applicable to the repatriation of profit and other cross-border payments to foreign companies not related to a PE in Azerbaijan. The tax is payable at the following rates:

Double tax treaties

The rate of withholding tax under existing double tax treaties varies depending on the content of a particular treaty. The maximum rates of withholding tax under current double tax treaties are shown in the table below.

Offence	Penalty
Failure to file declarations	AZN 40
Understatement of tax liability	50% of understated tax
Payments from petty cash while bank accounts are under tax sanctions or penalties imposed by the tax authorities	50% of expenses paid from petty cash
Failure to register a foreign bank account with the tax authorities	100% of the revenue collected on such accounts
Delay in paying VAT on supplier/service provider invoices in accordance with the rules on the payment of VAT using a designated bank account	50% of VAT paid in violation of the special rules
Carrying out cash settlements in violation of the rules on cases where cash settlements are prohibited	1 st time in a calendar year – 10% of the total transaction amount; 2 nd time – 20%; 3 rd time or more – 40%.
Purchasing goods without receiving a delivery note, electronic delivery note or e-VAT invoice	1 st time in a calendar year – 10% of the value of the goods purchased; 2 nd time – 20%; 3 rd time or more – 40%.
Supplying goods without issuing an electronic delivery note or an electronic tax invoice required to be issued under the Tax Code	1 st time in a calendar year – 10% of the value of the goods supplied; 2 nd time – 20%; 3 rd time or more – 40%.

The statute of limitations for a tax violation is three years.



Payee resident in	Dividends (%)	Interest (%)	Royalties (%)
Austria	5/10/15	0/10	5/10
Belarus	15	0/10	10
Belgium	5/10/15	0/10	5/10
Bosnia and Herzegovina	10	0/10	10
Bulgaria	8	0/7	5/10
Canada	10/15	0/10	5/10
China	10	0/10	10
Croatia	5/10	0/10	10
Czech Republic	8	0/5/10	10
Denmark	5/15	0/8	5/10
Estonia	5/10	0/10	10
Finland	5/10	0/10	5/10
France	10	0/10	5/10
Georgia	10	0/10	10
Germany	5/15	0/10	5/10
Greece	8	0/8	8
Hungary	8	0/8	8
Iran	10	0/10	10
Israel	15	0/10	5/10
Italy	10	0/10	5/10
Japan	15	0/10	10
Jordan	8	0/8	10
Kazakhstan	10	0/10	10
Kuwait	5/10	0/7	10
Latvia	5/10	0/10	5/10
Lithuania	5/10	0/10	10
Luxembourg	5/10	0/10	5/10

Payee resident in	Dividends (%)	Interest (%)	Royalties (%)
Macedonia	8	0/8	8
Malta	8	0/8	8
Moldova	8/15	0/10	10
Montenegro	10	0/10	10
Netherlands	5/10	0/10	5/10
Norway	10/15	0/10	10
Pakistan	10	10	10
Poland	10	0/10	10
Qatar	7	0/7	5
Romania	5/10	0/8	10
Russian Federation	10	0/10	10
San Marino	5/10	0/10	5/10
Saudi Arabia	5/7	0/7	10
Serbia	10	0/10	10
Slovenia	8	0/8	5/10
South Korea	7	0/10	5/10
Sweden	5/15	0/8	5/10
Switzerland	5/15	0/5/10	5/10
Tajikistan	10	0/10	10
Turkey	12	0/10	10
Turkmenistan	10	0/10	10
UAE	5/10	0/7	5/10
Ukraine	10	0/10	10
United Kingdom	10/15	0/10	5/10
Uzbekistan	10	0/10	10
Vietnam	10	0/10	10
Notreaty country	10	10	14

5 Accounting and reporting



All entities registered in Azerbaijan (Azerbaijani legal entities, representative offices and branches) are required to maintain their books and records in the territory of Azerbaijan in accordance with the appropriate standards.

The Law on Accounting stipulates that all public interest entities, including credit institutions, insurance companies, investment funds and managers of such funds, non-public (private) social funds, licensed participants in the securities market, listed entities, commercial organizations meeting certain criteria and, subject to certain exceptions, public legal entities, must maintain their records in accordance with International Financial Reporting Standards ("IFRS"). At the same time, large and medium-sized enterprises and medical and educational institutions must follow IFRS for Small and Medium-Sized Entities ("IFRS for SME") if their charters allow them to engage in entrepreneurial activities. All other large and medium-sized enterprises may also use IFRS. Micro and small enterprises may either use the bookkeeping rules for micro and small enterprises set by the Ministry of Finance of Azerbaijan, or follow IFRS for SME.

Investment Incentive Certificates

An investment incentive certificate ("Certificate") entitles its holder to tax and customs benefits. The Certificate is granted by the Ministry of Economy of Azerbaijan to entrepreneurs who have submitted investment projects that meet criteria approved by the Cabinet of Ministers regarding the field of economic activity, the minimum investment amount and the region in which the investment project is to be carried out. Accordingly, the Tax Code and the Law on Customs Tariffs set out the applicable tax and customs duty exemptions for entrepreneurs. The following exemptions from taxes apply

for a period of 7 years from the date the Certificate is obtained:

- ▶ Personal income tax – 50% of an individual entrepreneur's income;
- ▶ Profit tax – 50% of a legal entity's income;
- ▶ VAT – full exemption for the import of machinery, production equipment and devices by individual entrepreneurs and legal entities;
- ▶ Property tax – full exemption for relevant property of individual entrepreneurs and legal entities;
- ▶ Land tax – full exemption for relevant land parcels owned or used by individual entrepreneurs and legal entities.



6 EY Azerbaijan



Introduction

EY has led projects in Azerbaijan continuously since 1993. We were the first international accounting and tax consulting network to establish a member firm in Azerbaijan. Our office in Baku opened in 1994. Currently we have a team of over 200 professionals, led by Assurance Partner Ilgar Veliyev, a member of the American Institute of CPAs.

Services

EY Azerbaijan, in conjunction with partners and staff in other EY offices, provides Assurance, Tax & Law, Advisory and Transaction Advisory Services to both international and local clients.

We have undertaken a number of major assignments in the country relating to inbound investment, enterprise and sector restructuring, and public policy.

Assurance

EY has been licensed to conduct audits in Azerbaijan since 1994. We have gained unprecedented experience in that time.

Many of the auditors at our Baku office are certified public accountants (US) and/or ACCA members.

We provide audit services to numerous companies operating in Azerbaijan under PSAs. We audit the cost recovery reports and profit tax returns of all PSAs

and perform profit tax return audits for numerous contracting parties owning interests in various PSAs.

We also provide accounting advice and other Assurance services to foreign and Azerbaijani companies preparing accounts in accordance with IFRS, US GAAP and UK GAAP.

Tax & Law

EY is recognized as the leading tax and legal advisor in Azerbaijan. The Tax and Law service line is headed by Partner Arzu Hajiyeva. Through its team of tax and legal consultants, EY

advises on all aspects of corporate and personal tax planning and compliance and licensing, corporate, insurance, business, migration, contract and labor law. We have provided advice on local and international tax and legal issues to numerous international entities that have already made or are considering making investments in Azerbaijan. Our areas of expertise include international tax planning, transaction structuring, expatriate tax affairs, local tax compliance, currency and foreign exchange planning and legal advisory and due diligence, as well as litigation support, representing clients in disputes, including in proceedings before courts and other adjudicatory bodies.



Our impressive client base speaks for itself. The firm has established good working relationships with key state bodies and government agencies and is in a position to facilitate negotiations between potential investors and the authorities.

This continues to be a key service in a legislative environment that is constantly evolving and open to interpretation.

The firm's tax practice receives technical support and a wider perspective on tax affairs in the CIS through its links with the rest of the EY network.

Advisory Services

EY's Advisory practice comprises professionals with extensive experience in addressing a broad spectrum of business goals. We are experts in delivering performance improvements and business value to our clients, reducing costs, managing risks, operating efficient IT systems, and successfully accomplishing operational and strategic objectives.

A dedicated team develops each project based on the specific features of the industry and the client.

Our clients in Baku are major private holdings and state-owned entities. As part of a global network, we are able to team up with professionals from all over the world to help our clients overcome market challenges and address unique business risks. We combine our international perspective and experience with knowledge of the local market and realities to provide unsurpassed consulting services, ensuring our clients' businesses grow.

Our major services include:

- Performance Improvement;
- Financial Services Advisory.

Transaction Advisory Services

EY's Transaction Advisory Services team provides assistance in finance raising (including project finance, infrastructure financing and public-private partnerships), mergers and acquisitions, infrastructure and real estate transactions. We are experienced independent financial advisors who have participated in numerous transactions regionally and locally.

We provide a full range of hands-on, operationally focused support and advice across the transaction life cycle, on both buy-side and sell-side. We also put together the most effective restructuring plans, improving transactions to achieve clients' strategic goals.

Our services include assistance in valuing clients' businesses, financial interests, assets and liabilities, utilizing our proven experience in legal taxation and financial due diligence to provide clients with valuation advice for a multitude of purposes. With more than 10 years of local expertise, we provide the following Transaction Advisory Services:

- Lead Advisory;
- Operational Transaction Services;
- Real Estate Advisory Services;
- Restructuring;
- Transaction Support;
- Transaction Tax;
- Valuation & Business Modeling.

Ernst & Young Holdings (CIS) B.V. Baku office

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About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY works together with companies across the CIS and assists them in realizing their business goals. 5,500 professionals work at 19 CIS offices (in Moscow, Ekaterinburg, Kazan, Krasnodar, Novosibirsk, Rostov-on-Don, St. Petersburg, Togliatti, Vladivostok, Almaty, Atyrau, Nur-Sultan, Baku, Bishkek, Kyiv, Minsk, Tashkent, Tbilisi, Yerevan).

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