

International Tax

Azerbaijani Highlights

In Plain English



CASTRO
& CO
INTERNATIONAL



1701 Pennsylvania Ave NW, Suite 200
Washington, DC.
20006, USA

Phone : +1 202 792 6600
www.CastroAndCo.com

Investment basics:

Currency – Azerbaijani Manat (AZN)

Foreign exchange control – There are no restrictions on the import or export of capital. Supporting documentation, including tax payment documents and bank statements, must be submitted when cash withdrawals exceed amounts previously imported into the country. Amounts may be repatriated in any currency, and both residents and nonresidents can hold bank accounts in any currency.

Accounting principles/financial statements – IFRS are required (except for micro and small enterprises). Contractors operating under production sharing agreements (PSAs), risk service agreements (RSAs) or host government agreements (HGAs) in the oil and gas industry are required to maintain books in US dollars in accordance with the principles of generally accepted international petroleum industry accounting. Financial statements must be prepared annually.

Principal business entities – These are the limited liability company, open/closed joint stock company, general partnership, limited partnership, cooperative, and branch and representative office of a foreign company.

Corporate taxation:

Residence – An entity that is incorporated in Azerbaijan is considered resident; branch offices and representative offices of foreign legal entities are considered nonresident.

Basis – Residents are taxed on worldwide income; nonresidents are taxed only on Azerbaijan-source income.

Taxable income – Profit tax is imposed on a company's operating profits, computed as the difference between total taxable income and deductible expenses. Normal business expenses are deductible in computing taxable income. Companies operating in the oil and gas sector are governed mainly

by PSAs, RSAs or HGAs but projects not covered by such agreements are taxed in accordance with the rules in the tax code.

Taxation of dividends – Dividends received from Azerbaijan companies and permanent establishments of foreign companies located in Azerbaijan are exempt from profit tax; they are subject only to a 10% withholding tax.

Capital gains – Capital gains are treated as normal income and taxed at the ordinary profit tax rate.

Losses – Losses may be carried forward for five years. The carryback of losses is not permitted.

Rate – Azerbaijan legal entities are subject to profit tax at 20% on their worldwide income. Nonresidents are taxed on Azerbaijan-source income at the same rate. PSA and RSA contractors that carry out business in Azerbaijan in connection with petroleum operations pay profit tax at pre-negotiated rates of 20% to 32%. In lieu of profit tax, foreign subcontractors operating under PSAs and RSAs pay withholding tax at rates ranging from 5% to 10% of the gross payments received as consideration for work or services performed in Azerbaijan. The tax is deducted by the payer and is a final tax for the foreign subcontractor. In accordance with new PSAs and RSAs, foreign subcontractors who have a registered presence in Azerbaijan must pay profit tax in accordance with the provisions of the tax code. Tax is imposed on the taxable annual profit of each main exporting pipeline (MEP) participant relating to MEP project activities at a flat rate of 27%.

Surtax – No

Alternative minimum tax – No

Foreign tax credit – Corporate income taxes paid outside Azerbaijan may be credited against Azerbaijan tax due. Excess foreign tax credits may not be offset against a

resident taxpayer's Azerbaijan tax liabilities on any domestic-source income, nor may they be carried forward or back.

Participation exemption – No

Holding company regime – No

Incentives – The tax code provides for a 50% exemption from profit tax for legal entities holding an investment promotion certificate. The exemption is valid for seven years from the date of obtaining the certificate. Certain other incentives also may be available for legal entities and individuals holding an investment promotion certificate. As from 1 January 2019, profit tax exemptions also are available for: i) 50% of the income from the disposal of shares and participations held for at least three years; ii) profits of micro or small enterprise start-ups for three years after the start-up certificate is obtained; and iii) 75% of the profits of micro enterprises.

Withholding tax:

Dividends – Dividends paid to a nonresident are subject to a 10% withholding tax, unless the rate is reduced under a tax treaty.

Interest – Interest paid to a nonresident is subject to a 10% withholding tax, unless the rate is reduced under a tax treaty.

Royalties – Royalties paid to a nonresident are subject to a 14% withholding tax, unless the rate is reduced under a tax treaty.

Technical service fees – Although Azerbaijan tax law does not specifically address technical service fees, such fees generally are subject to a 10% withholding tax.

Branch remittance tax – Net profits remitted to the foreign head office of a branch are subject to a 10% withholding tax.

Other – Direct or indirect payments made by Azerbaijan residents to persons registered in one of the 40 listed countries and territories deemed to have low-tax regimes are subject to an additional

withholding tax of 10%.

Other taxes on corporations:

Capital duty – No

Payroll tax – No

Real property tax – An annual land tax is levied on the owners and users of land (whether or not resident), with the amount of tax depending on the location and use of the land.

Legal entities holding an investment promotion certificate are exempt from land tax for seven years from the date of obtaining the certificate.

Social security – Both employers and employees are required to make social insurance contributions (SIC). For a seven-year period as from 1 January 2019, the SIC rates payable by employers on behalf of private sector employees (other than those working in the oil and gas industry) are 3% on the first AZN 200 of gross salary and 10% on the excess.

An additional 1% unemployment insurance contribution also is payable - 0.5% paid by the employer on the gross payroll and 0.5% withheld by the employer from the gross salary of the employee.

Stamp duty – No

Transfer tax – No

Other – An assets tax is levied on owners of fixed assets, with some exceptions.

A seven-year exemption from assets tax on relevant fixed assets is granted for: i) legal entities (from the date of obtaining an investment promotion certificate) and ii) small and medium enterprises that are part of an SME cluster (from the date of their registration). Legal entities and individual entrepreneurs classified as micro enterprises also are exempt from assets tax.

Anti-avoidance rules:

Transfer pricing – Transactions between related parties must be on arm's length terms. The tax authorities may adjust the contract price: i) in barter or import-export transactions; ii) in transactions between related persons (as defined in the tax code); iii) where the price deviates by 30% or more from transactions involving similar or identical goods, work or services, taking into account conditions that would affect market price; iv) where the property is insured for a value exceeding its net book value; and v) where a monthly lease fee is paid for immovable property (other than housing).

Transfer pricing rules apply to cross-border controlled transactions with associated parties. Controlled transactions exceeding AZN 500,000 per counterparty per calendar year must be reported to the tax authorities by 31 March of the year following the reporting year.

Thin capitalization – Thin capitalization rules are introduced as from 1 January 2019 where the foreign borrowing of a company is at least twice its net asset value (the foreign leverage ratio). The interest paid attributable to the portion of the debt exceeding the ratio is not tax-deductible.

Controlled foreign companies – An Azerbaijan resident that holds, directly or indirectly, more than 20% of the charter capital or voting shares of a foreign legal entity that receives income from a low-tax jurisdiction must include its proportionate share of that foreign entity's income in its taxable income. A foreign jurisdiction is considered a low-tax jurisdiction if the tax rate is 50% or less than the rate in Azerbaijan, or if the country has laws on the confidentiality of information about companies or laws that allow secrecy of financial information or information on the actual owner of property or income (property) recipient.

Disclosure requirements – No

Compliance for corporations:

Tax year – Calendar year

Consolidated returns – A legal entity may file a consolidated return that includes the taxable income and deductible expenses of its branch offices.

Filing requirements – The profit tax return is due by 31 March (inclusive) following the end of the tax year. Other tax returns are filed on a periodic basis (monthly, quarterly and annually).

Legal entities and entrepreneurs that are registered for VAT purposes and simplified taxpayers paying employment income to individuals must submit tax declarations to the tax authorities before 31 January of the year following the reporting year.

Penalties – Penalties apply for late filing, failure to file or tax avoidance or evasion.

Rulings – A taxpayer may apply for an advance tax ruling for each transaction (separately) exceeding a value of AZN 10 million.

Personal taxation:

Basis – Azerbaijan residents are subject to income tax on taxable income, which is defined as gross income received from all sources, regardless of where the income was earned or paid, less allowable deductions.

A 50% exemption from personal income tax is granted to individuals who hold an investment promotion certificate for seven years from the date of obtaining the certificate.

As from 1 January 2019, a 75% exemption is granted for income of entrepreneurs classified as micro enterprises and income from innovative activities of micro or small enterprises will be exempt from taxation for three years upon receipt of the start-up certificate.

Nonresidents are subject to Azerbaijan income tax on Azerbaijan-source income.

Residence – Unless otherwise provided in an applicable tax treaty, an individual generally is considered to be tax resident if he/she is physically present in Azerbaijan for a period of more than 182 cumulative days in a calendar year (regardless of nationality).

Filing status – Each taxpayer must file an individual tax return; joint returns are not permitted.

Taxable income – Taxable income includes income from employment, income from entrepreneurial activities and passive income. Certain income, such as property inherited from family members, alimony, etc., is exempt.

Capital gains – Capital gains are treated as normal income and taxed at the ordinary personal tax rate.

Deductions and allowances – Expenses incurred by an entrepreneur may be deducted in computing taxable income.

Rates – Rates are progressive up to 25%. Employment income of up to AZN 8,000 per month is exempt from personal income tax for seven years as from 1 January 2019 for private sector employees (other than those working in the oil and gas industry). The excess and any investment income are taxed at 14%. Individual entrepreneurs are taxed at a 20% rate.

Other taxes on individuals:

Capital duty – No

Stamp duty – No

Capital acquisitions tax – No

Real property tax – An annual land tax is levied on the owners and users of land (whether or not resident), with the amount of tax depending on the location of the land and how it is used.

Inheritance/estate tax – No

Net wealth/net worth tax – No

Social security – SIC for employed individuals are withheld by the employer; self-employed individuals must register and pay their own contributions. For a seven-year period as from 1 January 2019, the SIC rates payable by private sector employees (other than those working in the oil and gas industry) are 22% on the first AZN 200 of gross salary and 15% on the excess.

An additional 1% unemployment insurance contribution also is payable. The employee contribution of 0.5% of gross salary is withheld by the employer.

Foreign nationals working under PSAs, RSAs and HGAs are exempt from SIC.

Other – An assets tax is levied on all owners of fixed assets, with some exceptions. For individuals, the rate depends on the type of asset.

Individuals holding an investment promotion certificate are fully exempt from assets tax for relevant fixed assets for seven years from the date of obtaining the certificate.

Legal entities and individuals engaged in entrepreneurial activities with taxable supplies up to AZN 200,000 in any consecutive 12-month period and that are not registered as VAT payers may pay a simplified tax. The simplified tax is 2% of gross revenue.

Individual entrepreneurs that pay the simplified tax are exempt from profit tax, VAT, assets tax and personal income tax.

Compliance for individuals:

Tax year – Calendar year

Filing and payment – Tax returns are due by 31 March following the tax year. However, a tax return for employment income withheld at source is filed by the employer on a quarterly basis by the 20th day of the month following the end of the reporting quarter. Payers of the simplified tax and VAT must

submit the tax return annually, no later than 31 January of the year following the reporting year. Personal income taxes, which generally are withheld by the employer, must be remitted to the state budget within 20 days of the following month.

Penalties – Penalties apply for late filing, failure to file or tax avoidance or evasion.

Value added tax:

Taxable transactions – VAT in Azerbaijan is similar to that in most European VAT systems, with tax levied on the supply of most goods and services and on the import of goods. VAT payers are entitled to recover the amount of VAT paid on purchases (input VAT) that exceeds the VAT received from their taxable supplies (output VAT). Electronic invoicing is required.

Rates – The standard VAT rate is 18%, although some transactions are exempt (e.g. financial services) or zero-rated.

Registration – Taxpayers must register for VAT purposes if turnover in a consecutive 12-month period exceeds AZN 200,000. If the total value of one transaction or contract exceeds AZN 200,000, the taxpayer must register for VAT purposes before commencing activities. The tax code also permits voluntary registration for VAT purposes. Where services are provided by nonresident entities that are not registered for VAT purposes in Azerbaijan, the local entity must self-assess a reverse-charge VAT and remit the tax to the state budget.

Filing and payment – VAT must be reported on a calendar-month basis. VAT payers are required to submit VAT returns no later than the 20th day of the month following the reporting month, and must calculate the VAT due to the state budget by reducing their output VAT liability by any input VAT credit.

Source of tax law: Tax Code of Azerbaijan, PSAs, RSAs, HGAs and other statutory acts

Tax treaties: Azerbaijan has signed 51 tax treaties.

Tax authorities: Ministry of Taxes

This communication contains general information only, and none of Castro & Co. International, its member firms or their related entities (collectively, “Codex International”) is, by means of this communication, rendering professional advice or services. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser. No entity in the Castro & Co. International network shall be responsible for any loss whatsoever sustained by any person who relies on this communication.

© 2020. For information, contact Castro & Co. International.