Guide to doing business in Azerbaijan
Preface

This book has been written by EY Azerbaijan to provide the busy executive with a quick overview of taxation, the forms of business entity, and business and accounting practices in the country. EY provides assurance, advisory, tax & law, and transaction services in key cities throughout the world.
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**Country overview**

According to the Constitution of 12 November 1995, Azerbaijan is a secular, democratic, presidential republic. The country is led by a president elected for a five-year term. Currently, the Republic of Azerbaijan is governed by President Ilham Aliyev. The First Vice-President of Azerbaijan is subordinate to and appointed by the President. Presently, the Vice-President of Azerbaijan is 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 single 125-member chamber Milli Majlis (the National Assembly), which is elected for a five-year term. Milli Majlis may not be dissolved by the President; however, the President is able to veto its decisions.


**General statistics***

<table>
<thead>
<tr>
<th>Population</th>
<th>9.7 million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Territory</td>
<td>886,600 square kilometers (approx. 34,000 sq. miles)</td>
</tr>
<tr>
<td>Neighboring countries</td>
<td>Russia, Iran, Armenia, Georgia, Turkmenistan, Kazakhstan, Turkey</td>
</tr>
<tr>
<td>Titular nationality</td>
<td>Azerbaijani (91.6%)</td>
</tr>
<tr>
<td>Ethnic minorities</td>
<td>Russian, Lezghi, Talysh, Tatar</td>
</tr>
<tr>
<td>Capital</td>
<td>Baku (pop. 2,245,800)</td>
</tr>
<tr>
<td>Other main cities</td>
<td>Gyanjda (pop. 330,100), Sumgait (pop. 336,200)</td>
</tr>
<tr>
<td>Autonomous Republic</td>
<td>Nakhichevan Autonomous Republic (pop. 444,400)</td>
</tr>
</tbody>
</table>

*Source: http://azstat.org/
Economic structure

Vast oil reserves attract foreign investment to the Azerbaijani economy, and, consequentially, the oil & gas sector has become the main target of foreign investments. Several major oil contracts have been signed since 1994. Pursuant to the 2015 Azerbaijani State Statistics Committee report, foreign investments in the oil & gas sector comprised 80% (US$ 3,238m) of all foreign investments. Moreover, following the success of oil & gas projects, the government declared a policy that called for the development of the non-oil sector. In 2013, Azerbaijan achieved a fold increase of the total value of foreign investment compared with 2001. Given the rapid development of non-oil sector, the share of oil & gas investments relating to the total value of foreign investments has gradually decreased as compared with the earlier years.

On 26 May 2000, the President of the Republic 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. The Agreement on the South Caucasus Pipeline (SCP) was executed on 29 September 2001 and approved by the Law of the Republic of Azerbaijan on 26 October 2001. The SCP is the main route for transporting Azerbaijani gas to the world market.

In particular, the pipeline is used to ship natural gas from the offshore Shah-Deniz gas field to Turkey. The country owns oil refineries with technical capacity of over 22 million tons of crude oil per annum. Five big petrochemical plants, as well as two metallurgical plants, are located in Sumgait, 28 kilometers from Baku. In addition, 2 industrial and 2 high tech parks with 7-year tax holidays for entrepreneurs have been established.

Industrial and agricultural production has been stable since 1996, following four years of decline. A five-fold increase in oil production is anticipated in the future.

The President of the Republic 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. These rules set up a Commission responsible for generating proposals on establishing a favorable business environment, developing a respective legal and institutional framework, and preparing a respective action plan.
Business overview

Licensing for engaging in entrepreneurship activity

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

It should also be noted that licenses for entrepreneurship are granted for an unlimited period.

Labor licensing requirements

Foreign employees are required to have individual work permits issued by the State Migration Service. The legislation envisions a harsh penalty for employers that fail to obtain a work permit. The penalty is AZN 3,000 to AZN 4,000 for officials and AZN 15,000 to AZN 20,000 for legal entities. Management personnel of branch/representative offices of foreign companies, their deputies and foreign entrepreneurs are exempt from the requirement to obtain work permits.

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

Apart from that, foreign citizens coming to Azerbaijan for more than ten days should be registered with the State Migration Service within ten days based on an application by the premises owner where they are staying. Foreign citizens who wish to live in Azerbaijan are required to obtain a temporary residence permit before their visas expire (i.e., those entering Azerbaijan under the non-visa regime should apply for a residence permit for stays of more than 30 days). Temporary residence and work permits are issued under the so-called “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 for a one-year temporary residence permit), whereas it is AZN 1,000 for a work permit. The employer should register the signing of employment contracts, as well as their amendments and termination, electronically in the respective E-Government web-based information system using an enhanced electronic signature.

Profit repatriation

Under the Law on 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)\(^1\). Foreign companies and individuals may have both AZN and foreign currency accounts at local banks. All settlements within Azerbaijan, including the payment of an employee’s salary, should be made in AZN, with a few exceptions.

Permission from the Central Bank of Azerbaijan is required in order to collect revenues in foreign currency on the territory of Azerbaijan.

\(^1\) Information on foreign versus AZN currency exchanges rates can be found on the website of the Central Bank of Azerbaijan (www.cbar.az)
Land ownership

Land ownership in Azerbaijan is governed by the Law on Land Reform adopted in 1996, the Law on the Land Market, the Civil Code, and the Land Code adopted in 1999, as well as other laws, decrees and legal acts. Azerbaijani citizens and legal entities are permitted to own land. Foreign individuals and legal entities cannot acquire land in Azerbaijan but they can enjoy other rights, such as the right to lease land. Legal entities can purchase residential premises together with the land on which they are located.

Establishing a business

The Foreign Investment Laws provide the legal framework for foreign investment in Azerbaijan. The Foreign Investment Laws stipulate the types of entity in which foreign companies can invest, the rules governing the repatriation of profit and earnings, 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 of an existing company
- Establishing a joint venture with Azerbaijani companies and individuals
- Entering into other acceptable forms of investment agreements.

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. Business presence is registered by the Ministry of Taxes.

Registration with other state authorities is not required, as this will be done by the Ministry of Taxes based on the “one-stop-shop” principle.

Types of business presence

The Civil Code of Azerbaijan and the Law on Protection of Foreign Investment provide for the following types of commercial legal entity in which a foreign individual or legal entity may participate:
- Open and closed joint stock companies (JSCs)
- Additional and limited liability companies (LLCs)
- General and limited partnerships
- Public legal entities

Foreign companies may also open a representative office or a branch in Azerbaijan.

Joint-stock companies (JSCs)

JSCs are regulated by the Civil Code of Azerbaijan. A JSC is established by at least one legal entity or an individual. A JSC shareholder’s liabilities are limited to the amount of its shares’ value. 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 can be founded by one or more legal entity or individual with the founding members having a portion of capital/interest in the LLC equal 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. Participation interest in LLCs can be freely transferable to third parties, unless provided otherwise under the Charter of the LLC.

Partnerships

General and limited partnerships are governed by the Civil Code of Azerbaijan. 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 or individual entrepreneurs with at least one partner having unlimited liability.

Public legal entities

Public legal entities can be founded by the executive authorities designated by the President of the Republic of Azerbaijan on behalf of the government or by respective municipal bodies on behalf of municipalities. Further, public legal entities may be founded by other public legal entities in case their charters envisage such authority. The charter funds of public legal entities are formed by the assets provided by their founders. The government and municipalities are not responsible for the obligations of the public legal entities founded by them and bear risk for business losses only to the extent of the assets contributed by them.

Other types of business presence

Foreign companies may operate in Azerbaijan without establishing a local legal entity by registering a branch or a representative office with the Ministry of Taxes. Branches and representative offices are allowed to conduct commercial activities in Azerbaijan.
Introduction

There are currently three separate and distinct tax regimes that are applicable in Azerbaijan. These are the statutory tax regime, the tax regime applicable to oil & gas and mining companies operating under Production Sharing Agreements (PSAs), and the tax regime for companies working under Host Government Agreements (HGAs) on the Main Export Pipeline and the South Caucasus Pipeline. The general profit tax regime is applicable to all entities operating in Azerbaijan beyond the scope of the PSA and the HGA regimes, i.e., outside the oil & gas regime. 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 Azerbaijan. 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 that cover 20+ production sharing agreements that have been ratified by the Milli Majlis. The PSA regime generally applies to all contractor parties under the production sharing agreements and their direct and indirect foreign subcontractors. The HGA tax regime applies to enterprises working on the Baku-Tbilisi-Ceyhan oil export pipeline and the South Caucasus Pipeline. For a complete summary of the two tax 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 that was introduced on 1 January 2001 and amended as of 30 December 2016. 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, legislation envisages social fund contributions and other taxes and charges (e.g., excise tax, property tax, road tax, land tax).

Corporate Taxation

Permanent Establishments (PEs)

The Tax Code defines a PE as an entity conducting commercial activities for 90 days in any twelve-month period.

However, despite this definition, the Tax Code also provides that entities conducting exclusively any or all of the following specific activities will not create a PE in Azerbaijan:

- Storage and display of goods
- Storage of goods for the purposes of processing by another entity and subsequent export from Azerbaijan
- Purchase of goods for own use and the collection of information
- Any other preparatory or auxiliary activities.

Foreign companies not creating a PE are subject to withholding tax (see below) at the source of payment on any taxable income received from the Azerbaijani sources.

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

Profit tax

The following entities are generally subject to profit tax in Azerbaijan:

- Azerbaijani companies, with or without foreign ownership
- Branches of foreign legal entities
- Representative offices of foreign enterprises undertaking commercial activities in Azerbaijan
- 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 performed in Azerbaijan.
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
The annual income disclosed in the company’s Azerbaijani statutory accounts is reduced for all business expenses except for those specifically disallowed by the Tax Code. The most significant items of nondeductible 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 connected with the provision of “therapeutic nourishment”, milk and similar foodstuffs to employees that are deductible up to certain limits)
- Business travel expenses in excess of the statutory limits.

Capital gains
Capital gains arising from the disposal of tangible and intangible assets are calculated as the difference between the selling price and the net book value (depreciated value) of an asset (without VAT). Capital gains are included in taxable profit and are therefore taxed at the basic rate of 20%.

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

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 the PEs of foreign companies are subject to 10% tax at the source of payment.

Depreciation charges
All assets which have a residual value of more than AZN 500 and which have a useful life of more than one year need to be capitalized and expensed through depreciation. The depreciation rates adopted in Azerbaijani legislation 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:

<table>
<thead>
<tr>
<th>Type of assets</th>
<th>Rate of depreciation (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buildings</td>
<td>7</td>
</tr>
<tr>
<td>Machinery and equipment</td>
<td>20</td>
</tr>
<tr>
<td>High-technology products</td>
<td>25</td>
</tr>
<tr>
<td>Means of transport</td>
<td>25</td>
</tr>
<tr>
<td>Livestock</td>
<td>20</td>
</tr>
<tr>
<td>Geological and exploration costs</td>
<td>25</td>
</tr>
<tr>
<td>Intangibles</td>
<td>10 (for those with an undetermined period of use)</td>
</tr>
<tr>
<td>All other assets</td>
<td>20</td>
</tr>
</tbody>
</table>

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

Transfer pricing rules
The Rules on the Determination and Application of Transfer Prices (the “Rules”) have been adopted by the Ministry of Taxes effective from 2017. The Rules are applicable to the transactions exceeding the threshold of AZN 500,000 and are used for the purposes of corporate income tax calculations. The taxes might be recalculated with respect to the transactions between the following persons:

- A resident of Azerbaijan and its related non-resident affiliate;
- A PE of a non-resident in Azerbaijan and the non-resident itself or any of its representative offices, branch offices or divisions located in other countries;
- A resident of Azerbaijan and/or a PE of a non-resident in Azerbaijan and entities incorporated (registered) in countries with a favorable tax regime.

The transactions defined above are called “controlled transactions”. The “Transfer price” itself is defined as an average price established by dividing the sum of prices set in comparable transactions executed under the same terms between other parties (i.e. other than those transacting at the transfer price) by the number of such transactions. As a general principle, in case the prices of the goods (works, services) purchased or carried out under the controlled transactions by a taxpayer do not correspond to prices in comparable
uncontrolled transactions conducted under the same or similar conditions at arm’s length, the taxpayer and the tax authority will calculate the tax from the transaction based on transfer prices. The Tax Code also defines certain methods for determining the transfer price in case no information on comparable transaction prices is available. However, it should be noted that the concept of transfer pricing is new to the Tax Code and there is still a fair amount of uncertainty about its practical implementation.

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

Market prices
In the event of import and export operations, barter transactions, transactions between related parties, transactions where the used price varies from market prices by more than 30% within 30 days and when the property is insured for amounts exceeding its residual value and if it is necessary to establish for tax purposes a minimum amount of monthly rent of real estate (except housing) the taxes may be recalculated based on the market price.

Declarations and payments
Corporate profit tax is calculated on a calendar year basis. All taxpayers have to submit their declarations no later than 31 March of the following year. The deadline may be extended for 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 they can be calculated as the ratio of the previous year’s tax to that year’s annual income applied to the latest quarterly income. The final payment of the balance is due no later than 31 March of the following year. Failure to comply can lead to penalties (for a detailed overview 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.

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 participation interest in an Azerbaijani company, any income from employment in Azerbaijan, etc. The place of payment in determining the source of income is irrelevant.

Rates
Income earned as a result of non-entrepreneurial activities is subject to the following marginal income tax rates:

<table>
<thead>
<tr>
<th>Monthly taxable income</th>
<th>Tax rates</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to AZN 2,500</td>
<td>14%</td>
</tr>
<tr>
<td>Over AZN 2,500</td>
<td>AZN 350 + 25% of the amount exceeding AZN 2,500</td>
</tr>
</tbody>
</table>

Individuals whose monthly income is less than AZN 250 are exempt from tax on the portion of their income equal to the minimum living wage of the country’s working population, which is currently AZN 155. Individuals whose annual income is less than AZN 30,000 are exempt from tax on the portion of their income in the amount of 12 times the minimum living wage of the country’s working population. Individuals deriving income from entrepreneurship without forming a legal entity are liable to personal income tax at the rate of 20%.
**Determination of taxable income**

Virtually all forms of compensation to an employee are taxable, including hardship and cost of living allowances, payments by the employer for the education of an employee’s child, and payment of taxes on behalf of an employee, unless they are specifically exempted. Such an exemption includes accommodation and meal expenses incurred by the 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 the employee**

Both Azerbaijani and foreign nationals earning income from working in Azerbaijan must contribute 3% of their gross salary to the Social Insurance Fund. Contributions are withheld at source and remitted to the Fund by the employer.

**Capital gains and investment income**

Sales of movable assets are not generally subject to income tax unless the disposal relates to a 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 three years. Except for these two exemptions, all other gains resulting from the sale of property would be taxed according to the annual income tax rates for individuals and the profit tax rate for legal entities. Interest on deposits of individuals as well as dividends received by legal entities and individuals with taxable income from Azerbaijan are subject to VAT.

**Declarations and payments**

If a taxpayer’s sole income is from Azerbaijani sources which are subject to withholding tax at source, the individual is not required to complete an income tax declaration. 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.

The deadline may be extended for three months, provided that tax is paid in full by the original due date. Failure to comply can lead to penalties (for a detailed overview of this, see the Interest and Penalties section below).

**Value added tax (VAT)**

**Scope**

All companies involved in business and or importing goods and services into Azerbaijan are subject to VAT.

**Rate**

The standard VAT rate is 18%.

**VAT registration**

There are detailed requirements for registration and accounting for VAT, with penalties for non-compliance. Legal entities and individuals with taxable transactions exceeding AZN 200,000 for twelve consecutive months, excluding those involved in trade and public catering services, must register as VAT payers. Further, companies involved in the construction of apartment complexes should separately register for VAT and pay VAT under special rules.

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 arising from the supply of all goods and services, including imports, unless they are zero rated or specifically exempt. Barter and the free transfer 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, the purchase of goods and services under projects funded by international loans, and imports paid for with foreign financial donations. Specifically exempt goods and services include:

- Financial services
- Transactions involving currency or securities
- Publications

Generally, goods are deemed to be imported or exported if they are customs cleared. When determining the treatment of exports and imports of services, there are detailed place-of-sale rules which need to be applied. Azerbaijani VAT 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, excess input VAT may be carried forward or offset against certain other tax liabilities. Taxpayers may also petition the tax authorities for a refund of excessive input VAT. VAT on the purchase 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 providing services in Azerbaijan without establishing a PE must pay VAT for the taxable supplies in Azerbaijan. In such cases, VAT is applied through the reversed charge mechanism. In other words, it is self-assessed by the recipient of the services and remitted to the Budget.
VAT deposit accounts
Effective as of 1 January 2008, all VAT payers are required to remit VAT amounts through the designated bank accounts called VAT deposit accounts. Only VAT payments made through these accounts may be creditable against the output VAT. Such VAT is then claimed by the payer.

Electronic VAT invoices
Effective as of 1 January 2010, all VAT payers are required to issue electronic VAT invoices. The general format and information to be contained in the electronic VAT invoices, as well as the procedures for their issue, amendment and cancellation, are stipulated in the Rules on Electronic VAT Invoices.

Declarations and payments
Declarations should be filed and VAT should be remitted monthly by the 20th of the following month. Output VAT is generally recognized on an accrual basis, while input VAT is generally recognized on a cash basis. VAT on imported goods is paid separately at the point of customs clearance.

Other taxes and fees
Excise tax
Excise taxes for domestically produced hydrocarbon products range from 3% to 72%, and alcoholic beverages, from AZN 0.1 to AZN 6 per liter, while for tobacco products from AZN 4 to AZN 10 per 1000 units. Excise tax and VAT are not included in the taxable base. In addition, imported automobiles, yachts, platinum, gold and diamond are also subject to excise taxes. Excise tax for platinum is AZN 2 per gram, and it varies from AZN 0.8 to AZN 2 per gram on gold, depending on the thousand weight units, whereas the excise tax is AZN 200 per carat for diamonds. The calculation may differ depending on the diamond's size.

The tax rates for imported automobiles and yachts vary from AZN 0.2 to AZN 10 per cm³ of engine capacity. When producing excisable goods from excisable supplies, any excise tax paid on the supplies may be deducted from the excise tax due on the finished product. Declarations should be filed and payment should 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 residual 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 the property of the 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.

• Facilities that are used for environmental protection, fire safety, or civil defense
• Product-conveying pipelines, rail and motorways, communication and power transmission lines, and irrigation facilities
• Vehicles discussed in the road tax section below
• 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. The 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 crossing into Azerbaijan to transport passengers or cargo, as well as automobile gasoline, diesel fuel, and liquid gas producers and importers, pay annual road tax. The tax rates for non-resident owners of vehicles crossing into Azerbaijan to transport passengers or cargo depend on the engine volume of the vehicle. For produced and imported automobile gasoline, diesel fuel, and liquid gas, AZN 0.02 is added to the wholesale price per liter. The deadline for payment and submission of the road tax return is the 20th of the month following the reporting month.

Land tax
Companies using land are generally subject to land tax calculated as AZN 2 to AZN 20 for every 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 due is payable twice a year, no later than 15 August and 15 November of that year.

Social fund employer contributions
Employers are required to make contributions to the Social Insurance Fund in the amount of 22% of the gross payroll of local and foreign employees. These contributions are made at the expense of the employer and are deductible for profit tax purposes. The relevant reports should be filed quarterly by the 20th of the following month.

Mining tax
All companies and individuals engaged in the extracting of 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 mining resources at rates ranging from 3% to 26%. For all other taxable mineral resources, mining tax is calculated based on a certain ratio of the conventional financial unit per cubic meter of the mineral. Taxpayers are required to submit their declarations monthly by the 20th of the following month. The tax due is payable monthly by the 20th of the following month.

Simplified tax system
Companies and individual entrepreneurs that are not required to register for VAT purposes are subject to the simplified tax regime, under which tax is levied at 4% for companies and individual entrepreneurs conducting business in Baku and 2% for companies and individual entrepreneurs conducting business in other regions of Azerbaijan. The taxable base is gross income received from the sale of goods and services.
the provision of work and services, except for income subject to the withholding tax. Tax rates may differ depending on the activities conducted by the taxpayer:

- Taxpayers working in trade – 6%;
- Taxpayers working in public catering – 8%;
- Taxpayers working in homebuilding activities – AZN 45 multiplied by 4 per square meter;
- Disposal of apartments – AZN 15 multiplied by 4 per square meter;
- Tax on the disposal of land 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 tax is calculated at AZN 0.5 per square meter multiplied by indices in respect of each location and, finally, by multiplying the amount by indices in respect of each specific district as determined in the Tax Code.

Legal entities working under the simplified tax regime are exempt from property tax. Any taxpayer whose business is transporting passengers or cargo (except for international transportation) will be subject to the simplified tax at the established tax rate and not rate sand will be required to obtain what is referred to as a “distinctive number”. Taxpayers not involved in local transportation businesses and owning vehicles for their own use will need to obtain a “special distinctive number” to differentiate themselves from simplified taxpayers. Both the distinctive numbers and the special distinctive numbers should be issued by the Ministry of Transport at no cost within two or five days, respectively, of an application being submitted.

Taxpayers under the simplified tax regime must submit their declarations quarterly by the 20th of the following month. The tax due is payable quarterly by the 20th of the following month. Credit and insurance organizations, investment funds, taxpayers producing excisable goods, securities market participants, taxpayers receiving income by leasing property, taxpayers owning fixed assets whose residual value exceeds AZN 1 million at the beginning of the year, non-state pension funds and natural monopolies established by the relevant executive authorities, are not entitled to be simplified taxpayers. Additionally, companies building apartment complexes are also included in the simplified taxpayers category.

Therefore, these construction companies should pay a fixed amount of tax. There are special rules for calculating this tax for construction companies, introduced by a decree of the Cabinet of Ministers. The tax rates under this regime vary, depending on the district/region where the construction site is located.

**Interest and penalties**

Certain interest and penalties are applied for failure to comply with the tax legislation. For example, interest on outstanding tax liabilities accrues at the rate of 0.1% per day. The following list of penalties may also be applicable:

<table>
<thead>
<tr>
<th>Offence</th>
<th>Penalty</th>
</tr>
</thead>
<tbody>
<tr>
<td>Failure to register as a taxpayer with the tax authorities</td>
<td>AZN 40</td>
</tr>
<tr>
<td>Failure to file declarations</td>
<td>AZN 40</td>
</tr>
<tr>
<td>Understatement of tax liability</td>
<td>50% of understated tax</td>
</tr>
<tr>
<td>Payments from petty cash while bank accounts are under tax sanctions or penalties imposed by the tax authorities</td>
<td>50% of expenses paid from petty cash</td>
</tr>
<tr>
<td>Failure to register a foreign bank account with the tax authorities</td>
<td>100% of the revenue collected on such accounts</td>
</tr>
<tr>
<td>Failure to notify the tax authorities of the changes in a taxpayer’s registration documents</td>
<td>AZN 40</td>
</tr>
<tr>
<td>Failure to provide a list of assets (as the first step in that property’s confiscation) by the established deadline following the request of the tax office</td>
<td>AZN 100</td>
</tr>
<tr>
<td>Delay in paying VAT on the supplier/service provider invoices in accordance with the rules on payment of VAT using a designated bank account</td>
<td>50% of VAT paid in violation of the special rules</td>
</tr>
<tr>
<td>For violation of rules for carrying out cash settlements for cases when cash settlements are prohibited</td>
<td>1st time in a calendar year - 10%; 2nd time - 20%; 3rd time or more - 40% of the total transaction amount;</td>
</tr>
<tr>
<td>Purchase of goods without e-VAT invoice</td>
<td>1st time in a calendar year - 10%; 2nd time - 20%; 3rd time or more - 40% of purchased goods.</td>
</tr>
</tbody>
</table>

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

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:

<table>
<thead>
<tr>
<th>Nature of payment</th>
<th>Rate of withholding (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Insurance premiums</td>
<td>4%</td>
</tr>
<tr>
<td>International communication and freight fees</td>
<td>6%</td>
</tr>
<tr>
<td>Dividends and interest, including the interest element of financial lease payments</td>
<td>10%</td>
</tr>
<tr>
<td>Management fees and fees for other services performed or deemed to be performed on Azerbaijani territory but not connected with an Azerbaijani permanent establishment</td>
<td>10%</td>
</tr>
<tr>
<td>Rents and royalties</td>
<td>14%</td>
</tr>
<tr>
<td>The remittance of profit, derived from a permanent establishment in Azerbaijan to the head office is subject to a branch remittance tax</td>
<td>10%</td>
</tr>
<tr>
<td>Payments to offshore countries*</td>
<td>10%</td>
</tr>
</tbody>
</table>

* List of offshore countries has been approved by the President of the Republic of Azerbaijan on 11 July 2017.
Double tax treaties
The rate of withholding tax varies under the existing double tax treaties, depending on the contents of a particular treaty. The maximum rates of withholding tax are shown in the table below with regard to the current double tax treaties.

<table>
<thead>
<tr>
<th>Payee resident in</th>
<th>Dividends (%)</th>
<th>Interest (%)</th>
<th>Royalties (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>5/10/15</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Belarus</td>
<td>15</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Belgium</td>
<td>5/10/15</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Bosnia and Herzegovina</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Bulgaria</td>
<td>8</td>
<td>0/7</td>
<td>5/10</td>
</tr>
<tr>
<td>Canada</td>
<td>10/15</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>China</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Croatia</td>
<td>5/10</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Czech Republic</td>
<td>8</td>
<td>0/5/10</td>
<td>10</td>
</tr>
<tr>
<td>Estonia</td>
<td>5/10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Finland</td>
<td>5/10</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>France</td>
<td>10</td>
<td>10</td>
<td>5/10</td>
</tr>
<tr>
<td>Georgia</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Germany</td>
<td>5/15</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Greece</td>
<td>8</td>
<td>0/8</td>
<td>8</td>
</tr>
<tr>
<td>Hungary</td>
<td>8</td>
<td>0/8</td>
<td>8</td>
</tr>
<tr>
<td>Iran</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Italy</td>
<td>10</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Japan</td>
<td>15</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Latvia</td>
<td>5/10</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Lithuania</td>
<td>5/10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>5/10</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Macedonia</td>
<td>8</td>
<td>0/8</td>
<td>8</td>
</tr>
<tr>
<td>Malta</td>
<td>8</td>
<td>8</td>
<td>8</td>
</tr>
<tr>
<td>Moldova</td>
<td>8/15</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Montenegro</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Netherlands</td>
<td>5/10</td>
<td>0/10</td>
<td>5/15</td>
</tr>
<tr>
<td>Norway</td>
<td>10/15</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Pakistan</td>
<td>10</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Poland</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Qatar</td>
<td>7</td>
<td>0/7</td>
<td>5</td>
</tr>
<tr>
<td>Romania</td>
<td>5/10</td>
<td>0/8</td>
<td>10</td>
</tr>
<tr>
<td>Russian Federation</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>San Marino</td>
<td>5/10</td>
<td>10</td>
<td>5/10</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>5/7</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Serbia</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Slovenia</td>
<td>8</td>
<td>0/8</td>
<td>5/10</td>
</tr>
<tr>
<td>South Korea</td>
<td>7</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Sweden</td>
<td>5/15</td>
<td>8</td>
<td>5/10</td>
</tr>
<tr>
<td>Switzerland</td>
<td>5/10</td>
<td>0/5/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Turkey</td>
<td>12</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Tajikistan</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>UAE</td>
<td>5/10</td>
<td>0/7</td>
<td>5/10</td>
</tr>
<tr>
<td>Ukraine</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>10/15</td>
<td>0/10</td>
<td>5/10</td>
</tr>
<tr>
<td>Uzbekistan</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>Vietnam</td>
<td>10</td>
<td>0/10</td>
<td>10</td>
</tr>
<tr>
<td>No treaty country</td>
<td>10</td>
<td>10</td>
<td>14</td>
</tr>
</tbody>
</table>
Accounting and reporting

All entities registered in Azerbaijan (Azerbaijani legal entities, representative offices and branches) are required to maintain their books and records on the territory of Azerbaijan in local currency and in accordance with 27 National Accounting Standards (NAS), which have been prepared on the basis of International Financial Reporting Standards (IFRS). One notable difference between NAS and IFRS is the use of a mandatory chart of accounts.

The Law on Accounting also stipulates that all significant entities, including credit institutions, insurance companies, investment funds and commercial organizations, which meet certain criteria, will be subject to IFRS. Others (except for small private businesses) will have to follow NAS or IFRS. Small private businesses registered as simplified taxpayers are not obliged to keep very detailed accounts and are therefore not required to follow NAS or IFRS.

Investment Incentive Certificates

Investment incentive certificates ("Certificates") entitle holders to tax and customs privileges. 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, which are as follows: certain fields of economic activity, a minimum investment amount, and certain regions where investment projects will be carried out. Accordingly, the Tax Code and the Law on Customs Tariffs outline the respective tax and duty exemptions for entrepreneurs. The following exemptions from taxes are applied during the respective duration for legal entities and individual entrepreneurs who obtain the Certificate:

- Personal income tax – 50% of an individual entrepreneur’s income acquired from the date the Certificate was obtained – for 7 years;
- Profit tax – 50% of a legal entity’s income acquired from the date the Certificate was obtained – for 7 years;
- VAT – full exemption for the import of machinery, production equipment and devices by individual entrepreneurs and legal entities from the date the Certificate was obtained – for 7 years;
- Property tax – full exemption for the respective property of individual entrepreneurs and legal entities from the date the Certificate was obtained – for 7 years;
- Land tax – full exemption for respective land plots owned or used by individual entrepreneurs and legal entities from the date the Certificate was obtained – for 7 years.
EY Azerbaijan

Introduction
EY has led projects in the Republic of 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, the capital, opened in 1994. A team of over 200 staff is 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 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 carry out US GAAP and IFRS audits for many companies, including SOCAR, BP, Azerfon, Kapital Bank, PASHA Holding, and Azersu, to mention but a few.

We provide audit services to numerous companies operating in Azerbaijan under production sharing agreements (PSAs). We audit the cost recovery reports and profit tax returns of all PSAs and perform profit tax return audits for numerous contracting parties which own interests in various PSAs.

Our statutory audit clients include Azeri MI, Caspian Shipyard Company and Caspian Drilling Company, all being joint ventures with the State Oil Company of the Azerbaijan Republic (SOCAR).

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

Tax & Law
EY is recognized as the leading tax and legal advisor in Azerbaijan. With a service line consisting of Tax and Law Partner Arzu Hajiyeva and a team of tax and legal advisors, EY gives advice on all aspects of corporate and personal tax planning and compliance, corporate, insurance, business, migration, licensing, contract and labor law. We have provided advice on local and international tax and legal issues to a number of international enterprises that have 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, legal advisory and due diligence, and participation in litigation representing clients in disputes, including before the courts and other adjudicatory bodies. Our impressive client base speaks for itself. The firm has established good contacts with key state bodies 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 ever changing 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 exceptional experience in addressing a broad spectrum of business tasks. 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 will develop each project based on the specific features of the industry and the client.

Our clients in Baku are major private holding companies and state-owned entities. Thanks to our international experience and global network of professionals, we are able to team with specialists from all over the world to help our clients overcome market challenges and address unique business risks. Our local market knowledge and international experience allow us to provide state-of-the-art 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 partnership), 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, whether supporting a buyer or seller. We also put together the most effective restructuring plans, improving transactions to achieve your strategic goals.

Our services include assistance in valuing your business, financial interests, assets and liabilities, utilizing excellence in legal taxation and financial due diligence to provide you 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
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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.

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