



Your Tax and Legal Lighthouse

2017

Tax and Legal

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Baku

Foreword

Dear reader,

This brochure has been prepared to provide a brief economic overview of Azerbaijan and to introduce the important tax and legal issues for those planning to do business in Azerbaijan. We particularly draw your attention to the short discussion on the benefits of investing in the separate economic zones.

Azerbaijan's tax and civil legislation is constantly developing and there is sometimes no clear answer to what might be considered a simple question. Therefore, court cases and actual legal practice are important sources for interpreting legislation.

This brochure is not intended to provide tax or legal advice for any specific person or situation. Readers considering business ventures are strongly advised to seek professional assistance from advisors with experience in Azerbaijan.

About KPMG

KPMG is one of the world's biggest advisory, audit, and tax and legal firms; one of the global 'Big Four' companies. KPMG provides audit, tax and advisory services via our global network of professional firms. The company employs over 162,000 outstanding professionals who work together to deliver value in 155 countries worldwide.

KPMG has been operating in Azerbaijan since 1997 through a fully functioning office. In 2011 KPMG has entirely renewed its office and hired new professionals who are professionals of financial services in Azerbaijan. KPMG Azerbaijan has more 80 professionals of which 20 professionals has 8-20 years of audit and advisory experience in Azerbaijan, Russia, Germany, Turkey, Georgia and other countries.

In the CIS, KPMG now has offices in Baku, Moscow, Ekaterinburg, Kazan, Krasnoyarsk, Nizhny Novgorod, Novosibirsk, Perm, Rostov-on-Don, Saint Petersburg, Almaty, Astana, Atyrau, Bishkek, Kyiv, Lviv and Tbilisi employing together over 4000 people.





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Baku

Introduction to Azerbaijan

Macroeconomic insights

Azerbaijan is an oil-rich post-Soviet Union country situated in the Caspian Sea basin. Country has oil and gas reserves, developing industrial sector and fertile agricultural land. Heavy (aluminum mining and refining, metallurgy, petroleum extraction and refining and etc.) and light industries (textiles, food processing and etc.) are presented in the market. The country had a GDP of a total of USD 37.58 billion in 2016, mainly formed by the income from operations in oil and gas fields, which has decreased by 3.8 % due to cutback of production in construction area by 27.6 % and declining oil prices. The country enjoyed rapid growth from 2007 to 2009, following completion of the Baku-Tbilisi-Ceyhan oil pipeline in May 2006, whereas remaining main economic driver alongside with Baku-Novorossiysk and the Baku-Supsa Pipelines. By the completion of Southern Gas Corridor between Azerbaijan and Europe, revenues from gas exports are expected to be increased.

In February 2015, the drop in oil prices put pressure on the Central Bank's foreign currency reserves. The Central Bank of Azerbaijan subsequently devalued the Manat (AZN, the national currency of Azerbaijan), by 35%, as it replaced the hard peg to the USD with a euro-dollar basket. Now the exchange rate has stabilized at around 1 USD - 1.55 AZN (for more detailed information please refer to the website www.cbar.com).

"Strategic Road Maps on the national economy and main sectors of the economy" is a document which is expected to increase development of non-oil sector of Azerbaijan through sustainable and competitive environment, particularly agriculture, logistics and tourism. The document was approved in December 2016 and its content is still being evaluated by experts for the most precise implementation. The long-term development of economy depend on diversification of economy and non-oil sector, export of growing gas production and oil prices worldwide.

The investment climate in Azerbaijan is developing steadily, although considerable challenges remain. The Nagorno-Karabakh conflict and lack of foreign investment into non-oil sector of Azerbaijan are dragging its economy down. Another major issue is corruption in both public and private sectors, whereas several efforts have been made to combat this, such as creation of "ASAN" one-stop window concept for government services and improvement of customs work.

The Azerbaijani Government has set diversification of the economy, the attraction of foreign investment, integration with the global marketplace and sustainable growth as priorities. In support of this, investment into the country enjoys the environment created by the USD 5033.1 MM Central Bank reserves and USD 34790,9 MM oil fund reserves.

In order to facilitate diversification, the government has established the Azerbaijani National Entrepreneurial Support Fund. The Fund mainly works to provide entrepreneurs with low interest loans, with 82% of its loans used to develop the agricultural sector, while the remaining 18% is assigned to other, non-oil industries.

Introduction to Azerbaijan

Country facts

Country snapshot

Capital:

Baku (pop. 2,204,200)

Area:

86,600 sq km

Population:

9.6 mln

President:

Ilham Aliyev

Currency:

Manat (AZN)

Neighboring countries:

Russia, Iran, Armenia,
Georgia, Turkmenistan,
Kazakhstan, Turkey

Titular nationality:

Azerbaijani (91%)

Ethnic minorities:

Russian, Lezghi, Talysh, Tatar

Other main cities:

Ganja (pop. 328,400)
Sumgait (pop. 332,900)

Autonomy:

Nakhchivan Autonomous
Republic (pop. 439,800)

Living and working in Azerbaijan: Useful tips

Learn Azerbaijani. It is not only useful for everyday communications (many street vendors, waiters and shop assistants do not speak English. Russian language can be used in some cases) but also for business. Even if you conduct your meetings in English or via an interpreter, it can be useful to know how you are being translated and to understand what is left untranslated.

Develop personal relationships. They are quite important in Azerbaijani business. Rewards do not always come in cash, but it always pays to be a sociable, reliable individual.

Personal safety is not a problem. Baku is as safe as, or safer, in terms of street violence, than other major Western cities. Although walking around the suburbs late in the evening or on days when there are football matches is ill advised, as in other major Western cities.

Beware of traffic. Expats should select drivers for themselves and their children carefully and make sure they are competent and extremely patient. Expats who drive or walk should exercise extreme caution, because cars can make illegal and unexpected manoeuvres at any time.

Qualified medical services are available. While there are many qualified doctors in Azerbaijan, expats often prefer doctors who speak English or their native language. There are several western medical clinics in Baku.

Good food. There are many quality restaurants in Baku (and elsewhere).

If you are coming to stay:

- Qualified (even English-speaking) household help can be found easily through other expats.
- There are English, French and other foreign language schools catering to expat children in Baku (as well as some other cities), although there is likely to be a less diverse choice of schools and curricula than in your home country.

Routine issues:

- As an expat (except those with a 'highly qualified' visa status), you must register and unregister each time you travel abroad or outside of your place of residence in Azerbaijan.
- To pay some bills, you must physically go to a certain bank and pay cash. Fortunately, cash machines are readily available.
- Registering your car can take 1-2 days of your or, hopefully, your driver's time (but your driver can only register your car for you if you have spent the time and money to grant the driver a power of attorney over your car. The power of attorney must be updated 2-3 times annually). While the above does not cover all of the aspects of living in Azerbaijan, it is enough to infer that expats can and do live safely, successfully and happily in Azerbaijan, even for long periods.

Starting Business in Azerbaijan

Overview of commercial legal entities in Azerbaijan

The procedures by which a legal presence is established in Azerbaijan are given predominantly in the Civil Code of the Republic of Azerbaijan and the Law "On State Registration and the State Register of Legal Entities". In order to simplify the registration process for commercial legal entities, as well as branches and representative offices of foreign legal entities, President Ilham Aliyev signed an Order in October 2007 introducing registration of new commercial entities via a "One-Stop Shop" mechanism. This system allows commercial entities to be registered within 2 business days by means of a simplified submission procedure. The Azerbaijani Ministry of Tax is the authorised body which registers commercial legal entities in Azerbaijan.

Foms of establishing legal presence in Azerbaijan

Investors have to choose the form of establishment for their legal presence in order to do business in Azerbaijan. Azerbaijan's civil legislation allows several types of commercial entity to operate in Azerbaijan. They are:

- Limited Liability Companies (LLC)
- Branches of foreign legal entities
- Representative offices of foreign legal entities
- Joint Stock Companies:

- Open Joint Stock Companies (OJSC) and Closed Joint Stock Companies (CJSC)
- Additional Liability Companies (ALC)
- Partnerships
- Cooperatives

Limited Liability Company ("LLC")

The LLC is one of the most widely used company types to perform commercial activities in Azerbaijan. The LLC is a legal entity that can be formed by one or more physical and/or legal entities. The liability of those participating in an LLC is limited to their ownership stake, which means that their liabilities can only extend to the amount of their contribution to the charter capital. Moreover, while the members in an LLC are not liable for any of its obligations, the LLC in its turn is not liable for any of its members obligations to third parties. The LLC is required by law to appoint an independent auditor to verify its annual financial reports.

The share capital of an LLC is composed of assets that secure the minimum amount of its creditors' contributions. Another distinctive feature of this legal form is the absence of any minimum capital requirements.

Moreover, the sale of stakes in the LLC to third parties can be limited by the LLC's charter.

The charter capital of a newly established LLC may consist of investment belonging to local as well as foreign individuals/legal entities. Unlike other forms of legal entity, LLCs can engage in any type of business activity permissible by law.

Baku:
Heydar Aliyev square

¹ Effective as of 1 September 2000

² Effective as of 9 January 2004

Representative offices and branches

Under Azerbaijani legislation, branches and representative offices of foreign legal entities are not considered as legal entities. From a practical standpoint, branches and representative offices are similar in legal nature. Civil legislation defines representative offices as divisions of legal entities that represent and protect the interests of that legal entity in another country. However, a branch is defined as a division of a legal entity that carries out all or some of the functions of that legal entity in another country, including (but not limited to) representing and protecting its interests. Consequently, civil legislation states that representative offices cannot engage in commercial activities.

It should be noted that the Constitutional Court of the Republic of Azerbaijan in its Resolution on Interpreting Article 17, Section 5 of the Law "On Entities" ruled that if a charter confirmed by foreign legal entity allows its representative offices to conduct commercial activities, then the representative office can perform commercial activities in Azerbaijan. Therefore, in practice, representative offices can perform the same activities as branches.

Legislation subjects both representative offices and branches to the same legal, tax, currency

and reporting requirements. It is worth noting that salaries for foreign employees at branches and representative offices can be paid by head office to their overseas accounts.

Branches are free of the requirement to have a minimum charter capital. In addition, branches and representative offices cannot be re-organised (via mergers, divisions, or acquisition) into another legal form.

Joint Stock Company ("JSC")

In accordance with the requirements of Azerbaijani legislation, Joint Stock Companies can be either Open or Closed JSCs.

Open Joint Stock Company

An Open Joint Stock Company (OJSC) is a company with charter capital divided into a certain number of shares. OJSCs can be established by one or more physical or legal persons, and have shares that can be openly sold to the public and acquired by third parties without restriction. OJSC shareholders are not liable for their company's obligations; moreover, the liabilities of shareholders in an OJSC are limited to their shareholding, which means that their liabilities can only extend to the amount of their contribution to the charter capital.

The charter capital amount of an OJSC should be no less than AZN 4,000. The general meeting

of shareholders is the supreme supervisory body of an OJSC, and it must convene at least once a year.

The Charter of an OJSC must state: the name of the legal entity, its address, its main activities and the legal entity's deregistration rules, the types of securities it has issued and their quantity and individual price, and the amount of charter capital.

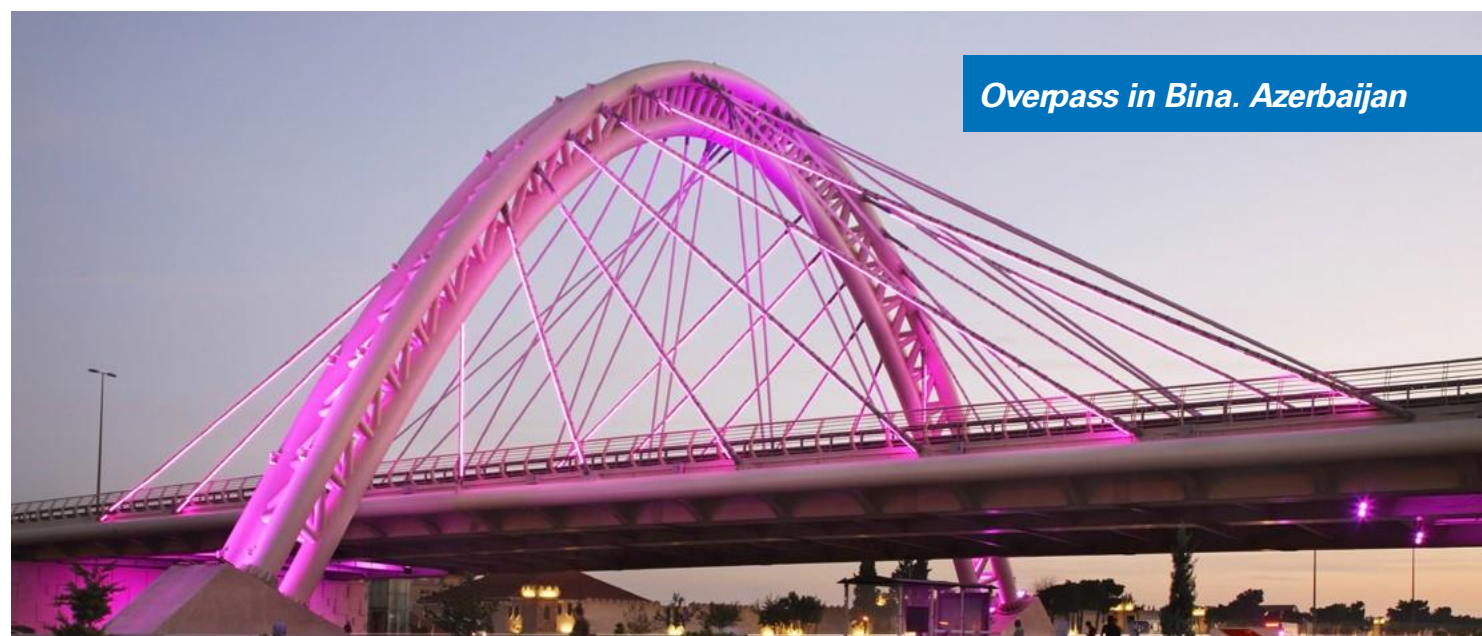
An OJSC is required to appoint an independent auditor to audit its annual financial reports. In addition, its annual financial reports must be published.

Initial Public Offerings (IPO) have been more popular recently among companies in Azerbaijan, demonstrating the growing relevance of the OJSC as a legal entity within the business community of Azerbaijan.

Closed Joint Stock Company

A CJSC has many common features with the OJSC, though several distinctions divide them:

- Shares in a CJSC are circulated among its shareholders and within a pre-determined group
- The minimum charter capital amount for a CJSC is AZN 2000;
- Shares in a CJSC can be sold to third parties if they are not bought by other shareholders under pre-emptive rights or by the CJSC itself;



Overpass in Bina. Azerbaijan



Baku: TV tower

- A CJSC with more than 50 shareholders must be reorganised into an OJSC within one year.

Subsidiary

Azerbaijani legislation provides no definition for the word “subsidiary”. However, Azerbaijani legal entities established by foreign legal entities are considered subsidiaries.

The most commonly registered Azerbaijani legal entity is either a Limited Liability Company or Joint Stock Company, with the Limited Liability Company considered the best option for conducting business.

Additional Liability Company (“ALC”)

An ALC is a legal entity that can be established by one or more persons, with charter capital divided into a certain number of stakes as defined in its charter. An ALC shares similar features with those of an LLC, though the liabilities an ALC’s participants are exposed to from the company can exceed the amount of their contributions. This is regulated by the charter.

Partnership

A partnership is a form of legal entity established by one or more of its members with its charter capital divided into a specific number of either general or limited stakes. A partnership possesses several distinctive features regarding the requirements for its founders, its liabilities, and its governance. The Civil Code states that only entrepreneurs and/or commercial entities may establish a general partnership. In addition to this, general partners continue to owe liability towards it even after withdrawing from the partnership. Members (general partners) are jointly and severally liable for the partnership’s liabilities.

Cooperative

A cooperative is a voluntary union that can be founded by at least five individuals and/or legal entities with the purpose of satisfying the

material and other needs of the participants through consolidation of the participants' material contributions. Cooperatives may be of different categories, such as production cooperatives, consumer cooperatives, and others.

Cooperative Membership

Members of a cooperative must make their respective contributions to the share fund in full before it is registered with the state. If, in the results of the fiscal year, a cooperative reports financial losses, the members must cover these losses by making additional contributions in the two months following the date on which the annual balance sheet is approved. Any individual who joins a pre-existing cooperative is liable for that cooperative's obligations unless the charter of that cooperative stipulates otherwise. Individuals intending to join a cooperative must be informed of any obligations in advance.

A cooperative's profit is divided between the members of the cooperative in proportion to their contributions. In addition, the profit of a cooperative may be used to settle creditors' debt, to pay dividends, and for any other matters as regulated by the charter of the cooperative.

Registration

LLC

An LLC is established upon the adoption of an agreement / resolution of the founders at an incorporation meeting. At the same meeting, the charter is also approved and adopted. In order to operate as a legal entity, the LLC must register with the state authorities in Azerbaijan, and this is done by submitting an application package with the LLC's corporate documents to the Ministry of Tax. LLCs are registered within 2 working days following submission of all the required documents to the registration body.

Please note that LLCs established through a local investment are registered via submission of an e-application within a day.

JSC

A JSC is established when a meeting of its incorporators adopts a resolution to establish a company. The JSC's charter is adopted at the same time. JSCs, like other commercial legal entities, are registered by the Ministry of Tax within 2 working days after submission of all the required registration documents has taken place. Similar to LLC registration processes, in order to register a JSC in Azerbaijan, the founders have to submit an application form along with specific documents depending on whether the founders are physical persons or legal entities, either foreign or local.

As LLCs, the full value of a JSC's shares must be paid for prior to its registration (except for cases where an LLC's charter specifies otherwise). In addition to this, a JSC's shares must be registered separately with the Financial Markets Supervision Chamber within 20 business days via the central depository.

Branch or Representative Office

The registration process for branches and representative offices is similar to that for legal entities. They are also registered via the Ministry of Tax's One-Stop Shop within 2 working days following the submission of all the required documents.

It is important to note that branches and representative offices function on the basis of regulations similar to the charters of other legal entities. All documents issued outside Azerbaijan must be certified and apostilled / legalised. However, not all countries' apostilles are recognised in Azerbaijan, and therefore all documents that cannot be apostilled must accordingly be legalised. Additionally, all documents issued abroad in a foreign language must be translated into the Azerbaijani language and notarised by a local notary in Azerbaijan.

De-registration of companies in Azerbaijan

The liquidation and deregistration of companies in Azerbaijan happens in 2 main stages:

Stage 1.

In stage one, the founder of the company (i.e. "Head Office") adopts a decision to liquidate the branch (a "Liquidation Resolution").

The Head Office resolves, among other decisions, to appoint a liquidation commission or a sole liquidator and empowers it/him/her to carry out all of the necessary steps to deregister the company. In practice, a third party(-ies) is/are appointed by the sole liquidator or liquidation commission to perform all of the relevant actions as part of the company deregistration process (the sole liquidator and the liquidation commission are hereinafter referred to as the "Liquidator/Commission"). The Liquidator/Commission may issue to the third party(-ies) power of attorney to take all necessary actions to deregister the company. If in a foreign language, both the Liquidation Decision and power of attorney must be notarised and apostilled/legalized.

A first announcement that the company is to be deregistered, along with the procedure and deadlines for the settling of creditor's claims, must be placed in the official newspaper (the "Taxes" newspaper) within 10 (ten) days from the date of the Liquidator/Commission's appointment. This information must be published an additionally 2 (two) times with an interval of 15-20 days. The announcement is thus made to give the branch's creditors the opportunity of applying for the repayment of their loan (i.e. debt). In total, there is a period of at least sixty days from the date of the announcement during which all creditors have the opportunity of submitting claims. Appropriate notifications must be sent to all known creditors on the date the first announcement is placed in the newspaper.

In addition to the aforementioned documents, the head of the company must adopt official documents confirming the (in)solvency of the branch or engage an independent auditor to provide a report on the solvency/insolvency of the branch at least 20 days prior to adoption of the Liquidation Resolution.

The company stamp and the appropriate application form shall be submitted to the Ministry of Tax of the Republic of Azerbaijan (the "Registration Body"), along with documents confirming the (in)solvency of the branch or the independent auditor's report, within 15 days from the date of the appointment of the Liquidator/Commission.

Once the aforementioned documents are submitted to the Registration Body, the latter shall enter the submitted information into the State Registrar of Legal Entities within 5 days.

In addition, the Liquidator/Commission must submit the final tax returns to the Ministry of Tax within 30 days from the date on which the Liquidation Decision was adopted. The final tax returns must cover activities from the beginning of the year until the date of liquidation.

An application letter must be submitted with the Liquidation Decision to the Social Protection Fund requesting that the Ministry of Tax confirms that the company does not owe any debt(s) to the Fund. Once the company is cleared of owing debt, the Fund will issue a letter (a "Clearance Letter") which must then be submitted to the Ministry of Tax.

The following procedures can be performed at any time between the official liquidation announcement (i.e. Stage 1) and submission of the final package of documents to the Registration Body as stated below (Stage 2):

- Termination of employment contracts with existing employees (must be done in accordance with the relevant labour legislation requirements);

- Closure of bank accounts. After the branch's accounts have been closed, a letter from the relevant bank(s) needs to be obtained confirming this fact;
- VAT deregistration.

Audits will then be conducted by the Ministry of Tax and/or the State Social Protection Fund.

It may in practice take much more time and effort to survive these last audits, as the inspector(s) may challenge various documentation / payment orders / company tax returns, or may require additional supporting documentation / evidence. It can be several months before these audit(s) are completed and the deregistration process finalised.

Upon expiration of the period of 60 (sixty) days from the date of publication of the announcement on liquidation of the company, the Commission/Liquidator must prepare and approve an interim liquidation balance sheet that reflects information on the assets of the company undergoing liquidation and the list of creditor and debtor claims within 10 (ten) days.

Any outstanding obligations to any creditors or to the State Budget must be settled. The Commission/Liquidator shall initiate bankruptcy proceedings if the assets of the company are not enough to settle the claims of creditors.

The Commission/Liquidator shall split the remaining assets between company participants (i.e. between the company's founders) within 10 (ten) days from the date on which the final liquidation balance is adopted.

Stage 2.

The Liquidator/Commission must submit the following documents to the Registration Body within 10 (ten) days from the date on which the assets of the company founders are distributed to the founders:

- The approved final liquidation balance;
- A report containing details of the planned distribution (utilisation) of assets;
- The document confirming that the assets were divided up between the participants/ shareholders of the company;
- The original Certificate of Incorporation and Regulations / Charter of the company;
- The stamp with the inscription "undergoing liquidation";
- The clearance letters from the Customs Authorities and Social Protection Fund.

The decision to deregister the branch shall be adopted by the Registration Body within 7 (seven) days from the date all of the required documents are submitted.

Registration of changes

In accordance with the Law of the Republic of Azerbaijan *"On state registration and the state registrar of legal entities"*, any changes made to the registration documents of legal entities, branches or representative offices must be registered with the Ministry of Tax of the Republic of Azerbaijan. Applications to have changes registered must be submitted to the Azerbaijan Ministry of Tax within 40 (forty) days following the date on which the change took place. The change must be included on the application form, which must be submitted along with any other documents that prove the fact that a change has occurred.

It should be noted that the change to the documents of the legal entities, branches or representative offices is valid only after state registration. Legal entities, branches or representative offices cannot do anything based on the change before it is registered.

Lately, legislative changes have increased the fines for not submitting notifications to have

changes registered with the Ministry of Tax of the Republic of Azerbaijan within the 40-day period. The Code of Administrative Offences of the Republic of Azerbaijan sets the fine for breaching this rule from between AZN 2,500 to AZN 3,000.

Foreign investment in Azerbaijan

Foreign investment in Azerbaijan is predominantly regulated by the Law *“On Protection of Foreign Investment”*; the Law *“On Investment Activity”*; and the Law *“On Privatisation”* and the Second Privatisation Programme.

Foreign Investment

Foreign investors may engage in any investment activity not prohibited by legislation in the Republic of Azerbaijan. According to the Law *“On Protection of Foreign Investment”*, foreign investment can take the following legal forms:

- Participation in entities established jointly with legal entities or citizens of the Republic of Azerbaijan;
- Establishment of enterprises wholly owned by the foreign investors;
- Purchase of enterprises, proprietary complexes, buildings, structures, shares in enterprises, other shares, bonds, securities, and other kinds of property which, under the laws of the Republic of Azerbaijan, may be owned by foreign investors;
- Obtaining the right to use land and other natural resources, as well as other proprietary rights; and
- Conclusion of agreements with legal entities and citizens of the Republic of Azerbaijan providing for other forms of foreign investment.

Investment Promotion Certificate

Depending on the area, territory and the amount of the investment, it is possible to receive various benefits. This is achieved by obtaining an Investment Promotion Certificate. Benefits include an exemption of 50% of income tax and 100% of property and land assets' tax, as well as exemptions from customs duties. The minimum investment required for each region varies between AZN 0.1 and 10 million.

Pursuant to a Presidential Decree of 20 April 2016, the main criteria by which Certificates are granted are set out as below:

- The investment plan must include information on the investment area, amount and location;
- Confirmation must be provided that 10% of the total investment amount exists;
- A Tax Registration Certificate must be provided.

Baku: Heydar Aliyev International airport



Applications are made to the Ministry of the Economy and considered within 5 business days. The Ministry informs the Ministry of Tax and the State Customs Committee prior to the issuance of a Certificate, which takes 3 days. Once granted, the Certificate will allow the entrepreneur to access the tax benefits for 7 years.

Protection of Foreign Investors

Under Azerbaijani laws, foreign investments are provided with the following guarantees:

- Foreign investments are protected on the territory of the Republic of Azerbaijan;
- If there are legislative changes that worsen the investment climate:
 - The legislation that was in force at the time when the foreign investment was made shall remain in force for another 10 years, irrespective of the new amendments;
- Foreign investments cannot be nationalised unless the investments damage the interests of the people and state of Azerbaijan. Nationalisation is only possible via a resolution of the National Assembly. Confiscation is also possible, though only under the circumstances of natural disaster, epidemics, or other extraordinary situations following a decision of the Cabinet of Ministers. In both nationalisation and confiscation, foreign investors must be compensated.
- Foreign investors are entitled to repatriate profits, revenues, and other amounts received in connection with their investments, provided that all applicable Azerbaijani taxes have been paid.

Bilateral Investment Treaties

Azerbaijan has concluded 44 bilateral treaties on the mutual protection of investments. Azerbaijan also signed a multilateral treaty on the mutual protection of investments with the OPEC Fund for International Development on 19 November 2002, which was ratified on 9 December 2003.

Licensing requirements

Business activities that require a licence in the Republic of Azerbaijan (except for financial markets) are regulated by the Law “On Licences and Permits” of 15 March 2016 and the Rules “On the Issuance of Licences” dated 21 December 2015. These laws simplify the licensing procedures using the ‘one-stop shop’ principle.

The Law defines a licence as an official document granting the right to engage in commercial activities to legal entities and self-employed entrepreneurs. A permit is defined as an official document confirming the right to conduct entrepreneurial activity. This permit could be in the form of an approval, certification, accreditation, etc .

From now on, licences in Azerbaijan are granted for unlimited time periods by the Ministry of Economy and Industry (except the cases stated in legislation). Global recognition of licences granted in Azerbaijan, as well as of licences of foreign legal entities and their branches in Azerbaijan, could be possible via adoption of international agreements between the parties.

Application for a licence can be submitted electronically and will be

processed within 10 business days. The licence is non-transferable, meaning it can only be used by the licensee.

The list of activities that require licences has significantly been reduced to areas relating to state security, natural reserves, the environment and public health.

Once granted, the licence (or permits) will contain information on the name of the issuing authority, the licence owner, and the field of permitted activity. Licences are classified as ‘general’ and ‘special’, with ‘general’ ones granting the right to engage in all relevant commercial activities without obtaining a separate licence for each sub-category.

Holders of ‘special’ licences will need to obtain a separate licence for each activity sub-type stipulated in the licence. The suspension or termination of any one activity in a general licence does not serve as a basis for terminating or suspending any of the other activities contained in the same licence.

Applications to renew licences should be made when changes occur to the field of activity of the entrepreneur, if an entity has been re-organised, or within 15 days if the granted licence has been revoked in the manners stipulated above.

Licences can also be suspended or terminated by the issuing authority if they are not used for their permitted purpose or in other circumstances prescribed by law.

Below is a non-exhaustive list of licensable activities in the Republic of Azerbaijan, along with the respective list of state authorities responsible for issuing licenses:

| Type of licensable activity | Executive authority |
|--|---|
| Storage and disposal of radioactive and ionized waste, utilization and neutralization of toxic waste, as well as gathering of raw material of wild medicinal plants | Ministry of Economy of the Republic of Azerbaijan |
| Creation of biometric technologies and maintenance of such technologies; | Ministry of Transport, Communications and High Technologies of the Republic of Azerbaijan |
| Private Medical activities; pharmaceutical activities | Ministry of Economy of the Republic of Azerbaijan |
| Production and sale of veterinary medicines: Non-governmental phytosanitary services, including in relation to plant protection products and agro-chemicals substances | Ministry of Economy of the Republic of Azerbaijan |
| Communication services | Ministry of Economy of the Republic of Azerbaijan |
| Activities related to manufacturing and designing of data protection equipment. | State Security Service of the Republic of Azerbaijan |
| Educational activities conducted by educational institutions | Ministry of Economy of the Republic of Azerbaijan |
| Banking activities | Financial Markets Supervision Chamber of the Republic of Azerbaijan |
| Activities in insurance sector | Financial Markets Supervision Chamber of the Republic of Azerbaijan |
| Stock exchange activities; The activities of joint-stock investment funds; The activities of professional equity market participants (brokers, dealers, asset management, determination of mutual obligations (clearing), deposit, registering holders of securities, organising equity market trade). Activities on producing and selling all types of securities | Financial Markets Supervision Chamber of the Republic of Azerbaijan |
| TV and radio broadcasting activity, inter alia, Nationwide TV Broadcasting, TV Broadcasting in Baku, Regional TV Broadcasting, Nation-wide Radio Broadcasting, cable network broadcasting, regional radio broadcasting, satellite broadcasting, foreign broadcasting | National Television and Radio Council |
| Creation and maintenance of biometric technologies and maintenance of such technologies | Ministry of Economy of the Republic of Azerbaijan |
| Creation and maintenance of personal data and information system information resources of personal data and information systems, their maintenance | Ministry of Transport, Communication and High Technologies of the Republic of Azerbaijan |

Baku



Land ownership

Based on the Civil Code of the Republic of Azerbaijan (the “Civil Code”), ‘ownership’ is the subject’s right (i.e. the right of either a physical person or legal entity) – recognised and protected by the state – to possess, use and dispose of property (or of an object) belonging to him/her at his/her own discretion. Thus ownership is the aggregate of the following rights:

- the right to possess: the legally-protected possibility of possessing property;
- the right to use, defined as the legally-protected possibility of enjoying the useful features of the property (or object), as well as to obtain benefit from it; benefit from use may be expressed in the form of income, growth, or any other form;

- the right to dispose, defined as the legally-protected possibility of determining the legal fate of the property (or object).

The Civil Code attributes land plots to immovable property. It also includes in this classification land plots, separate water bodies, forests, long-standing land for cultivation and sowing, buildings, installations and other facilities closely attached to the land. The Civil Code demands that ownership rights to immovable property (including land plots) must be registered.

Documents confirming ownership rights

Based on the provisions of the Land Code of the Republic of Azerbaijan (the “Land Code”), the granting of rights to land plots owned by the state or a municipality to a legal entity or physical person must be performed on the basis

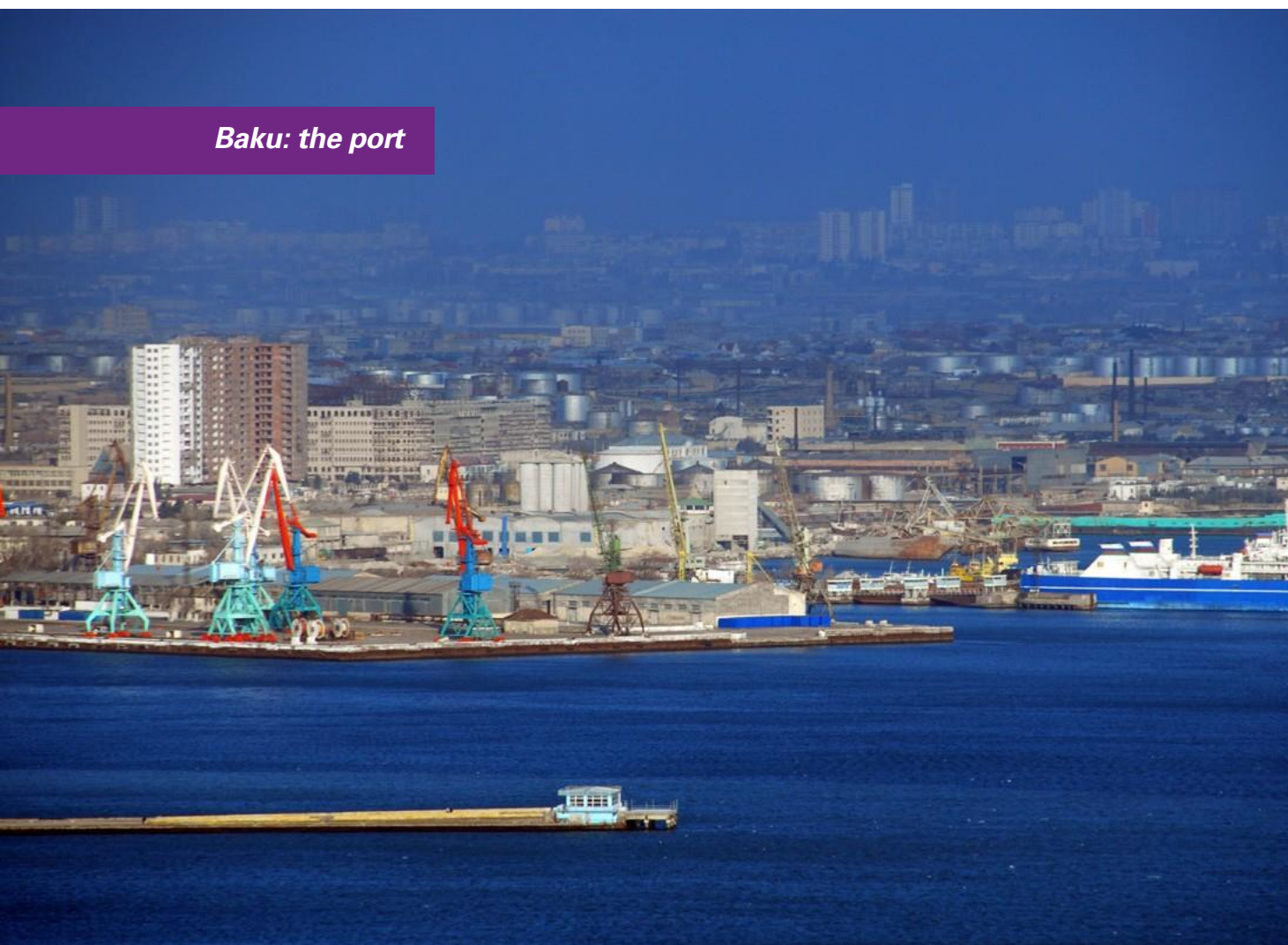
of a decree from the appropriate executive power body and following agreement between the parties.

The transfer of all rights to a private land plot from one person to another is performed on the basis of an agreement concluded between the parties. This agreement should be notarised.

Rights over land plots (except for lease and usage rights on land plots not exceeding 11 months) are registered with the state registrar of immovable property and are formalised by this same registrar.

The Land Code states that rights arising from the purchase of land plots that were in state ownership or owned by municipalities, as well as rights obtained via the conclusion of deeds related to land plots and other immovable property, must be registered.

Baku: the port



Labor Law

Introduction

Labor matters in the Republic of Azerbaijan are regulated by the Labor Code of the Republic of Azerbaijan. The Labour Code defines an employer as an owner, or person appointed by the owner as head of the enterprise, who has the authority to enter into, terminate, or amend employment agreements with employees. The working conditions provided by the employer must meet the minimum conditions provided for in labour law.

Minimum Salary and Currency of Salaries

An employee's salary may not be lower than the minimum monthly wage, which is currently AZN 116 (approximately USD 70).

The Azerbaijani Manat (AZN) is the official currency in the Republic of Azerbaijan, therefore all salaries must be paid in Manats.

Labor Books

The Labour Book is considered an official record of the employment activities of an employee.

An employer must make an appropriate notation in the labour book of his/her employee if employment lasts for more than five days. The labour book plays a key role in establishing the employee's right to state-provided pension benefits. An employee entering into an employment contract (except in cases where a contract is concluded for the first time) must provide the employer with his/her labour book. However, this requirement does not apply to forced migrants, refugees, foreigners, or stateless persons.

Probationary Period

Probationary periods must be stated in employment contracts and may not exceed three months. In some cases, there is no need for probationary periods.

Work Week

The regular work week is 40 hours, reduced for certain people groups. As a rule, overtime is not enforceable unless necessary for state defence, public safety, or to guarantee the supply of public utilities, and in certain other situations. Overtime work may not exceed the limits established in the Labour Code. For each hour of overtime work, an employee must be compensated at a rate of at least twice his or her normal hourly rate.

Holidays

The Labour Code provides for 14 public holidays and one day of mourning. If one of these official non-working days falls on a day off (Saturday or Sunday), the business day following the official non-working day is non-working. Work on official public holidays and other non-working days is compensated with higher pay. The minimum paid annual leave is 21 calendar days, or more for certain groups of employees.

Sick Leave

Compensation for the first 14 days of sick leave is provided by the employer. Compensation for the remaining days is provided by the State Social Protection Fund.

Maternity Leave

Women are entitled to paid maternity leave for 70 calendar days prior to childbirth and 56 days (70 in certain cases) after childbirth. Maternity allowance is paid by the State Social Protection Fund, not the employer.

Cost of Employment

Employers are required to pay social security contributions at a rate of 22% of salary on behalf of their employees. Additionally, employers must insure their employees against occupational illness and workplace injury. Depending on the industry



Baku: Government House

and occupational hazards, insurance premiums for this mandatory coverage vary from 0.2% to 2.0% of an employee's annual gross salary.

Employers are obliged to withhold income taxes for their employees and certain social contributions at the rate of 3% of salary on behalf of their employees.

Foreign Workers in Azerbaijan

Foreign nationals wishing to work in Azerbaijan are required to register at their place of residence and obtain a work permit. Work permits are issued by the State Migration Service. A work permit may be issued for 3 or 6 months, or up to one year. The heads of representative offices and branches of foreign legal entities (and their deputies) are not required to obtain a work permit in Azerbaijan.

⁴ Effective as of 1 July 1999

General Tax Information – Azerbaijan

Currently, the Republic of Azerbaijan has three tax regimes:

1. The Statutory Tax (Tax Code) Regime;
2. The tax regime for companies (oil and gas) working under Production Sharing Agreement (PSAs); and
3. The tax regime for companies operating under Host Government Agreement (HGAs).

- Storage and display of goods;
- Storage of goods for the purposes of processing by another entity and subsequent export from Azerbaijan;
- Purchase of goods and collection of information;
- Performance of any other preparatory or auxiliary activities;

Foreign companies not creating a PE are subject to withholding tax at the source of payment on any taxable income received from the sources in Azerbaijan.

Tax Base: The taxable base is profit, i.e. difference between income and deductible expenses.

Tax rate: 20% is the profit tax rate in Azerbaijan. 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 tax.

Deductible expenses: Expenses resulting from entrepreneurial activities, except non-deductible and/or limited expenses, are allowed by the Tax Code to be deducted from the gross income earned from these activities. Expenses not connected with income earning activity, personal expenses, and entertainment expenses are not deductible.

Financial sanctions, administrative penalties and interest for late payment as stipulated by other legislative-normative acts (excluding interest, fines and payment for material damages due to late fulfillment of obligations, and other similar fines due with regard to civil contracts) are not deductible expenses.

Statutory Tax Regime

The following are the main taxes applicable under the statutory tax regime in Azerbaijan:

- Corporate profit tax;
- Personal income tax;
- Value added tax;
- Property tax;
- Withholding tax;
- Social fund contribution;
- Other taxes

Corporate Income (Profit) Tax

Taxpayers: Both residents and non-residents are subject to profit tax in Azerbaijan. Residents in Azerbaijan are taxable on their worldwide income. Non-residents are taxable on income generated from sources in Azerbaijan.

Permanent Establishment: The Tax Code defines a PE as an entity conducting commercial activities for not less than 90 days cumulatively in any twelve-month period. However, despite this definition, the Tax Code also provides that entities exclusively engaged in any or all of the following specific activities will not create a PE in Azerbaijan:

**Tax Ministry of
Azerbaijan Republic**

The Tax Code also provides rules and limitations relating to specific deductions: interest payments subject to limitations, bad and doubtful debts, insurance reserve funds, scientific research and experimental design, depreciation of fixed and intangible assets (subject to limitations), repair (subject to limitations), insurance payments, geological exploration and extraction of natural resources.

Depreciation: All assets with residual value of more than AZN 500, and which have useful lives of more than one year, need to be capitalized and expensed through depreciation. The depreciation rates adopted in the legislation of Azerbaijan depend on the category of the assets. The following are the maximum depreciation rates by category for the most common groups of assets:

Annual depreciation rates:

| | |
|--|---|
| Buildings, construction and installations | 7% |
| Equipment and machinery | 25% |
| High tech computing machines | 25% |
| Means of transport | 25% |
| Livestock | 20% |
| Geological and exploration costs | 25% |
| Intangibles | 10% or proportionally to useful life (if known) |
| All other assets | 20% |
| Assets purchased for state entities via the investment of the State Budget | Rates above*40% |

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 future periods.

Payment and reporting: Tax payers are required to make quarterly advance (current) tax payments calculated either:

- at 25% of the previous year's tax liability; or
- by multiplying their income amount in the current quarter by the weighted tax coefficient of the gross income for the previous year. There is a formula that can explain this calculation in more detail:

$$\text{Current (Advance) profit tax} = \text{"Current quarter's gross income"} \times (\text{Last year's profit tax} / \text{Last year's gross income}).$$

The annual profit tax declaration is due no later than 31 March of the following reporting year. This deadline may also be extended for three months provided that tax is paid in full by the original due date.

Transfer pricing

Transfer prices are determined as average prices defined by way of dividing sum of the prices formed in the comparable transactions conducted under similar conditions between the parties other than the controlled persons, by the number of these transactions.

Transfer pricing may be applicable to the transactions between the following persons:

- Azerbaijani resident persons and the related party non-resident persons;
- Transactions between PE of non-resident persons of Azerbaijan and the non-residents itself or any representative offices, branches, divisions of this non-resident in other countries;
- Transactions between Azerbaijani resident or the PE of a non-resident in Azerbaijan and the persons established (registered) in offshore zones.

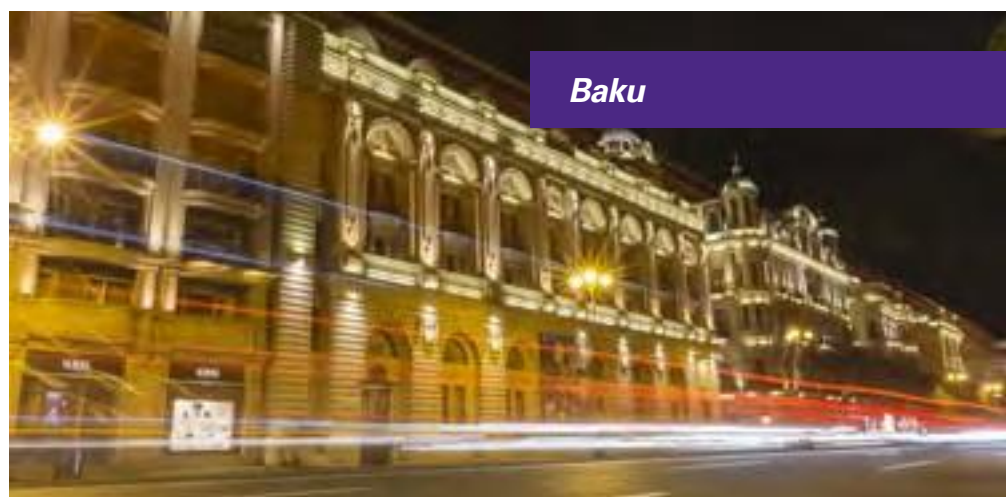
If the comparable data about separate transactions is not available and (or) obtaining information about the price of providing goods from the official sources is impossible, transfer pricing is defined by one of the following methods:

- Subsequent sale price;
- Cost plus method;
- Profitability;
- Allocation of profit.

Transfer pricing is only applied to the operations with the total amount of more than AZN 500,000. The persons conducting such operations shall submit the relevant certificate to the tax authorities no later than 31 March of the following year.

Personal Income Tax

Tax payers: Both resident and non-resident individuals are subject to personal income tax.



Resident individuals are taxed on their worldwide income. Non-resident individuals are taxed on their income from Azerbaijan sources only. Tax on Azerbaijan source income is normally paid by withholding of tax at source, at progressive rates. Income from overseas sources is, for residents, assessed on a current year basis.

Resident individuals are:

- Physical persons staying in the Republic of Azerbaijan for more than 182 days cumulatively in the calendar year.
- If the individual was present in Azerbaijan for less than 183 days in a calendar year, and was not present for more than 182 days in another State:
 - The individual will be resident in Azerbaijan if the individual has a permanent place of residence in Azerbaijan but not in another state; or
 - If the individual has a permanent place of residence in Azerbaijan and another State, or has no permanent place of residence, the individual will be resident in Azerbaijan if the individual has his or her place of vital interest in Azerbaijan; or

- If it is not possible to determine where the individual's place of vital interest is located, the individual will be resident in Azerbaijan if his or her normal place of normal residence is in Azerbaijan; or
- If it is not possible to determine where the individual's place of normal residence is located, the individual will be resident in Azerbaijan if he or she is an Azerbaijani citizen.

Non-resident individuals:

- Diplomats, their family members and personnel of international organisations registered in Azerbaijan (e.g. the UN), provided that they do not perform business activities in Azerbaijan.
- Diplomatic representations, consulates, other official representatives of foreign states, international organisations, Branches and Representative Offices of foreign legal entities not performing business activities.
- Other persons not covered by the term "resident"

PIT Rates:

| Monthly taxable income | Tax rates |
|---|--|
| Up to 2,500 AZN (approximately USD 1,470) | 14% |
| Over AZN 2,500 | AZN 350 + 25% on amounts exceeding AZN 2,500 |

The portion of employment income equivalent to the minimum living wage is exempt from taxation if the monthly income of the individual gained at the principal place of work is less than AZN 2,500. According to the respective legislation, the minimum living wage for Azerbaijan in 2017 is AZN 155.

The taxable income of individuals engaged in entrepreneurial activity is subject to PIT at the rate of 20%.

Declaration and payment: If a taxpayer's only income is from the sources in Azerbaijan subject to withholding tax at source, then the individual is not required to complete an income tax declaration.

Income tax declarations of both resident and non-resident individuals must be completed and filed no later than 31st of March of the following



tax year. Payment of tax must be made by the filing deadline.

The deadline regarding income tax declarations may be extended for three months provided that tax is paid in full by the original due date.

Value Added Tax

Commercial activities carried out in Azerbaijan, import of goods and certain services provided by the non-residents to Azerbaijan residents are subject to VAT.

Rate: The standard rate is 18%, although some transactions are exempt or zero-rated.

Registration: Taxpayers must register for VAT purposes if turnover in a consecutive 12-month period exceeds AZN 200,000. Additionally, if the total value of one transaction or contract exceeds AZN 200,000, the taxpayer must register for VAT purposes before commencing their activities. The Tax Code also permits voluntary registration for VAT purposes.

Where services are provided by non-resident entities with no VAT registration in Azerbaijan, the resident must self-assess a reverse-charge VAT and remit it to the state budget.

VAT Deposit Account: All VAT payers are required to remit the VAT amounts via designated bank accounts called VAT deposit accounts. Only VAT payments made through these accounts may be creditable against the output VAT. This VAT is then claimable by the VAT payer (subject to fulfilment of other requirements).

Failure to remit VAT later than the day of payment of the principal amount for the goods (services, works) is subject to financial sanctions of 50% on the late paid VAT amount.

Electronic VAT Invoices: All VAT payers are required to issue electronic VAT invoices. The general format, details and requisites of the electronic VAT invoices, as well as the procedures to issue, amend and cancel the invoices, are specifically prescribed by the Rules on Electronic VAT invoices.

Output VAT: Once an entity is registered as a VAT payer, it is required to charge VAT on goods provided or work / services performed in Azerbaijan. The VAT charged should be noted on an Electronic VAT Invoice.

The place of sale of goods is considered to be the place where goods are passed to the purchaser. For goods that require transportation, the place of supply is considered as the starting point of transportation.

The Tax Code defines the place of service provision for a number of service types. For advertisement and consulting services, as well as for data processing and other similar services, the place of provision of service is defined as the place of incorporation or the location of the entity receiving the work or services.

Input VAT: In general, input VAT paid to the customers (and reverse charge VAT) may be credited against output VAT.

Excess VAT (the positive difference between input and output VAT) may either be refunded or offset against other taxes. Tax refunds are very difficult to achieve in practice, though offsetting against other taxes (e.g. profit tax) is usually allowed by the tax authorities.

Declaration and payment:

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

Property Tax

Property tax is levied at the rate of 1% on 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 value at the beginning and end of the year. Property tax is deductible for profits tax purposes.

The following are specifically exempt from property tax:

- facilities that are used for environmental preservation, fire protection or civil defense purposes;
- product-conveying pipelines, rail and motorways, communication and power transmission lines, and irrigation system facilities;
- vehicles discussed under the “Road Tax” section of this publication;
- property belonging to educational, health, sport and cultural institutions used only for officially designated purposes.

Declaration and payment: Taxpayers are obliged to submit their declarations no later than 31 March of the following year. The tax due is payable in quarterly instalments by the 15th of the second month of the calendar quarter at 20% of the property tax due for the previous year.



Withholding Tax

A foreign legal entity that is not a taxpayer in Azerbaijan is subject to withholding taxes on income derived from sources in Azerbaijan at the following rates:

- 4% – Insurance payments
- 6% – Telecommunications and international transportation services, freight income
- 10% – Dividends
- 10% – Interest
- 14% – Lease payments
- 14% – Royalties
- 10% – Other income from Azerbaijani sources
- 10% – Payments to the entities established (registered) in countries or territories with concessive taxation.

Parties making the above payments to non-resident entities are required to withhold taxes at the above rates and remit it to the Azeri state budget.

As of 11 July 2017 the list of the countries and territories with concessive taxation was issued by the Decree of the President of the Republic of Azerbaijan. Below is the list of the countries and territories with concessive taxation:

- Andorra
- Anguilla
- Antigua and Barbuda
- Aruba
- The Netherlands Antilles
- Bahamas
- Bahrain
- Bermuda
- British Virgin Islands
- Belize
- Barbados
- Gibraltar
- Jersey
- Dominica
- Hong Kong (China)
- Cayman Islands
- Cook Islands
- Costa Rica
- Guernsey
- Grenada
- Liberia
- Liechtenstein

- Maldives
- Isle of Man
- Marshall Islands
- Montserrat
- Monaco
- Macau (China)
- Nauru
- Niue
- Panama
- Palau
- Seychelles
- Saint Kitts and Nevis
- Samoa
- Saint Vincent and the Grenadines
- Saint Lucia
- Turks and Caicos Islands
- Vanuatu
- Virgin Islands (USA)
- Petroleum products;
- Passenger vehicles (with the exception of motor transport means for special purposes, with special markings and equipment);
- Leisure and sports yachts, as well as other boats vehicles stipulated for the aforementioned purposes;
- All imported jewelry and products made from precious metals, as well as processed, sorted, framed and fixed diamonds are included into the list of goods subject to excise tax (since the 1st of January 2015);
- Fur-leather products.

Branch Tax (a tax on the net profit of a permanent establishment of a non-resident): In addition to the profit tax paid by the PE of the non-resident, each amount transferred from the net profit of the PE to the non-resident is taxed at 10%.

Social Fund Contributions

Employers and employees are responsible for making payments to the Social Insurance Fund. The employer pays 22% of an employee's gross salary and employee pays 3% of their gross salary. 3% is withheld from the gross salary by an employer.

Other Taxes

Mining tax – Legal entities and individuals involved in the recovery of minerals, crude oil and natural gas in Azerbaijan are obliged to pay the mining tax. The rate varies for crude oil, natural gas and minerals from 3% to 26% of the wholesale price and non-minerals from AZN 1 to AZN 10 per each m2.

Excise tax – Excise goods produced in or imported into Azerbaijan are subject to excise tax, unless said goods are specifically exempt.

The following goods are excisable goods and subject to excise tax:

- Spirits, beer and all other types of alcoholic beverages;
- Tobacco products;

Land tax – Land tax is calculated as a fixed payment for land area, regardless of the results of the economic activity of the landowners and users.

Resident and non-resident physical persons, as well as Azerbaijani and foreign companies, can be registered after obtaining documents proving their right to own or use land plots.

Road tax – Legal entities engaging in production or import of automobile fuel, diesel fuel and liquid gas and foreign nationals are payers of road tax. The road tax rate varies depending on vehicle engine volume, weight carried, litre of fuel, etc.

Simplified tax – This tax is mostly oriented towards small enterprises as well as construction sector entities. Persons not registered for VAT purposes and whose volume of taxable income for 12 consecutive months is AZN 200,000 or less are entitled to pay simplified tax. Simplified tax is charged at the following rates on the gross revenue of small enterprises:

- 4% for operations in Baku;
- 2% for operations in other regions.

Additionally, a different rate of tax is applied for the following activities:

- 6% for trade activities;
- 8% for public catering activities;
- 1% for cash withdrawal from bank accounts by legal entities and individual entrepreneurs.

For those engaged in the construction of buildings, taxable structures are residential and non-residential buildings under construction (except for parts allocated to the state), including detached private, individual residential and holiday home premises. According to the Tax Code, the total area of each floor of a constructed building is subject to taxation.

Persons engaged in house construction and supply of residential and non-residential under their ownership should pay a simplified tax at the rate of AZN 45 and AZN 15 appropriately per m² of the taxable object, multiplied by rates established by the Cabinet of Ministers, which is determined by city and district zones.

Simplified tax payers must submit a declaration on the amount of tax due to the tax authorities no later than by the 20th day of each month following the reporting period, and make tax payments to the state budget within the same period.

Customs

Import taxes: 15% is the maximum tax rate on imports. If the goods are imported temporarily for periods of less than a year and not with the purpose of deriving income from them, then they are exempt from import tax.

Export taxes: Mostly goods are free of export tax; however, there is a list of goods to which export tax applies. Currently there are various amendments to the customs legislation to ease the process of customs clearance, automation of customs procedures, etc.

Double Tax Treaties

Azerbaijan is party to conventions for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains with various countries (double tax treaties). The double tax treaties envision specific rules on taxable base, withholding rates, etc. The maximum rates of withholding taxes are shown in the table below with regard to the current double tax treaties.

| Double Tax Treaties | Tax rate for Dividends (%) | Tax rate for Interest (%) | Tax Rate for Royalties (%) |
|------------------------------------|----------------------------|---------------------------|----------------------------|
| Austria | 5/10/15 | 0/10 | 5/10 |
| Belgium | 5/10/15 | 0/10 | 5/10 |
| Belorussia | 15 | 0/10 | 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 | 10 | 10 |
| Czech Republic | 8 | 0/5/10 | 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 |
| Great Britain and Northern Ireland | 10/15 | 10 | 5/10 |
| Greece | 8 | 8 | 8 |
| Hungary | 8 | 8 | 8 |
| Iran | 10 | 10 | 10 |
| Italy | 10 | 10 | 5/10 |
| Japan | 15 | 10 | 10 |
| Kazakhstan | 10 | 0/10 | 10 |
| Korea | 7 | 0/10 | 5/10 |
| Kuwait | 0/5/10 | 0/7 | 0/10 |
| Latvia | 5/10 | 0/10 | 5/10 |
| Lithuania | 5/10 | 0/10 | 10 |
| Luxembourg | 5/10 | 10 | 5/10 |
| Macedonia | 8 | 0/8 | 8 |
| Moldova | 8/15 | 10 | 10 |
| Montenegro | 10 | 0/10 | 10 |
| Netherlands | 5/10 | 10 | 5/10 |
| Norway | 10/15 | 10 | 10 |
| Pakistan | 10 | 10 | 10 |
| Poland | 10 | 10 | 10 |
| Qatar | 7 | 0/7 | 5 |
| Romania | 5/10 | 0/8 | 10 |
| Russia | 10 | 0/10 | 10 |
| Saudi Arabia | 5/7 | 7 | 10 |
| Serbia | 10 | 0/10 | 10 |
| Slovenia | 8 | 0/8 | 5/10 |
| Switzerland | 5/15 | 0/5/10 | 5/10 |
| Tajikistan | 10 | 0/10 | 10 |
| Turkey | 12 | 0/10 | 10 |
| Ukraine | 10 | 10 | 10 |
| United Arab Emirates | 5/10 | 0/7 | 5/10 |
| Uzbekistan | 10 | 0/10 | 10 |
| Vietnam | 10 | 0/10 | 10 |

The following double tax treaties with the following countries are signed but not effective yet:

- Spain, signed on 23/04/2014
- Jordan, signed on 05/05/2008
- Israel, signed on 13/12/2016

Tax regime for companies working under Product Sharing Agreement

PSAs have been ratified by the Azerbaijani Parliament as national law and their provisions should override the provisions in Azerbaijan's statutory legislation in places where such legislation contradicts or is inconsistent with the provisions of the PSA. Each PSA and its Tax Protocols envisage specific taxation rules. Below, we outlined taxation rules under the Azeri, Chirag and Gunashli PSA.

Profit Tax

The individual liability of a Contractor Party for the Profit Tax shall be based on such Contractor Party's separate share of the items of income and deductions. The Profit Tax shall be imposed on the Taxable Profit of each Contractor Party for a calendar year at a fixed rate of 25%.

Taxable Profit/(Loss) for a calendar year shall be computed with respect to each Contractor Party as follows:

- Sales Income
- Other Income
- Expenses
- Amortisation
- Interest Costs
- Balance Profit/(Loss)

- Brought Forward Losses
- Taxable Profit/(Loss)

Each Contractor shall, beginning in the first calendar year in which it estimates it will earn a taxable profit, pay estimated profit tax for each calendar quarter based upon its estimate of its taxable profit for such quarter and for the preceding calendar quarters in such a calendar year. Estimated Profit Tax shall be paid on or before 25 days following the end of the relevant calendar quarter and shall be accompanied by a calculation in the form.

Withholding Tax

Payments to the Foreign Subcontractor (FSC) for Work and Services

The term "Foreign Subcontractor" means a subcontractor which is (i) an entity or organisation incorporated, legally created or organised outside the Republic of Azerbaijan, or (ii) a physical person or individual who is a citizen of a country other than the Republic of Azerbaijan.

According to the Protocol on the Taxation of Foreign Subcontractors, an FSC must withhold tax from gross taxable payments (less reimbursable expenditures) to Corporate Foreign Subcontractors in respect of work or services provided to it by the Corporate

Foreign Subcontractor in the Azerbaijan Republic at a rate from 5% to 10%.

"Reimbursable Expenditures" means expenditure which will not give rise to profit that is reflected separately in contracts or payment documents. These expenses include travel and accommodation expenditure, and must be supported by the provisions in contracts and/or original receipts or their copies.

In the Protocol, "work" and "services" means any activity performed in the Azerbaijani Republic by any legal entity for any other legal entity (including raw materials and elements necessary for the performance of such work and services which as a result cease to become an independent unit and are not separately provided). Work and services include but are not limited to the following activities: design work, geological research, exploration, production, drilling, extraction, modernisation, construction, engineering and various other types of technical activity, leasing immovable property, administrative, technical, legal, bookkeeping, advertising, transportation, procurement, logistics and communications, computer support, security services, consultant and financial activities, training and other similar activities. It is specifically stated that works and services do not include goods or separately provided raw materials.

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“Goods” means any tangible or intangible property (asset) including electricity and thermal energy, gas, and water.

Value Added Tax

An exemption with credit (charged at a 0% rate) from VAT on all goods, work or services under the PSA is applicable to the FSC, as according to the PSA, “Subcontractors shall be exempt with credit (at a rate of zero (0) percent) from Value Added Tax on Hydrocarbon Activities”. This will apply to the following:

- goods, works and services supplied to or by it,
- exports of Petroleum and all products processed or refined from such Petroleum;
- imports and acquisitions of goods (excluding tobacco, foodstuffs and alcohol), works and services.”

The 0% rate of VAT applies to both input and output VAT (i.e., supplies made by or to the FSC under the PSA).

For confirmation of the 0% VAT rate, the FSC should apply and obtain a 0% VAT rate certificate from the Azerbaijani Tax Authorities. The Ministry of Tax shall issue this certificate within 30 days from the date of receipt of an application from the FSC.

Personal Income Tax (PIT)

In general, according to the PSA, resident foreign employees should be subject to Azeri personal income tax only on income received as a direct result of employment Azerbaijan.

Under the Protocol concerning Taxation of Employees and Physical Persons of the Azeri-Chirag-Deepwater Gunashli Production Sharing Agreement ACG PSA, the tax residency of foreign employees is determined using the following criteria:

- 1 “Ordinary Business Purpose” Foreign Employees. The Protocol does not define the term “ordinary business purpose”, but these employees are understood to be persons with a primary place of employment outside of Azerbaijan.

This category of person would become tax resident in Azerbaijan if he/she is present in Azerbaijan for a period exceeding 30 consecutive or 90 cumulative days in a calendar year. The person would be liable to pay Azerbaijani tax on his/her taxable income as a result of his/her employment in Azerbaijan for any days exceeding 30 consecutive or 90 cumulative days (i.e. on income earned on 31st or 91st day onwards).
- 2 “Rotators” are defined as persons who are present in Azerbaijan “on a routine basis for regularly scheduled periodic employment as his/her primary place of employment and which employment is not incidental to the exercise of that primary place of employment outside of Azerbaijan”. Such persons would be considered tax resident if they have been present in Azerbaijan for periods cumulatively exceeding 90 days in a calendar year. Such persons would be liable for Azerbaijani personal income tax on all taxable income directly earned from employment in Azerbaijan, including taxable income earned during the first 90 days of their employment in Azerbaijan

The Azerbaijani personal income tax liability for each local employee and for tax-resident foreign employees is calculated at the tax rate prescribed in accordance with the Tax Code of the Azerbaijani Republic as below:

PIT Rates:

Same PIT rates apply (see above for details).

Reporting/Payment Requirements

The FSC will be liable to withhold and pay personal income tax for each Tax Resident Foreign Employee and remit it to the State Budget of Azerbaijan no later than 10 days following the reporting month.

The FSC shall also submit a quarterly declaration with regard to its tax resident foreign employees 20 days following the reporting quarter.

Social Fund Contributions

According to the PSA, the Foreign Subcontractor shall make contributions to the State Social Insurance Fund of the Republic of Azerbaijan and other similar payments (including but not limited to contributions to the pension funds, the recruitment fund, the social insurance fund, the employment fund and the medical fund) only for employees who are citizens of the Republic of Azerbaijan.

Therefore, the FSC will be liable to make payments to the Social Insurance Fund for its Azerbaijani employees. The FSC must pay 22% of the employee’s gross salary while the employee must pay 3% of their gross salary.

Import and Export Duties and Taxes

The branch shall have the right, free of any taxes, to import into and re-export from the Azerbaijan Republic all equipment, materials, and goods in relation to its PSA activity. These imports and exports would be subject only to the following customs service (procedure)/documentation fees:



| Declared Value of Shipment in Dollars | Duty |
|---------------------------------------|---|
| \$0-\$100,000 | 0.15% of value |
| \$100,001 – \$1,000,000 | \$150 plus 0.10% of value over \$100,001 |
| \$1,000,001 – \$5,000,000 | \$1,050 plus 0.07% of value over \$1,000,001 |
| \$5,000,001 – \$10,000,000 | \$3,850 plus 0.05% of value over \$5,000,001 |
| More than \$10,000,000 | \$6,350 plus 0.01% of value over \$10,000,000 |

In order to enjoy the above customs exemptions, the branch should apply for and obtain an Import/Export Exemption Certificate from the State Customs Committee.

Reporting requirements

Once the FSC has registered with the Ministry of Tax in Azerbaijan, it will be required to submit the following PSA reports:

- Value Added Tax Return (quarterly)
- Report on Withholdings from Foreign Subcontractors (quarterly)
- Statistical Committee Reports (monthly, quarterly)
- Social Funds Reports (quarterly)
- Personal Income Tax Declarations (quarterly and annual).

Should the FSC be engaged in activities other than those related to the PSA, such FSC would be required to submit a separate set of reports for each activity.

Industrial and Technological Parks

Following the success of oil & gas projects, the government has announced policies seeking to develop the non-oil sector. In 2013, Azerbaijan achieved a more than ten-fold increase in the total value of foreign investment compared with 2001.

Sumgait Technology Park (STP), launched by Ilham Aliyev, the President of Azerbaijan, on 21st December 2011, is the pioneer project in establishing Technological Parks in the region. STP is a complex of

factories and plants manufacturing different products, but benefitting from the concentrated know-how. STP is a unique project in the region, capable of meeting the demands of both domestic and foreign markets.

More than 4500 people are currently employed in the fields of production and construction-installation at STP, and once all of the planned plants have been launched, over 10,000 people more are expected to be employed, significantly improving living standards.

Another important development, High Tech Park (HTP), was launched as part of “Azerbaijan 2020: Vision of the Future”, which aims to transform the oil-based economy into a knowledge-based economy by developing a sustainable and competitive environment for Information and Computer Technology (ICT) firms. HTP has been established as a company wholly owned by the Azerbaijani Government, reporting to the Ministry of Communication and High Technology.

The Sumgait Chemical Industrial Park (SCIP), overseen by the Ministry of Economy and Industry of the Republic of Azerbaijan, includes territories designated to produce agricultural, medical, consumer, construction industry, electronics and automotive chemicals, polymers and industrial equipment.

Residents (legal entities or individuals) of industrial and technology parks that have been created in accordance with decrees from respective executive bodies (hereinafter, Parks) are exempt from the following taxes for periods of 7 years from the date on which they are registered in the Parks:

- Profit Tax for profit generated by legal entities in the Parks
- Import VAT on the import of various equipment (including technical equipment) for the development and construction of infrastructure and production areas, as well as scientific-research and conducting experiments and construction activities

- Property tax applicable to assets located in the Park
- Land Tax

The Executive Organization and Operators of the Park are exempt from the following taxes:

- Profit tax: the amount of taxable profit invested in construction and maintenance of the Park's infrastructure
- Import VAT on the import of various equipment (including technical equipment) for the development and construction of infrastructure and production areas, as well as scientific-research and conducting experiments and construction activities
- Customs duties of imported equipment and etc. upon presence of confirmation documents issued by relevant state authority
- Property tax applicable to assets located in the Park
- Land Tax

Baku: Modern high-end flagpole building



In addition, the income of physical persons (who have not registered as legal entities), and who are carrying out activities in the Park, is exempt from taxation (except personal income tax, which is applicable to salaries).

Investment promotion certificate

Exemptions and privileges related to personal income tax: Annual interest income paid from paid from the deposits of individuals in local banks and branches of foreign banks in the Republic of Azerbaijan, as well as dividends paid by issuers of investment securities, discounts, and interest are exempt from income tax for 3 (three) years effective from 1st February 2016.

- Additionally, 50% of the profit made by individual entrepreneurs who have obtained investment promotion certificates shall be exempt from income tax for 7 years from the date on which the certificates were obtained.
- Exemption from profit tax: The profit of entities that have obtained investment promotion certificates shall be exempt from 50% of income tax for 7 years from the date on which the certificate was obtained.
- Exemptions from VAT: Any entity or individual entrepreneur which has obtained an investment promotion certificate shall be exempt from VAT for a period of 7 years from the date on which the certificate was obtained upon import of equipment, technological equipment and devices which have the agreement of the relevant executive authority.
- Exemption from property tax: Any entity or individual entrepreneur that has obtained an investment promotion certificate shall be exempt from property tax for a period of 7 years from the date on which the certificate was obtained.
- Exemptions from land tax: Any entity or individual entrepreneur which has obtained an investment promotion certificate shall be exempt from property tax for a period of 7 years from the date on which the certificate was obtained.
- Technology and technological equipment imported by entities and individual entrepreneurs engaged in investment activity, as well as by resident entities and individual entrepreneurs in industrial or technology parks for the purpose of constructing production areas within the industrial or technology parks, and for conducting scientific research and development work in accordance with authorising and confirming documentation, are to be exempt from custom duties and VAT for a period of 7 years.



Miscellaneous

Non-cash settlements

Law of the Republic of Azerbaijan on Non-cash Settlements was introduced earlier 2017.

Non-cash settlements

- The settlements made via transfer from one person's bank account to the other person's bank account by use of payment tools (payment cards, payment orders, etc.) and payment means (mobile phone devices, computer and other equipment). For a transfer between tax registered parties to qualify as a non-cash settlement, such transfers shall be made by this method only;
- Settlements carried out via payment terminals;
- Settlements made by direct cash transfer to the vendor's bank account.

Limitations on cash settlements

- Taxpayers registered for VAT purposes and the taxpayers engaged in trading or catering services whose taxable turnover exceeds AZN 200,000 in any month during consecutive 12-month period are eligible to make cash settlements for up to AZN 30,000 during a calendar month. The limitation is effective starting 1 January 2017;
- Other taxpayers are eligible to make cash settlements for up to AZN 15,000 during a calendar month. The limitation is effective starting 1 April 2017.

Financial sanctions on violation of the limitations on cash settlements

Due to violation of the law on "Non-cash transactions" of the Republic of Azerbaijan tax payers will be subject to financial sanctions. The tax payers who are not compliant with the requirements of the law on "Non-cash transactions" shall be subject to:

- 10% of the amount in excess of the limits, if such violation occurs for the first time;
- 20% of the amount in excess of the limits, if such violation occurs for the second time; and
- 40% of the amount in excess of the limits, if such violation occurs for the third and more times.

Payments to be settled non-cash

- Payment of taxes, customs duties, administrative penalties and financial sanctions charged by the authorities;
- Payment of debts on leasing transactions and provision of loans;
- Salaries, pension, scholarship, financial aid, benefits, compensation, indemnity paid by the persons (except the persons with taxable operations less than AZN 200,000 in any month during the consecutive 12-month period);
- Payment of stationary phone services and utility expenses;

Baku: Building with clock



Central park of the Baku city

- Payment and reimbursement of funds bearing no interest (except for the cases where the funds are provided by the persons not registered as tax payers) and other allocations.

Advanced Tax Ruling

Advanced Tax Ruling refers to advance determination by the tax authorities of potential tax liabilities and legal results arising from application of the tax legislation to the planned operations.

In order to benefit from advanced tax ruling, application form, as well

as the relevant documents must be submitted to the tax authorities. Official duty to be paid is AZN 500 and the decision is valid for 3 years.

Decision on advanced tax ruling may be rejected in the following cases:

- The information stated in application form and documents is incompliant with the law;
- Taxable operation stated in the application form has already been completed or there is a decision of the tax authorities or court regarding this operation;
- Cost of the taxable operation is less than AZN 10,000,000.

Execution of the decision on application for advanced tax ruling for the stated operation is legally binding to taxpayer and tax authority, provided that the taxpayer will carry out this operation.

The tax payer is not obliged to carry out the operation for which the decision on application of advanced tax ruling is adopted.

Accounting

Accounting regulations are set out in the Law of the Republic of Azerbaijan "On Accounting" (March 1995). In 2004, steps to improve the transparency of financial reporting and accelerate the economy's integration into the global financial system, as well as modernise the national accounting system and reporting with respect to international standards, was taken by the Azerbaijani government.

The Law "On Accounting," adopted in June 2004, stipulates that International Financial Reporting Standards (IFRS) be adopted by organisations involved in commercial activities within Azerbaijan. The Law defines the accounting standards that different organisation types have to adopt.

Public interest entities are defined as credit organisations, insurance companies, private pension funds and legal entities with stock market share listings. Entities that meet at least two of the following criteria are also considered public interest entities: 1) with revenue of AZN 30 million (approximately US\$ 38 million); 2) an average of 1,200 employees, and 3) a total balance sheet of AZN 100 million (approximately US\$ 123 million). All public interest entities in Azerbaijan must adhere to IFRS. Commercial organisations must either follow IFRS or the National Accounting Standards for Commercial Organisations (NASCO).

Small businesses are allowed to follow simplified accounting rules approved by the Ministry of Finance. Alternatively, they may choose to follow NASCO. Small businesses are defined by looking at the size of their business in the exclusive sphere of their operations. For instance, for industry and construction, an entity with fewer than 40 employees and an annual turnover of less than AZN 200,000 is considered a small business.

NASCO regulations are largely based on IFRS (2006 release). The use of IFRS and NASCO standards became compulsory for commercial entities and public interest entities on 1 January 2008. These standards have also been in force for non-commercial organisations since January 2009.

The transition period is specified as one year for small businesses, two years for Public Interest Entities, and three years for non-commercial and non-governmental entities. The Civil Code contains general provisions on financial reporting and audit requirements for legal entities. Open JSCs and limited liability companies are required to use an independent auditor to audit their annual financial statements (Open JSCs must also publish their annual accounting reports and balance sheets). Depending on the value of the assets on the balance sheet, or annual revenues, companies are required to have their balance sheet audited.

Why KPMG

The tax and legal system in Azerbaijan is constantly changing. These changes can occur rapidly, frequently leaving taxpayers unprepared to face them. We combine our in-depth knowledge with the international experience of KPMG specialists operating in 150 different countries to offer progressive approaches to your tax and legal issues. With our help, our clients are optimising their business practices and freeing up additional financial resources to grow their businesses.

We are open to constructive dialogue and capable of providing practical solutions to any and all issues.



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