



**Taxation  
and investment  
in Azerbaijan**

2018

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# Business and investment environment

## 1. General rules on investment activity and forms of business organizations in Azerbaijan

Azerbaijani legislation defines "foreign investment" as any kind of property and proprietary rights, including the right to the results of intellectual activity and other intangible rights contributed by foreign investors for the purpose of deriving profit.

Foreign investors may make investments in Azerbaijan in the following way:

- Share participation in enterprises and organizations established in collaboration with Azerbaijani companies and individuals

- Establishment of enterprises fully owned by foreign investors
- Purchase of enterprises, buildings, equity shares in enterprises, other shares, bonds and securities, as well as other property which, according to the legislation, may belong to foreign investors
- Acquisition of rights for the use of land and other natural resources

### Privileges for and state guarantees to foreign investors

Foreign investors enjoy a legal regime that is as favorable as the one created for local investors. Azerbaijani law guarantees investors' interests from future adverse

changes in the legislation. However, this does not apply to changes in legislation concerning defense, taxation rules, national security and public order, environmental protection, credit and finance, and public morale and health.

Foreign companies may establish either a branch or a representative office in Azerbaijan. Neither branches nor representative offices constitute legal entities, but are considered to be separate divisions of the foreign legal entity they represent.

Although there is no difference between the tax treatment of branches and representative offices, a branch office is a more appropriate form for conducting commercial operations from a legal point of view. Unlike a representative office, a branch may perform commercial operations that are also conducted by its head office.

Limited liability companies and branches are the most popular forms of doing business in Azerbaijan among foreign investors.

All of the processes necessary for state registration of entities are carried out by the Ministry of Taxes of Azerbaijan according to the "one stop shop" principle. Registration of legal entities and branch or representative offices of foreign legal entities must be completed within two days. Legal entities with local shareholders can be registered immediately through a fast e-registration process while regular e-registration is completed within one day.

## 2. Authorized Capital and Contributions of Partners

According to Azerbaijani civil legislation, as a general rule, a company's authorized capital cannot be less than the amount of the company's liabilities to its creditors.

## Business organizations in Azerbaijan

Azerbaijani legislation provides for a number of different forms through which business activities may take place. They include the following:

Type of commercial organisation	Main characteristics or requirements
<b>Open or closed joint stock company</b>	<ul style="list-style-type: none"> <li>• Limited liability</li> <li>• One or more founders (an individual and/or a legal entity)</li> <li>• Charter and charter capital required</li> </ul>
<b>Limited liability company</b>	<ul style="list-style-type: none"> <li>• Limited liability</li> <li>• One or more founders (an individual and/or a legal entity)</li> <li>• Charter and charter capital required</li> </ul>
<b>General partnerships</b>	<ul style="list-style-type: none"> <li>• Unlimited personal liability</li> <li>• Charter and shared capital required</li> </ul>
<b>Limited partnerships</b>	<ul style="list-style-type: none"> <li>• Limited liability for partners and general partner(s) (unlimited liability)</li> <li>• Charter and shared capital required</li> </ul>
<b>Companies with additional liability</b>	<ul style="list-style-type: none"> <li>• Founders bear subsidiary liability established in the charter</li> <li>• Charter and charter capital required</li> </ul>
<b>Cooperatives</b>	<ul style="list-style-type: none"> <li>• Established by not less than five individuals and/or legal entities (property liability)</li> <li>• Charter and participation fund required</li> </ul>

The minimum limit of authorized capital for joint stock companies is AZN 2,000 for closed joint stock companies and AZN 4,000 for open joint stock companies.

### 3. Licensing and compulsory notification of state authorities

Certain activities in Azerbaijan (for example, banking, audit, insurance, construction, etc.) require a license/ special permit. Companies that intend to engage in activity subject to licensing should apply to the Ministry of Economy of the Republic of Azerbaijan through ASAN (Azerbaijan Service and Assessment Network) Services for a license following their state registration.

### 4. Acquisition of real estate in Azerbaijan

Any purchase of immovable property should be notarized. The title to the property is considered to have been transferred to the buyer as soon as the appropriate records have been made in the State Register of Immovable Property.

Although foreign investors, including individuals, may own immovable property, they cannot purchase land in Azerbaijan. Foreign nationals and foreign legal entities may only obtain the rights to land through a lease or use agreements.

### 5. Exchange controls, bank accounts and confidentiality of bank information in Azerbaijan

Manat, Azerbaijan's official currency, has limited convertibility. According to the Constitution of Azerbaijan, Manat is the only means of payment in Azerbaijan.

1 USD is equal to 1.7000 AZN, according to the exchange rate published by the Central Bank of Azerbaijan as at 03 April 2018.

Both residents and non-residents of Azerbaijan have the right to open and close accounts in the national or any other foreign currency. Residents and non-residents may import and exchange currency in accordance with the procedures established by the Central Bank of Azerbaijan.

Taxpayers engaged in entrepreneurial activity are obliged to notify the tax authorities about opening offshore bank accounts.

Foreign investors may repatriate their profits after paying the appropriate taxes.

Under current legislation, disclosure of confidential bank account information is prohibited. Such information may be disclosed only on the basis of a court ruling or limited cases of requirement by public authorities in accordance with the laws.

### 6. Construction activities

City building and construction activities in Azerbaijan are regulated by the City Building and Construction Code of the Republic of Azerbaijan ('Construction Code') effective from 1 January 2013, other laws and regulations, technical norms and standards (collectively, Construction Standards, available at the official website of the State Committee on Town Planning and Architecture).

Pursuant to the Construction Code, in most cases, other than for small-scale construction projects or construction projects with non-commercial purposes, construction works require construction permits and licenses to be obtained.

The Construction Code provides for specific regulations with respect to the following subjects of construction activity:

- i. customer;
- ii. project manager;
- iii. contractor.

Under the Construction Code, state authorities, municipal bodies, physical and legal entities may qualify as customers of a construction project, while the project manager and contractor are required to be legal entities registered in the Republic of Azerbaijan and holding the appropriate license.

Furthermore, the Construction Code introduces professional certification requirements for individuals involved in the following areas of construction activity:

- i. engineering/research;
- ii. project management;
- iii. construction/installation;
- iv. mechanization/ transportation;
- v. production of construction materials;
- vi. construction projects expertise.

The Construction Code provides for certification of construction products and materials, so that only certified products and materials, consistent with fire safety regulations are used in construction works. Laboratories offering certification of construction materials and products must be accredited.

### 7. Competition rules

Competition on the Azerbaijani market is regulated mainly by the Law on Antimonopoly activity ('Antimonopoly Law') and the Law on Natural Monopolies and the Law on Unfair Competition along with other supplementary laws and regulations. Antimonopoly Law provides for compulsory notification and authorization from the State Antimonopoly Services in the following cases:

- Merger/consolidation



- Where a merger/consolidation leads to the creation of entities with a market share exceeding 35%;
- Where a merger/consolidation takes place between market participants with total value of assets which exceed the value of 75 thousand times the minimum wage (AZN 130.00 as of January 2018);
- Acquisition of shares
  - Acquiring more than 20% of the voting shares (interest) of a market participant;
  - Acquiring the main production means or non-tangible assets of a market participant, provided that such property represents more than 10% of the main production means or non-tangible assets of the seller.
  - Acquiring the rights necessary to define the business and perform the functions of the highest governing management body of a market participant provided that:
- The value of the entity's total assets exceeds 75 thousand times the minimum wage (AZN 130.00 as of January 2018); or
- One of the entity's market share exceeds 35%; or
- The entity acquiring shares (interest) controls the activities of the entity transferring such shares (interest).

Furthermore, market participants with a dominant position or with special or exclusive rights or natural monopolies have to disclose the terms and prices for their goods and services and any modifications to them 30 days prior to issuing such terms and prices or modifications to them. A dominant position is defined as an exceptional position, which allows a market participant to use its economic potential to influence competition, so as to restrict access of other market participants to the market. Market participants with a market share

exceeding 35% or other figure specified by legislation are considered as entities with a dominant position.

### 8. Immigration

According to the Migration Code of the Republic of Azerbaijan effective since 1 August 2013, every able-bodied person over 18 years of any nationality (or stateless) is entitled to work within the territory of the Republic of Azerbaijan. Foreigners or stateless persons may work in Azerbaijan provided that the following conditions are met:

- i. existence of a job vacancy that is not claimed by a citizen of the Republic of Azerbaijan who has the skills and necessary qualification for such job,
- ii. the employment services are unable to meet employers' need from local labor resources. In such circumstances, employers may obtain work permit for the foreigners or stateless persons whom they want to employ.

Foreigners or stateless persons are required to have a work permit in order to work in Azerbaijan. Work permits are issued by the State Migration Service of Azerbaijan. Work permits are issued for up to one year and may be extended for unlimited number of times each being valid for a period of up to one year.

Individuals coming to Azerbaijan with the purpose of involvement in an entrepreneurial activity\*, or for business trips not exceeding 90 days cumulatively within a calendar year within specific fields of business (i.e. mining Industry; processing industry; electricity, gas, steam and air conditioning supply; information and communication; finance and insurance; education; transport; water supply, waste water and refuse treatment); heads of legal entities with foreign

investment or branches/ representative offices of foreign legal entities and their deputies are exempt from the requirement to obtain a work permit.

Employers (legal entities) who employ expatriates without obtaining work permits risk an administrative penalty ranging in the amount from AZN 15,000 to AZN 35,000.

### Temporary residence

Any expatriate visiting Azerbaijan on the basis of a visa or visa free regime may apply for a temporary residence permit on any of the grounds below:

- A close relationship with a citizen of Azerbaijan Republic (father, mother, husband (wife), children, sibling, niece and nephew, grandfather, grandmother etc.);
- Investment in the economy of the country of an amount of AZN 500,000 or greater;
- Possession of real estate in Azerbaijan or a deposit with a bank in Azerbaijan of a minimum of AZN 100,000;
- The applicant is a high-level specialist in the economic, industrial, defense, scientific, cultural, sporting or other sphere;
- The applicant is an expert, having higher education in shipbuilding area or vocational training in the relevant field with at least 1 year experience in the respective area, invited either by Azerbaijani citizens or contractors of an Azerbaijani legal entity, or the residents of Garadagh Industrial Park;
- The applicant is the family member of an expatriate temporarily or permanently residing in Azerbaijan;
- Holding the post of head or deputy head of a legal entity with foreign investment or branch/representative office of a foreign legal entity in Azerbaijan;

- Involvement in entrepreneurial activity in Azerbaijan\*;
- Obtaining a work permit;
- Full-time education in an educational institution in the Azerbaijan Republic;
- Professional involvement in a registered religious institution;
- In the cases as defined by the intergovernmental agreements of the Republic of Azerbaijan;

\* Entrepreneurial activity is exempt from work permit requirement and may serve to obtain a temporary residence permit only if an applicant undertakes business activity and has at least five full time or 10 part time employees hired with appropriate employment agreements. In such cases, at least 80% of the employees have to be Azerbaijani citizens.

### Registration upon arrival

Foreigners and stateless persons planning to stay in Azerbaijan for more than 10 days must be registered at the place of sojourn within 10 days as of the date of their arrival.

### 9. Customs

Customs relations are regulated by the Customs Code of the Republic of Azerbaijan effective as of 1 January, 2012 and other supplementary laws and regulations issued by the respective state authorities.

Under the Customs Code, legal entities may be registered as an Authorized Economic Operator, and will then be subject to simplified customs control procedures for the purposes of delivering goods in a safe and secure manner and facilitating foreign trade. The Code sets eligibility criteria for acquiring the status of an Authorized Economic Operator.

During a Customs Audit, the customs authorities may audit goods that have been previously cleared.

Under the Code, in the customs territory of the Republic of Azerbaijan ('customs territory'), customs procedures fall into two groups:

#### General customs procedures:

- export,
- re-export,
- temporary export,
- release for free circulation and
- re-import procedures.

#### Specific customs procedures:

- transit (international/domestic),
- specific use (temporary import/end use),
- processing (inward/outward),
- warehousing (temporary/customs) and
- free zone.

The legislation envisages customs exemptions for individuals and legal entities holding investment promotion certificate.

Customs preferences are listed below:

- Full exemption from customs duties upon import of technological equipment for the high priority industry sectors;
- Full exemption from customs duties upon import of technological equipment by the management organization or operator of industrial and technological parks for construction and research & development purposes for seven years from the date of obtaining investment promotion certificate;
- Full exemption from customs duties upon import of technological equipment by resident legal entities and individuals of industrial and technological parks for construction and research & development purposes for seven years from the date of obtaining investment promotion certificate.

### 10. Securities

The securities market is regulated mainly by provisions of The Civil Code of the Republic of Azerbaijan, norms and regulations issued by the Financial Markets Supervision Chamber and other related laws and regulations.

Under the Civil Code, securities fall into three categories:

- registered securities, where a security is issued in the name of a certain person;
- bearer securities, where a debtor undertakes performance of obligations in respect of any person presenting that security; and
- certificated securities.

Securities may take the form of investment securities, such as shares and bonds, and non-investment securities, such as promissory notes, deposits of mortgage and others.

Only stock companies (open and closed) may act as issuers of shares.

The following actions are considered to be issuing of investment securities:

- issuing of corporate bonds by legal entities of the Republic of Azerbaijan;
- share issues by stock companies in cases of share combination or division, or increase or decrease in nominal value of shares;
- additional share issues by stock companies in order to increase charter capital;
- issue of investment securities in cases of re-organization of commercial entities.

A prospectus is required for the public placement of investment securities or the issue of additional shares by stock companies.

A Public placement of shares is required for the issue of shares by open joint-stock companies (other than in cases where the issue is to establish or re-organize an OJSC or for share conversion) and is prohibited for closed joint-stock companies. Public placement of shares by an OJSC must be undertaken via a stock exchange.

The limitations exist there in the legislation for Azerbaijani legal entities to place investment securities outside the territory of the Republic of Azerbaijan.

For the purposes of increasing transparency, detection and prevention of abuse within the securities market, protection of shareholders rights and monitoring security transactions, a set of new regulations was adopted in 2012, which require reporting and disclosure to the Financial Markets Supervision Chamber in the following cases:

- i. report and disclosure of information on security transactions by professional participants of securities market (brokers, dealers, depositaries, registrars of securities owners and those, performing the functions of a stock exchange);

- ii. Insider trading cases, where an insider enters into an agreement with respect to the shares of an issuer with whom it has a separate relationship;
- iii. annual publication of reports on activities by issuers of investment securities;
- iv. attestation of professional participants in the securities market.

### **11. Banking issues**

The banking system in Azerbaijan comprises supervisory authority of financial markets, which is the Financial Markets Supervisory Chamber, the Central Bank of the Republic of Azerbaijan ("Central Bank") and credit institutions. Credit institutions include banks and non-bank credit institutions. Banking activity within the territory of Azerbaijan is conducted on the basis of a license obtained from the Financial Markets Supervisory Chamber.

Banks can be established by a minimum of three persons (physical or legal entities) and they are required to function as Open Joint Stock Company.

Bank charter capital is set at AZN 50 (fifty) million as of 1 January 2014 in line with the Rules on Bank Capital Adequacy ("Rules"), adopted by the Central Bank on 25 July 2012.



# Taxation system in Azerbaijan

The tax system in Azerbaijan consists of three taxation regimes:

- the statutory tax regime governed by the Tax Code;
- the tax regime established by the existing Production Sharing Agreements ("PSAs");
- the taxation regime established by the two Host Government Agreements ("HGAs") such as main Export Pipeline (Baku-Tbilisi-Ceyhan) HGA ("BTC") and South Caucasus Pipeline (Shah Deniz Gas) HGA ("SPC").

Below is a general overview of the taxes applicable under these taxation regimes.

## I. Statutory taxation

The Tax Code sets out the general taxation framework in Azerbaijan and establishes the following taxes:

- Profit tax
- Value added tax ("VAT")
- Property tax
- Personal income tax
- Mining tax
- Land tax
- Excise tax
- Road tax
- Simplified tax

## 1. Profit tax

### 1.1. Tax jurisdiction and payers of profit tax

Legal entities incorporated in Azerbaijan are normally treated as residents and are taxable on their worldwide income. Legal entities incorporated abroad are normally treated as non-residents and are taxable on income from sources in Azerbaijan.

Both resident and non-resident enterprises in Azerbaijan pay profit tax.

## 1.2. Taxation of resident entities

### Taxable base

Legal entities are taxed on profit, which is determined as gross income from economic activities less allowable deductions at a flat rate of 20%.

### Deductible expenses

The Tax Code allows some expenses incurred in the course of economic activities to be deducted from the gross income earned from such activities. Expenses not connected with income earning activity, personal expenses, and entertainment expenses are not deductible (unless entertainment is considered to be the taxpayer's economic activity). Deductions are also not allowed for the acquisition of fixed assets and intangible assets, although such assets may be depreciated.

The Tax Code also provides rules and limitations relating to specific deductions. Some specific allowable deductions are as follows: interest payments subject to limitations, bad and doubtful debts, insurance reserve funds, scientific research & experimental design, depreciation of fixed and intangible assets subject to limitations, repairs subject to limitations, insurance payments, geological oration and extraction of natural resources.

### Deductibility of interest expenses

Any interest expenses paid or incurred by the taxpayer in the course of their business activities is generally deductible. However, there are some limitations.

The deduction of interest on loans received from abroad or related parties cannot exceed the expense calculated using an interest rate of 125% of the inter-bank credit auction rate set forth by the Central Bank of Azerbaijan.

## Depreciation and amortization allowance

The Tax Code provides for a group method for the depreciation of fixed assets (except buildings, which are depreciated separately). Annual depreciation rates per group of assets are as follows:

- Buildings, facilities and installations, structures: up to 7%
- Machinery, equipment: up to 20%
- Calculation technology which is the product of high technology: up to 25%
- Means of transportation: up to 25%
- Expenses on geological exploration and preparation for the production of natural resources: up to 25%
- Other fixed assets: up to 20%
- Intangible assets
  - For those with an indeterminable period of use: up to 10%
  - For those with a determined period of use: at an annual rate, pro-rata to that determined period of use

State owned companies are limited to take depreciation deductions up to 40% on assets acquired at the expense of the state financing.

Any amount paid or incurred for the acquisition, construction or improvement of assets for business use may not be deducted immediately, but should instead be capitalized and depreciated overtime. Gains from revaluation of fixed assets are not considered in determining the value of the assets for taxation purposes.

Land, art, buildings, and facilities that are historical or architectural monuments, and other permanent assets, may not be depreciated.

### Deductibility of repair expenses

The amount of deductible repair expenses each year is limited to the amount defined as a certain percentage of the residual value of each group of fixed assets as of the previous year-end.

Those rates are defined as follows:

- Buildings, facilities and installations, structures: 2% of the residual value
- Machinery, equipment and calculation technology and transportation means: 5% of the residual value
- Other fixed assets: 3% of the residual value

Any amounts spent in excess of the limits are deemed to increase the residual value of the asset at the end of the current year.

In the event that the actual amount of repair expenses is less than the amount established by this limit, then the repair expenses can be deducted from income. In this case, the maximum value of deductible repair expenses in the following tax years is increased by the difference between the amount of actual repair costs and amount calculated in the established limit.

### Loss carry forward

The Tax Code provides the opportunity for taxpayers to carry losses forward. Losses can be carried forward for up to five years and offset against other years' profits without limitation.

### Tax accounting rules

Taxpayers are required to maintain accurate and up-to-date records of their income and expenses in accordance with the rules provided in the Tax Code. A taxpayer may record income and expenses under either the cash or accrual method of accounting.

However, a taxpayer must use the same method for both accounting and tax purposes and be consistent in using the method throughout the tax year. The tax year is a calendar year.

### Cash method

Using the cash method of accounting, a taxpayer is required to record income upon its receipt, regardless of when income was earned. Expenses are recorded when the payment is made rather than when the expense was incurred.

### Accrual method

Contrary to the cash method, the general rule under the accrual method of accounting requires a taxpayer to record income when it is earned, regardless of when it is actually received. Expenses are recorded when they are incurred rather than when they are paid.

### Tax payment and reporting

Companies pay profit tax at a rate of 20% and are required to make quarterly advance tax payments calculated either as 25% of the previous year's tax liability or by multiplying the amount of their income in the current quarter with a weighted tax coefficient of the gross income for the previous year.

The formula below explains this calculation in more detail:

- A — Last year's profit tax
- B — Last year's gross income (without deduction of expenses)
- C — Current quarter's gross income

$$\text{Advance profit tax} = C \times (A/B)$$

The annual profit tax return is due no later than 31 March of the following reporting year.

## 1.3. Taxation of non-residents of Azerbaijan

### Tax jurisdiction over non-residents

A non-resident enterprise operating in Azerbaijan through a permanent establishment pays tax on its profit, i.e. on gross income generated from Azerbaijani sources in connection with the permanent establishment, less the amount of expenses incurred with respect to such income as per the Tax Code.

The tax rate is a flat rate of 20%.

The gross income of a non-resident enterprise that is not connected with the permanent establishment is taxed at the source of payment without the deduction of expenses. A non-resident enterprise generating income through the supply of property not connected with the permanent establishment pays tax on the said gross income received during a calendar year from an Azerbaijani source. The tax is paid after the deduction of expenses relating to income generation.

### Permanent establishment

In terms of the Azerbaijani Tax Code, a foreign individual's or a legal entity's permanent establishment in Azerbaijan is an establishment through which a taxpayer's economic activity is carried out either fully or partially for 90 or more days within a 12-month period, including the activities of an authorized representative.

The Tax Code provides for any of the following to be evidence of a permanent establishment: a place of management, subdivision, office branch or agency; construction and repair sites; installation and assembly facilities, as well as supervisory activities associated with them; platforms, sites,



drilling equipment or vessels used for the exploration and production of natural resources, as well as supervisory activities associated with them; any fixed base/location where a non-resident individual carries out entrepreneurial activity; premises used for the provision of consulting services; any places of employment in which other types of entrepreneurial activity are conducted in Azerbaijan; persons carrying out the functions of a permanent establishment for a non-resident enterprise or a non-resident individual in Azerbaijan, or people acting on their behalf, authorized to make agreements on their behalf and usually conducting such responsibilities; places of manufacture and sale of goods and the execution of works and services.

A place is not considered a non-resident enterprise's permanent establishment in Azerbaijan if used (regardless of the user) exclusively to store goods or products owned by the non-resident enterprise; keep a stock of goods or products owned by the non-resident enterprise only for the purpose of their eventual processing and subsequent export from Azerbaijan by a third party; purchase of goods or manufacturing of products by a non-resident

enterprise for its own needs; implementation by a non-resident enterprise of any preparatory or support activity for its own needs.

#### **Azerbaijani source income**

For withholding tax purposes, the following income types are treated as received from Azerbaijani sources:

- Interest income
- Dividends income
- Royalty income
- Rent income
- Insurance income
- Other income
- Income from engineering, architectural and cultural services.

#### **Withholding tax rates**

Unless otherwise specified in double tax treaties that Azerbaijan has entered into, the following withholding tax rates normally apply to the following items of income from Azerbaijani sources which are payable to non-residents, provided that such income is not attributable to a non-resident's permanent establishment in Azerbaijan:

<b>Income from Azerbaijani sources</b>	<b>Tax rate</b>
<b>Dividends</b>	10%
<b>Interest</b>	10%
<b>International communication and transportation services</b>	6%
<b>Royalties</b>	14%
<b>Management fees</b>	10%
<b>Interest on financial leasing</b>	10%
<b>Risk insurance and re-insurance fees</b>	4%
<b>Income received from performing works and rendering services</b>	10%
<b>Other items of income from Azerbaijan sources</b>	10%



#### 1.4. Tax exemptions

The Tax Code envisages the following exemptions from profit tax: income of charitable organizations, except for that coming from entrepreneurial activity; grants, membership fees and donations received by non-commercial organizations; income of international, interstate and intergovernmental organizations, except for that received from entrepreneurial activity and income from other similar activities

The Tax Code also grants tax exemption for resident entities of industrial or technology parks for seven years after the date they are registered with the mentioned parks. Additionally, part of the profit of entities managing industrial or technology parks which is directed to improvement of the infrastructure

of the parks, is exempt from profit tax. The Tax Code also envisages 50% exemption from profit tax for legal entities holding investment promotion certificate. The exemption is valid for seven years from the date of obtaining of investment promotion certificate.

In addition, the Tax Codes provides five years exemption from profit tax for legal entities' income generated from production of agricultural products (as well as production with the industrial method) starting from 1 January 2014.

#### 1.5. Taxation of cross-border transactions

##### Outbound transactions

Since resident entities are taxed on their worldwide income in Azerbaijan, and may also be taxed by foreign countries

on their income derived from sources or from carrying on business in such countries, the same income is potentially subject to double taxation.

In terms of domestic tax law, income or profit tax paid outside Azerbaijan is credited upon payment of tax in Azerbaijan. Excess foreign tax credit may neither be offset against a resident taxpayer's Azerbaijan tax liabilities on any domestic source income nor be carried forward or backward.

##### Double tax treaty relief in Azerbaijan

Azerbaijan has agreed double tax treaties with 53 (currently 51 of them are valid) countries that generally follow the OECD Model Income Tax Convention.

Azerbaijani tax legislation establishes rules on claiming a refund of taxes withheld from payments to non-residents who are subject to the provisions of double tax treaties signed between Azerbaijan and other countries.

According to administration rules on implementing double tax treaties, if a non-resident submits a claim for an exemption of tax from, or application of limited taxation with respect to, income derived from sources in Azerbaijan for all income types (e.g business profit, dividends, royalties and interest) generated by a non-resident, then the non-resident may be entitled to the benefits in advance in accordance with the provisions of the respective double tax treaty.



Country of recipient	Dividends	Interest	Royalties
<b>Austria</b>	5% -10%-15%	10%	5%-10%
<b>Belarus</b>	15%	10%	10%
<b>Belgium</b>	5%-15%	10%	5%-10%
<b>Bosnia and Herzegovina</b>	10%	10%	10%
<b>Bulgaria</b>	8%	7%	5%-10%
<b>Canada</b>	10%-15%	10%	5%-10%
<b>China</b>	10%	10%	10%
<b>Croatia</b>	5%-10%	10%	10%
<b>Czech Republic</b>	8%	10%	10%
<b>Denmark</b>	5%-15%	8%	5%-10%
<b>Estonia</b>	5%-10%	10%	10%
<b>Finland</b>	5%-10%	10%	5%-10%
<b>France</b>	10%	10%	5%-10%
<b>Georgia</b>	10%	10%	10%
<b>Germany</b>	5%-15%	10%	5%-10%
<b>Greece</b>	8%	8%	8%
<b>Hungary</b>	8%	8%	8%
<b>Iran</b>	10%	10%	10%
<b>Israel</b>	15%	10%	5%-10%
<b>Italy</b>	10%	10%	5%
<b>Japan</b>	15%	10%	0%-10%
<b>Kazakhstan</b>	10%	10%	10%
<b>Korea Republic</b>	7%	10%	5%-10%
<b>Kuwait</b>	5%-10%	7%	10%
<b>Latvia</b>	5%-10%	10%	5%-10%
<b>Lithuania</b>	5%-10%	10%	10%

Country of recipient	Dividends	Interest	Royalties
<b>Luxemburg</b>	5%-10%	10%	5%-10%
<b>Macedonia</b>	8%	8%	8%
<b>Malta</b>	8%	8%	8%
<b>Moldova</b>	8%-15%	10%	10%
<b>Netherlands</b>	5%-10%	10%	5%-10%
<b>Norway</b>	10%-15%	10%	10%
<b>Poland</b>	10%	10%	10%
<b>Qatar</b>	7%	7%	5%
<b>Romania</b>	5%-10%	8%	10%
<b>Russia</b>	10%	10%	10%
<b>San Marino</b>	5%-10%	10%	5%-10%
<b>Saudi Arabia</b>	5%-7%	7%	10%
<b>Serbia</b>	10%	10%	10%
<b>Slovenia</b>	8%	8%	5%-10%
<b>Sweden</b>	5%-15%	8%	5%-10%
<b>Switzerland</b>	5%-15%	10%	5%-10%
<b>Tajikistan</b>	10%	10%	10%
<b>Turkey</b>	12%	10%	10%
<b>UK</b>	15%	10%	5%-10%
<b>Ukraine</b>	10%	10%	10%
<b>United Arab Emirates</b>	5%-10%	7%	5%-10%
<b>Uzbekistan</b>	10%	10%	10%
<b>Montenegro</b>	10%	10%	10%
<b>Pakistan</b>	10%	10%	10%
<b>Vietnam</b>	10%	10%	10%

## Non-residents operating in Azerbaijan can apply for an advanced exemption or reduced taxation in respect of all income types, including business profits, dividends, interest and royalty income without creating a permanent establishment

To do this, firstly a non-resident must obtain a certificate of residency from the tax authorities of its country of residence to confirm its residence in that country.

According to the administration rules on double tax treaties, copies of the contracts confirming that the income is to be paid to the non-resident and other relevant documents (such as invoices, contract addendums, etc.), must be submitted to the Azerbaijani tax authorities for confirmation.

The rules also allow non-residents operating in Azerbaijan without creating a permanent establishment, to apply for a tax refund based on the provisions of the applicable double tax treaties. To do this, the non-resident must complete a DTA-05 form and submit it to the tax department where the payee is registered.

According to the above discussed administration rules, applications are reviewed by the tax authorities and shall be responded within 20 working days upon submission of the applications (e.g. DTA-03).

The tax refund must be made within 45 days of the submission of the application if the tax authorities make a decision to confirm the refund. A period of 45 days is starting from the day of application and should cover the actual transfer date of the overpaid taxes to the applicant (taxpayer) by state treasury account.

### 2. VAT

#### 2.1. Concept of VAT

The concept of VAT according to Azerbaijani tax legislation is similar to the principles used in most European countries. In accordance with Azerbaijani law, VAT payers are entitled to recover VAT paid on purchases (input VAT) even if this exceeds the VAT generated by the sale of goods or services (output VAT).

#### 2.2. Payers of VAT

An individual or legal entity whose taxable sales amount to more than AZN 200,000 in a consecutive 12-month period must register for VAT.

Taxpayers must register for VAT in advance of carrying out a taxable transaction worth more than AZN 200,000.

The Tax Code also allows voluntary registration for VAT purposes.

A taxpayer that has registered but whose total taxable sales over a 12-month period do not exceed AZN 100,000 may apply for the cancellation of their registration at any time within one year of their last registration for VAT purposes, subject to some exceptions indicated in the Tax Code.

#### 2.3. Objects of taxation

Under the Tax Code, the supply of goods/provision of services and import of goods are subject to VAT. Taxable transactions do not include services provided or work completed outside Azerbaijan.

However, the payments made by persons without tax registration for provision of works and services via e-commerce to non-residents which are not registered for VAT purposes (with exceptions for purchase of airline tickets and booking of hotel accommodation services outside of territories of the Azerbaijan Republic) are subject to VAT.

#### 2.4. VAT rate

The current VAT rate is 18%.

#### 2.5. VAT invoice

Any VAT payer that carries out a taxable transaction is required to issue a tax invoice to the person receiving the goods or services.

The taxpayer must draw up and issue a tax invoice to the purchaser of the goods/work/ services upon delivery or within five days of delivery.

VAT invoices are issued in electronic form. Registration and administration of electronic invoices is carried out by the Ministry of Taxes via the Internet.

#### 2.6. Time of recognition of VAT liability

Output VAT must be recognized





at the time of the payment if such payment is made within 30 days upon the supply. If the payment was not received within 30 days VAT must be recognized at the time of the issue of the VAT invoice provided that it was issued within five days of supply.

If payment is not received within 30 days and a VAT invoice was not issued within five days of supply, the time of recognition of output VAT liability will be the actual time of the supply of goods or services.

If payment was made before the supply, VAT liability must be recognized at the time of the payment, if a VAT invoice is not issued within five days of supply.

## 2.7. VAT administration

### Administration

VAT on domestic supplies and the import of services is administered by the tax service, and VAT on the import of goods is administered by the customs service.

### Payment and reporting

Registered VAT payers should assess the amount of VAT to be remitted to the budget by reducing its output VAT liability with input VAT credit.

Effective 1 January 2008, all input VAT must be paid through a VAT Deposit Account ("VDA"), a kind of an escrow bank account administered by the government. The purpose of introducing VDAs, according to official sources, is to combat VAT fraud.

The regulations require every VAT payer to have a VAT sub-account ("VSA"). A VSA is a part of a VDA. Only input VAT paid to the supplier's VDA is recoverable.

Registered VAT payers are required to submit VAT returns and pay VAT due on a monthly basis by the 20th day of the following month.

## 2.8. VAT refund

The reporting period for VAT is a calendar month. According to the Tax Code, the amount of input VAT remaining after the offset against a taxpayer's output VAT in the current month is automatically transferred to the next three months and should be offset against VAT liability arising during that period.

Taxpayers have the right to offset VAT receivable against liabilities with respect to other taxes, interest charges for late tax payment, financial sanctions and administrative penalties. Taxpayers are also entitled to request that the authorities transfer repayable VAT to pay other tax liabilities.

If after the three-month period, the input VAT is not fully offset, the remaining amount must be refunded to the taxpayer within 20 days of the taxpayer's submission of an application to the tax authorities.

Daily interest of 0.1 % is payable by the tax authorities if the amount of tax due to the taxpayer is not repaid within the 45 day period. However, we are not aware of any taxpayer in Azerbaijan that has been compensated for a late tax refund in this manner.

The taxpayer can recover input VAT up to three years after it becomes due.

The right of a taxpayer to claim overpaid taxes is limited to five years from the date when the tax reporting period ended.

It should be noted that the VAT refund process in Azerbaijan is extremely difficult. The Azerbaijani Ministry of Taxes and Ministry of Finance are always reluctant to approve VAT refund applications received from taxpayers.

### 3. Property tax

#### 3.1. Property tax for individuals

Payers of property taxes are resident and non-resident individuals who personally own buildings and their parts, as well as water and air transport facilities.

Individuals obtaining investment promotion certificate are fully exempted from property tax for the respective fixed assets for seven years from the date of obtaining investment promotion certificate. In addition, the Tax Code provides five years exemption from property tax for individuals regarding properties used in production of agricultural products (as well as production with the industrial method) starting from 1 January 2014.

Individuals pay property tax in the following order and at the following rates:

For the building in their ownership:

- Property tax is calculated by multiplying certain tax rates varying between AZN 0.1 to AZN 0.4 by total square metres of the area of the building, depending on the building's location.

For water and air transport vessels:

- AZN 0.02 per cubic cm of the water transport vessel's engine
- AZN 0.02 per cubic cm of the air transport vessel's engine
- 1% of the market value of water and air transport equipment without engines

#### 3.2. Property tax for legal entities

In respect of legal entities, taxable objects include:

- Average annual value of fixed assets on the enterprise's balance sheet
- For non-resident enterprises carrying out business activity through a permanent representation in Azerbaijan, only the average annual value of fixed assets connected with the permanent representation

Full exemption from property tax for the respective fixed assets is considered for legal entities for seven years from the date of obtaining investment promotion certificate.

Entities pay tax at a rate of 1% of the average annual residual value of the fixed assets, which is determined by adding up the residual value of the enterprise's property (excluding vehicles) as of the beginning and the end of the reporting year and dividing the resulting sum by two.

Quarterly advance payments of property tax should be made in an amount equal to 20% of the previous year's property tax no later than the 15th day of the second month of each quarter. The annual property tax return should be submitted no later than 31 March of the next reporting year.

### 4. Personal income tax

#### 4.1. Tax residency

Individuals who are present in Azerbaijan for more than 182 cumulative days during a calendar year, or those with a place of permanent residence, a centre of vital interests or an habitual abode in Azerbaijan, or who have Azerbaijani citizenship, are considered to be tax residents of Azerbaijan.

#### 4.2. Taxable income and exemptions

Residents of Azerbaijan are subject to income tax on taxable income, which is defined as gross income received from all sources (both Azerbaijani and non-Azerbaijani) during the tax year, regardless of where the income was earned or paid, less allowable deductions.

Non-residents are subject to Azerbaijani income tax only on income received from Azerbaijani sources.

The taxable base for personal income tax is determined as the difference between gross income for the tax year and expenses (or deductions) stipulated by the Tax Code for this period.

Virtually all forms of compensation to an employee are taxable, including hardship and payment of taxes on behalf of the employee. Income of sole entrepreneurs operating in the industrial parks is exempt from taxation. Moreover, 50% exemption from personal income tax is granted for individuals who hold investment promotion certificate for seven years from the date of obtaining investment promotion certificate.

Moreover, individuals' annual interest income paid by a local bank or branch of a foreign bank in Azerbaijan for term deposits, as well as dividends, discounts (difference as a result of investing bonds below the face value) and interests paid by an issuer for investment securities are exempted from personal income tax for seven years beginning from 1 February 2016.

#### 4.3. Tax rates

Worldwide income of tax residents and Azerbaijani source income of non-residents received from employment are subject to the following progressive income tax rates:

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

\* AZN 173 of a salary below AZN 2500 is not taxable

Monthly taxable income	Tax rate
Up to AZN 30,000	14%
Over AZN 30,000	AZN 4,200 + 25% of the amount exceeding AZN 30,000

\* AZN 2076 of an annual salary below AZN 30,000 is not taxable

At the same time, all individuals engaged in entrepreneurial activity will be taxed at a fixed rate of 20%.

Also domestic sport betting, income of individuals from lottery winnings, (with exception of cash winnings on sports games betting, winnings from lotteries and from other type of competitions and contests outside of Azerbaijan) are subject to 10% withholding tax at the source of payment which should be withheld and paid to the State Budget on a monthly basis. A tax base for such an income is a difference between the winning and the principal amount paid for participation in such betting or lotteries.

#### 4.4. Payment and reporting of personal income tax

Income from employment is subject to withholding by the employer at source. Taxes withheld are to be remitted by the employer to the budget within 20 days of the following month.

Since 1 January 2010, legal entities and entrepreneurs that are registered for VAT purposes, or simplified taxpayers paying employment income to individuals, have had to submit tax returns to the tax authorities before 31 January of the following reporting year.

Employers that are not payers of VAT or simplified tax must submit tax returns no later than 20 days after the end of each calendar reporting quarter.

#### 4.5. Individual filing

Residents and non-residents must complete and file their income tax returns no later than 31 March of the following tax year.

#### 5. Social insurance

According to Azerbaijani law, social insurance contributions are paid by both Azerbaijani nationals and foreign individuals.

Employers are liable for paying social insurance contributions at a rate of 22% of the employee's gross salary, and 3% is deducted from the employee's gross salary as the employee's portion of the social insurance contribution.

Employers are also responsible for submitting quarterly reports to the social protection fund authorities in respect of the social insurance contributions calculated and paid in respect of local employees and foreign employees who are on the local payroll, by the 20th of the month following the reporting quarter.

The Agreement on Cooperation in the Area of Social Insurance was signed between the governments of Turkey and Azerbaijan on 17 July 1998. According to Article 7.1 of the Agreement, Turkish citizens employed by Turkish companies operating in Azerbaijan for less than 24 months are exempt from paying Azerbaijani social insurance contributions.

However, Article 7.5 of the Agreement states that this exemption will not apply if Turkish citizens are employed by a division or a permanent establishment of a Turkish company in Azerbaijan.

#### 6. Unemployment insurance

According to the Law "On unemployment insurance" dated 30 June 2017, employees as insured parties, employers as insurers are required to make unemployment contributions.

Employers are liable for paying unemployment insurance contributions at a rate of 0.5% of the employee's gross salary, and 0.5% is deducted from the employee's gross salary as the employee's portion of the social insurance contribution.

Employers are also responsible for submitting quarterly reports to the social protection fund authorities in respect of the unemployment insurance contributions calculated and paid in respect of local employees and foreign employees who are on the local payroll, by the 20th of the month following the reporting quarter.

Employer is also responsible for remitting 0.5% as employee's portion and 0.5% as its portion on the day of salary payment but no later than 15th of the month following the calendar month to which the unemployment insurance contributions is related.

#### 7. Mining tax

Legal entities and individuals extracting mineral resources in Azerbaijan and on the Caspian shelf pay mining tax at rates ranging from 3% to 26%. The tax is paid after the extraction of minerals on a monthly basis by the 20th day of the month following the accounting month. Mining tax is deductible for profit tax purposes. Payers of mining

tax submit tax returns on a monthly basis no later than the 20th day of the month following the accounting month.

### 8. Land tax

A land tax is imposed on owners and users of land, the amount of which depends on the use, location and total area of the land. For instance, in Baku, the tax rate on industrial land up to 10,000 square metres is AZN 10 and AZN 20 for part exceeding 10,000 square metres per 100 square metres.

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

Legal entities calculate land tax on an annual basis based on the total area of the land and the respective land tax rates and then submit their calculations to the tax authorities no later than 15 May each year.

Land tax is paid twice yearly in equal installments no later than August 15 and November 15.

### 9. Excise tax

All individuals and legal entities producing excisable goods in Azerbaijan or importing excisable goods are subject to excise taxes.

Tobacco products, alcoholic beverages and petroleum products are subject to excise tax at fixed rates, e.g. AZN 2 per liter of spirits or AZN 4 per 1,000 cigarettes produced in Azerbaijan.

Imports of passenger cars, leisure and sport yachts are subject to excise tax at different rates depending on the size of their engines.

Imported platinum, gold, jewelry and other domestic products made from it, processed, sorted, framed and mounted diamonds are subject to excise tax at different rates depending on:

- each gram of platinum;
- amount of gold in a thousand weight unit;
- carat of a diamond.

Import of fur-leather products is also subject to excise tax at a rate of 10% from its wholesale sales price.

The export of excisable goods is subject to 0% tax.

### 10. Road tax

Road tax is paid by non-resident entities and individuals entering Azerbaijan, as well as persons engaged in production or import of motor petrol, diesel fuel and liquid gas in Azerbaijan.

The tax payable by non-resident entities and individuals entering Azerbaijan is collected by the customs authorities at different rates depending on the type of vehicle, distance driven within Azerbaijan and the length of time spent in the country.

The road tax for motor petrol, diesel fuel and liquid gas produced in the territory of Azerbaijan and directed to domestic consumption is calculated by adding AZN 0.02 to the wholesale price of each liter thereof.

The road tax for imported motor petrol, diesel fuel and liquid gas is calculated by adding AZN 0.02 to the customs value of each liter thereof, that is not lower than the wholesale price.

### 11. Simplified tax

Individuals and legal entities involved in entrepreneurial activity that are not registered VAT payers have the right to pay simplified tax. However, producers

of excised goods, credit and insurance organizations, investment funds, professional securities market participants, non-governmental pension funds and certain other persons are not allowed to become a simplified taxpayer. Simplified tax is calculated from the revenue obtained from the provision of goods, completion of works, rendering of services and non-sale income at the following rates:

- Baku — 4%
- Other regions — 2%
- Revenue of operators of sports-gambling games — 6%
- Income of commissioners of sports-gambling games — 4%

Persons engaged in trading and catering activities whose taxable turnover exceeds AZN 200,000 at any month within consecutive twelve months are entitled to register as simplified taxpayers at the following rates:

- For trading activities — 6%
- For catering activities — 8%

Persons engaged in the construction of buildings are also entitled to register as simplified taxpayers voluntarily. Simplified tax for construction of buildings is calculated at a rate of AZN 45 multiplied by the location zone rate, which varies from 0.5 to 4.0. The rate for non-residential buildings is 1.5 regardless of location.

People providing transportation services (except for international transportation) are payers of simplified tax. Rates for simplified tax payers providing transportation services vary from AZN 1 up to AZN 9 per month depending on such factors as the number of seats, cars and tonnage.

Furthermore, income from the sale of residential and non-residential property,



including property acquired from persons engaged in construction, is subject to a simplified tax at a rate of AZN 15 per square meter multiplied by the location zone rate, which varies from 0.5 to 4.0. The rate for non-residential buildings is 1.5 regardless of location.

Legal entities' and sole entrepreneurs' cash withdrawal from their bank accounts is subject to 1% of simplified tax which shall be withheld by local banks, branch offices of foreign banks in the Republic of Azerbaijan, and national operators of postal services.

Income from the sale of land space is subject to a simplified tax at a rate which depends on the use, location and total area of the land. For instance, in Baku, the tax rate is AZN 0.5 per square meter multiplied by the location zone rate, which varies from 1.2 to 4.0.

Simplified tax payers are obliged to make simplified tax payments and file tax returns no later than the 20th day of the month following each reporting calendar quarter.

Public notary approving the contract of the sale of residential and non-residential property is responsible for calculating, withholding and remitting the simplified tax amount to the State Budget within one banking day. The notary is also responsible for filing a monthly tax return with the tax authorities no later than 20th day following the reporting month.

## 12. Transfer Pricing

Transfer Pricing rules in Azerbaijan are generally in line with OECD TP guidelines, and transactions between below listed parties are considered as controlled transactions:

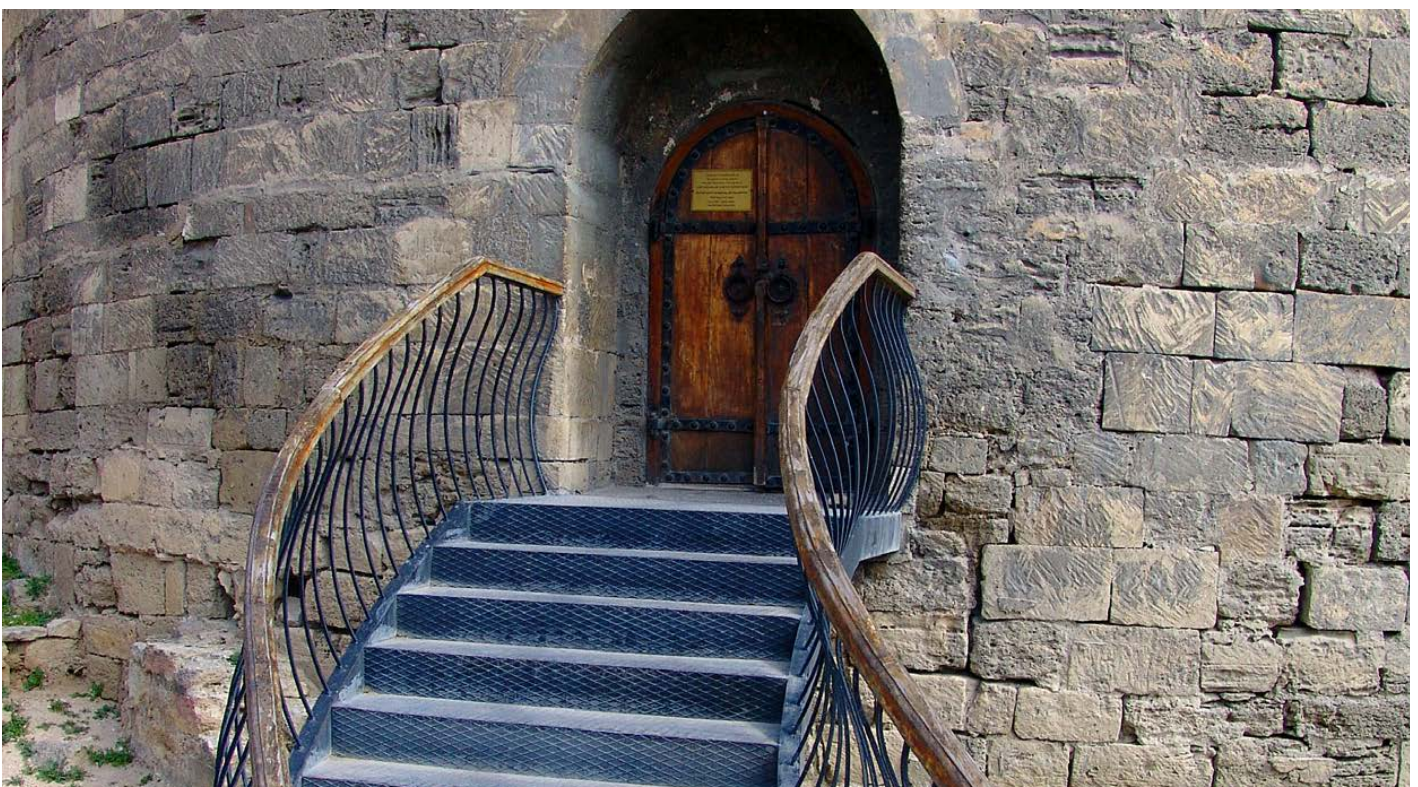
- between Azerbaijani resident and mutually dependent non-resident persons;

- between the non-resident's permanent establishment in Azerbaijan and non-resident itself or any representative, branch and other division of such non-resident located in other countries;

- between the resident of Azerbaijan or permanent establishment of non-resident in Azerbaijan and subjects established (registered) in countries with preferential taxation.

According to the tax legislation of Azerbaijan, transfer pricing considerations require taxpayers to submit special forms to the tax authorities if volume of transactions for each party exceeds AZN 500,000 (approx. EUR 250,000) per calendar year.

Failure to comply with filing requirements is subject to a financial sanction of AZN 500 (approx. EUR 250).



Parties to PSAs are the government of Azerbaijan, represented by the State Oil Company of the Republic of Azerbaijan (SOCAR) and contractors represented by various well-known foreign oil & gas companies.

## II. PSA taxation

Currently more than 20 PSAs have been signed and ratified in Azerbaijan.

PSAs contain provisions governing certain taxation rules.

In addition, detailed taxation procedures are set out in the PSA tax protocols.

The PSAs stipulate taxation rules for foreign sub-contractors performing work or providing services in connection with PSAs.

### 1. Profit tax

Under the PSAs, contractors carrying out business in Azerbaijan in connection with petroleum operations should pay profit tax: the rate is negotiated and varies from 20% to 32%.

Contractors should submit their financial statements and profit tax returns (drawn up exclusively in USD) for each calendar year, along with an appropriate report from an auditor to the tax authorities by the dates established in the PSAs.

### 2. VAT

Contractors and foreign sub-contractors are exempt from VAT with a 0% rate in connection their activities in the sector. This includes the following:

- Goods, work and services supplied to or by them
- Export of petroleum

- Import and acquisition of goods, work and services

To confirm VAT exemption status, contractors and foreign subcontractors should obtain a VAT exemption certificate. This certificate is issued by the Ministry of Taxes.

It should be noted that a VAT exemption certificate is issued to contractors, operating companies, direct local and foreign subcontractors registered in Azerbaijan.

### 3. Withholding tax

In lieu of profit tax, foreign subcontractors pay withholding tax at rates varying from 5% to 10%, calculated from gross payments received in respect of work or services performed in Azerbaijan. Under the PSAs, a foreign subcontractor is defined as a legal entity incorporated outside of Azerbaijan and providing goods, work or services directly or indirectly to the contractor who is a party to a PSA.

Income tax must be withheld by anyone making payments to a foreign sub-contractor and remitted to the Azerbaijani budget. This is the only profit tax liability of a foreign sub-contractor.

According to new SWAP PSA a foreign subcontractor, which has a legal presence in the Republic of Azerbaijan, must pay the profit tax in accordance with the provisions of the Tax Code.

## 4. Taxation of employees

Personal income tax of local employees is calculated in accordance with the statutory tax legislation.

Personal income tax of foreign tax resident employees is calculated only on their income earned as a direct result of their employment in Azerbaijan. Foreign employees who do not become tax residents should not pay Azerbaijani personal income tax.

### 4.1. Tax residency

Under the PSAs, there are three tax residency rules:

- An expatriate employee of a foreign sub-contractor, who is present in Azerbaijan for ordinary business purposes, becomes a tax resident if they spend more than 30 consecutive days in Azerbaijan in a calendar year. Income earned after the 30th day is taxable in Azerbaijan.
- Individuals spending less than 30 consecutive days but more than 90 cumulative days in Azerbaijan in a calendar year are also treated as tax residents, and income earned after the 90th day becomes taxable.
- Rotating employees and foreign employees who have their primary place of employment in Azerbaijan qualify as tax residents if they spend more than 90 cumulative days in Azerbaijan in a calendar year, and they are taxable from the first day of their stay in Azerbaijan.

### 4.2. Taxable income

Almost all payments to foreign employees in Azerbaijan, including wages, salaries, bonuses, personal travel costs, education costs of the expatriate's family members, etc. is considered to be taxable income.

### 4.3. Tax rates

The rates of personal income



tax are the same as the statutory rates set out above.

#### 4.4. Personal income tax withholding

Each employer must withhold personal income tax from payments made to local and foreign employees. Foreign employees are entitled to receive a tax receipt from the tax authorities for the amount of income tax paid.

#### 4.5. Tax reporting

Employers are responsible for reporting all Azerbaijani personal income tax payments made in respect of their local and foreign tax resident employees to the Ministry of Taxes.

#### 4.6. Social insurance

All foreign employees employed by companies engaged in the petroleum sector under PSAs are exempt from mandatory social insurance.

Employers are required to pay social insurance contributions to the State Social Protection Fund at a rate of 22% of the employee's gross income. In addition, employers must withhold social insurance contributions from the employee's income at the rate of 3% and pay them into the same fund.

#### 4.7. Unemployment insurance

All foreign employees employed by companies engaged in the petroleum sector under PSAs are exempt from unemployment insurance. Employers are liable for paying unemployment insurance contributions at a rate of 0.5% of the employee's gross salary, and 0.5% is deducted from the employee's gross salary as the employee's portion of the social insurance contribution.

#### 4.8. Customs duties under PSAs

All imports made in connection with a PSA are exempt from customs duties and VAT.

Contractors and foreign sub-contractors may obtain a certificate granting exemption from import/export duties. Certificates are issued by the State Customs Committee of the Republic of Azerbaijan. It should be noted that an import and export exemption certificate is issued only to contractors and foreign sub-contractors registered in Azerbaijan.

A contractor or a foreign sub-contractor importing goods in relation to the PSA should submit copies of its VAT and an import and export exemption certificates to the customs authorities during the import process.

### III. HGA taxation

#### 1. Profit tax

Profit tax is imposed on the taxable profit from the project activities of each participant in an HGA at a fixed rate of 27%.

HGA participants should submit their profit tax return (drawn up exclusively in USD) to the tax authorities for each calendar year, no later than April 15 (under BTC HGA) and April 1 (under SCP HGA) of the following calendar year.

#### 2. Other taxes

Under HGAs, no taxes are imposed on or withheld from payments to any contractor in connection with HGA activities. Contractors also do not have tax compliance or filing obligations in connection with HGA activities.

HGA participants are entitled to import into or export/ re-export from Azerbaijan free of taxes and restrictions, whether in their own name or on their behalf, all equipment, materials, machinery, tools, vehicles, spare parts, supplies, petroleum, fuels and lubricants to be used in connection with the HGAs and all other goods (other than natural gas), work, services or technology necessary or appropriate for use in connection with the HGA.

Foreign employees of HGA participants, contractors, and each family member of such foreign employees, have special rights with regard to import and export of goods and services. They may import into or export/ re-export from Azerbaijan all goods, work, services or technology for their own use and personal consumption. They may do this personally or arrange for a third party to provide import/export services on their behalf. However, re-sale of any such imported

goods to any other person is taxable, and, in the case of the sale of automobiles, furniture and professional tools and instruments, will result in liability for customs duties, in accordance with Azerbaijani law.

Personal income tax of foreign employees is calculated only on their income earned as a direct result of their employment in Azerbaijan and only if the employees spend more than 182 days in Azerbaijan per calendar year.

#### 3. Social insurance

Foreign nationals employed in connection with HGAs are exempt from mandatory social insurance.

The employment income of Azerbaijani nationals working under HGAs is subject to mandatory social insurance. Employers are liable for payment of social insurance contributions at a rate of 22% of the employee's gross salary, and 3% of the employee's gross salary is deducted as the employee's share of social insurance contributions.

The employer is responsible for making the monthly payment of social insurance contributions on the day that the employees' salary is paid, but no later than the 15th day of the month following the month when the income was accrued.

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