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OUTCOME OF PROCEEDINGS

From:	General Secretariat of the Council
To:	Code of Conduct Group (Business Taxation)
Subject:	Armenia's Reduced Tax Rate for Large Exporters (AM001) – Final description and assessment

I/ STANDSTILL REVIEW PROCESS (DECEMBER 2017)[1]:

a. Description

The regime applies to companies or group of companies meeting several criteria under the government's export promotion-oriented program, as follows:

– exclusively engaged in exports of goods and services;

– only export to Member States of the Eurasian Economic Union;

– do not carry out business activities in the field of metal mining and the processing and sale of precious minerals and excisable goods;

– receive the sales proceeds in foreign currency on bank accounts held in Armenia; and

– have their business plans approved by the government.

1 Endorsed by ECOFIN on 5 December 2017 (doc. 15429/17).

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Source: IBFD:
http://online.ibfd.org/kbase/#topic=doc&url=/collections/gtha/html/gtha_am_s_001.html&WT.z_nav=Navigation&colid=4915

b. Preferential (lower taxation than normal):

The companies or group of companies involved in the program approved by the government are taxed lower than the standard 20% company income tax rate:

– 5% if the annual exports of the company or the group of companies exceed AMD 40 billion; and

– 2% if the annual exports of the company or the group of companies exceed AMD 50 billion (on the whole amount exceeding the threshold).

c. Possible concern: ring fenced

A regime limited to operations outside the territory of the jurisdiction (ring fenced regime) does not meet criteria 1 & 2 of the Code of Conduct which forbid this type of ring fencing. The benefit of the reduced company income tax rate is limited to companies or groups of companies that exclusively export goods and services as the exported goods do not have to be produced in Armenia.

An important Code of Conduct criterion used to assess the harmfulness of a regime is its transparency (criterion 5). A measure is considered not transparent when it is not laid down in law but granted on a discretionary basis. It is unclear if the conditions for getting the government's approval are laid down in law or not.

d. Assessment

	1a	**1b**	**2a**	**2b**	**3**	**4**	**5**
Armenia – Reduced Tax Rate for Large Exporters	V	V	V	V	V	X	?

V = harmful

X = not harmful

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Explanation

Gateway criterion – Significantly lower level of taxation:

"*Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code*"

The general tax rate for companies in Armenia is 20%. The companies that are within the scope of the regime are granted tax reductions: 5% if the annual exports of the company exceed AMD 40 billion and 2% if the annual exports of the company exceed AMD 50 billion. The measure therefore provides for a significantly lower level of taxation and is potentially harmful under the Code.

Criterion 1 – Targeting non-residents:

"*whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents*"

Criterion 1a: The Reduced Tax Rate for Large Exporters regime seems targeted at activities outside the territory of the Republic of Armenia. The regime applies to resident taxpayers implementing a plan approved by the Government of the Republic of Armenia and for other resident profit taxpayers of the Republic of Armenia included in that plan ("group of resident profit taxpayers"). The group of resident profit taxpayers are engaged in export of goods, in works performed for non-resident organisations outside the territory of the Republic of Armenia and in services provided to non-resident organisations also outside the territory of the Republic of Armenia. The measure is de lege available to beneficiaries that carry out transactions only with non-residents outside of the territory of the Republic of Armenia.

Criterion 1b. Considering the purpose of the regime, it appears that the measure is applied only with respect to transactions carried out with non-residents and is not available for transactions within the territory of Armenia.

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Criterion 2 – Ring-fencing:

"*whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base*"

The Reduced Tax Rate for Large Exporters regime seems targeted at activities with foreign entities/markets since the tax advantages are granted only to companies that are engaged in exports of goods and services as the exported goods do not have to be produced in Armenia. It appears that the measure is applied only with respect to transactions carried out with non-residents and is not available for transactions within the territory of Armenia. Since the income of non-resident persons is not taxable in Armenia, the tax advantages are ring-fenced from the domestic market and, thus, do not affect the national tax base.

Criterion 3 – Substance:

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

The measure does not include any express requirement for real economic activity or substantial economic presence.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

A tax exemption does not contradict any internationally embraced principle.

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Criterion 5 – Transparency:

"*whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way*"

This regime does not seem transparent to the extent that there are no clear criteria for the tax concessions that may be granted. The companies should have their business plans approved by the government. The scope of the companies benefiting from the regime is not quite clearly defined as Art. 128(1) of the Tax Code of the Republic of Armenia states that the regime is available "for resident taxpayers implementing a plan approved by the government (…) and for other resident profit taxpayers of the Republic of Armenia included in that plan". The conditions for getting the government's approval are laid down in RA Government Decision No 387-N of 02.04.2015 "On approving the procedure of RA Government approval for the programs stipulated by parts 1.1 and 1.2 of Article 33 of RA Law "On profit tax"" but as this document has not been provided by Armenia, the transparency of granting the benefits of the regime could not be assessed. In order to make a definitive decision on whether or not the regime is transparent, more information is needed.

Overall assessment

"*Without prejudice to the respective spheres of competence of the Member States and the Community, this code of conduct, which covers business taxation, concerns those measures which affect, or may affect, in a significant way the location of business activity in the Community*"

In light of the assessment made under all Code criteria, the regime should be considered overall harmful from a Code of Conduct point of view.

The main concerns which deviate from the Code of Conduct criteria relate to:

– The regime seems **targeted at activities with foreign entities/markets** since the tax advantages are granted only to companies that are exclusively engaged in exports of goods and services only to Member States of the Eurasian Economic Union.

– The measure **does not include any express requirement for real economic activity or substantial economic presence**.

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– The regime does not seem transparent to the extent that the Government may grant tax benefits on a discretionary basis since the requirements and conditions for getting the benefits are not laid down in law. In order to make a definitive decision on whether or not the regime is transparent, however, more information is needed.

II/ ROLLBACK REVIEW PROCESS (OCTOBER 2018)[2]:

Following the recording of Armenia's commitment in Annex II to the Council Conclusions of 5 December 2017 the jurisdiction was included in the monitoring exercise. As part of its work to assist with the technical aspects of the monitoring the Commission Services on several occasions sought updates from Armenia on its progress in meeting its commitments. The Armenian authorities informed the Code of Conduct Group Chair on 25 June 2017 that the legislative package abolishing the two regimes at stake had been ratified by the National Assembly.

Armenia abolished Article 128 of Armenia's Tax Code as well as all references to this article in other articles of the Tax Code. The timing of the changes corresponds to the expectations: the new law which came into force on 1 July 2018, provides for the end of the regimes on 01/01/2019 and the end of grandfathering on 01/01/2022. See Annex.

Armenia can therefore be considered as having **fulfilled its commitment**.

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[2] Endorsed by the ECOFIN Council on 2 October 2018 (doc. 11763/1/18 REV 1).

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ANNEX

The Law of the Republic of Armenia

On

Making amendments to the Tax Code of the Republic of Armenia and making amendments to the Law TC-266-N "On Making amendments to the Tax Code of the Republic of Armenia", dated December 21, 2017

Article 32. Abolish the Article 128 of the Tax Code.

Article 128. Deducted profit tax rates

1. The amount of the profit tax for resident taxpayers implementing a plan approved by the Government of the Republic of Armenia and for other resident profit taxpayers of the Republic of Armenia included in that plan (hereinafter referred to as "group of resident profit taxpayers") shall be calculated against the tax base at deducted profit tax rates prescribed by part 2 of this Article, where the group of resident profit taxpayers concurrently meets all the following conditions:

(1) in the group of resident profit taxpayers there are no resident profit taxpayers carrying out activities in one of the following sectors: extraction and/or processing of minerals, processing and/or sale of precious stones, production and/or sale of jewellery, production and/or sale of precious metals, production and/or sale of excisable goods;

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(2) the sum of the customs value of goods exported from the territory of the Republic of Armenia through the customs procedure “Export” to states not deemed EAEU members and/or exported from the territory of the Republic of Armenia to EAEU member states, of the value of works performed for non-resident organizations outside the territory of the Republic of Armenia and/or of services provided to non-resident organizations outside the territory of the Republic of Armenia by the group of resident profit taxpayers during the tax year (or, in the case of approval of the plan by the Government of the Republic of Armenia during the tax year, within the period from the day of entry into force of the relevant decision of the Government of the Republic of Armenia to the end of the tax year) is at least AMD 40 billion, within the scope whereof, during each tax year of the implementation of the plan, the group of profit taxpayers shall ensure the minimum amount of the customs value — prescribed by the Government of the Republic of Armenia — of goods exported from the territory of the Republic of Armenia through the customs procedure “Export” to states not deemed EAEU members and/or exported from the territory of the Republic of Armenia to EAEU member states. The value of works performed for non-resident organizations outside the territory of the Republic of Armenia and/or of services provided to non-resident organizations outside the territory of the Republic of Armenia within the framework of the plan implemented by a group of resident profit taxpayers which carries out activities in the sector of construction and/or construction installation works and services exclusively outside the territory of the Republic of Armenia shall also be included in the calculation of the minimum amount of AMD 40 billion prescribed by this point, but the condition of the minimum amount of AMD 40 billion prescribed by this point for the value of works performed and/or services provided shall not apply, for the purpose of applying the profit tax rate deduction benefit prescribed by this Article, with respect to the plan implemented by the group of resident profit taxpayers which carries out activities in the sector of construction and/or construction installation works and services exclusively outside the territory of the Republic of Armenia;

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(3) during the tax year (or, in the case of approval of the plan by the Government of the Republic of Armenia during the tax year, within the period from the day of entry into force of the relevant Decision of the Government of the Republic of Armenia to the end of the tax year), foreign currency equivalent to at least AMD 40 billion in total has been credited, due to activities relating to the plan, to the bank accounts of taxpayers included in the group of resident profit taxpayers opened with banks deemed a resident organization. The foreign currency credited due to activities relating to the plan implemented by a group of resident profit taxpayers which carries out activities in the sector of construction and/or construction installation works and services exclusively outside the territory of the Republic of Armenia shall also be included in the calculation of the minimum amount of AMD 40 billion prescribed by this point, but the condition of the minimum amount of foreign currency credited due to activities relating to the plan shall not apply, for the purpose of applying the profit tax rate deduction benefit prescribed by this Article, with respect to the plan implemented by the group of resident profit taxpayers which carries out activities in the sector of construction and/or construction installation works and services exclusively outside the territory of the Republic of Armenia;

(4) profit taxpayers included in the group of resident profit taxpayers do not have incomes derived from supplying goods, performing works or providing services (except for the interest income received from a non-resident organization or non-resident natural persons for a granted loan, as well as for the income derived from the purchase and sale of securities and/or income derived from securities) in the territory of the Republic of Armenia during the tax year (or, in the case of approval of the plan by the Government of the Republic of Armenia during the tax year, within the period from the day of entry into force of the relevant Decision of the Government of the Republic of Armenia to the end of the tax year).

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2. The amount of the profit tax for a taxpayer included in a group of resident profit taxpayers concurrently meeting all the conditions prescribed by part 1 of this Article shall be calculated against the tax base:

(1) at the rate of five percent, where the sum of the customs value of goods exported from the territory of the Republic of Armenia through the customs procedure “Export” to states not deemed EAEU members and/or exported from the territory of the Republic of Armenia to EAEU member states, of the value of works performed for non-resident organisations outside the territory of the Republic of Armenia and/or of services provided to non-resident organizations outside the territory of the Republic of Armenia by the group of resident profit taxpayers during the tax year is at least AMD 40 billion;

(2) at the rate of two percent, where the sum of the customs value of goods exported from the territory of the Republic of Armenia through the customs procedure “Export” to states not deemed EAEU members and/or exported from the territory of the Republic of Armenia to EAEU member states, of the value of works performed for non-resident organizations outside the territory of the Republic of Armenia and/or of services provided to non-resident organizations outside the territory of the Republic of Armenia by the group of resident profit taxpayers during the tax year is at least AMD 50 billion;

(3) at the rate of five percent, where the group of resident profit taxpayers carries out activities in the sector of construction and/or construction installation works and services exclusively outside the territory of the Republic of Armenia, except for cases prescribed by point 2 of this part.

3. The procedure for approving the plans prescribed by this Article shall be prescribed by the Government of the Republic of Armenia.

Article 33. From the 1st part of the Article 130 of the Tax Code to remove the words ‘or part 2 of Article 128 of the Code’.

Article 130. Procedure for calculation of the amount of the profit tax subject to payment to the State Budget

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1. In accordance with the results of the activities of the reporting period, resident profit taxpayers shall pay to the State Budget the positive balance of the profit tax amounts — calculated against the profit tax base relating to that reporting period at the respective rate prescribed by part 1 of Article 125 or part 2 of Article 128 of the Code — and the amounts deductible from the profit tax. Within the meaning of this part, the following shall mean amounts deductible from the profit tax:

Article 34. From the 1st part of the Article 131 of the Tax Code to remove the words 'or part 2 of Article 128 of the Code'.

Article 131. Procedure for calculating the amount of the profit tax subject to compensation from the State Budget

1. In accordance with the results of the activities of the reporting period, the amount of the profit tax subject to compensation from the State Budget to resident profit taxpayers, as well as to non-resident profit taxpayers carrying out activities in the Republic of Armenia through a permanent establishment, shall be calculated as a negative balance of the profit tax amounts calculated against the tax base relating to the reporting period at the rate prescribed by part 1 of Article 125 or part 2 of Article 128 of the Code and the amounts deductible from the profit tax, prescribed respectively by part 1 or part 3 of Article 130 of the Code.

Article 39. In the Article 150 of the Tax Code:

1) Abolish the 2nd part

Article 150. Income tax rates

2. The income tax prescribed by Article 128 of the Code against the tax base of natural persons, who work or provide a service exclusively outside the territory of the Republic of Armenia on the basis of an employment or a civil law contract concluded with a tax agent included in the group of resident profit taxpayers carrying out activity in the field of construction and/or construction and installation works and services exclusively outside the territory of the Republic of Armenia, shall be calculated at a 13 percent rate.

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Article 86. This Law enters into force from the 1st July of 2018, except from the occasions mentioned in this article.

The 1st point of the Article 30, the Articles 31-34, and the 1st point of the Article 39 of this Law will enter into force from January 1, 2019. Until 1 January 2019, on the resident profit taxpayers who apply the program, approved by the Government and defined in the Article 128, and on other resident profit taxpayers of the Republic of Armenia, included in the program, the Article 128 and the part of the Article 150 of the Tax Code, will continue to be applied until 31 December 2021.

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