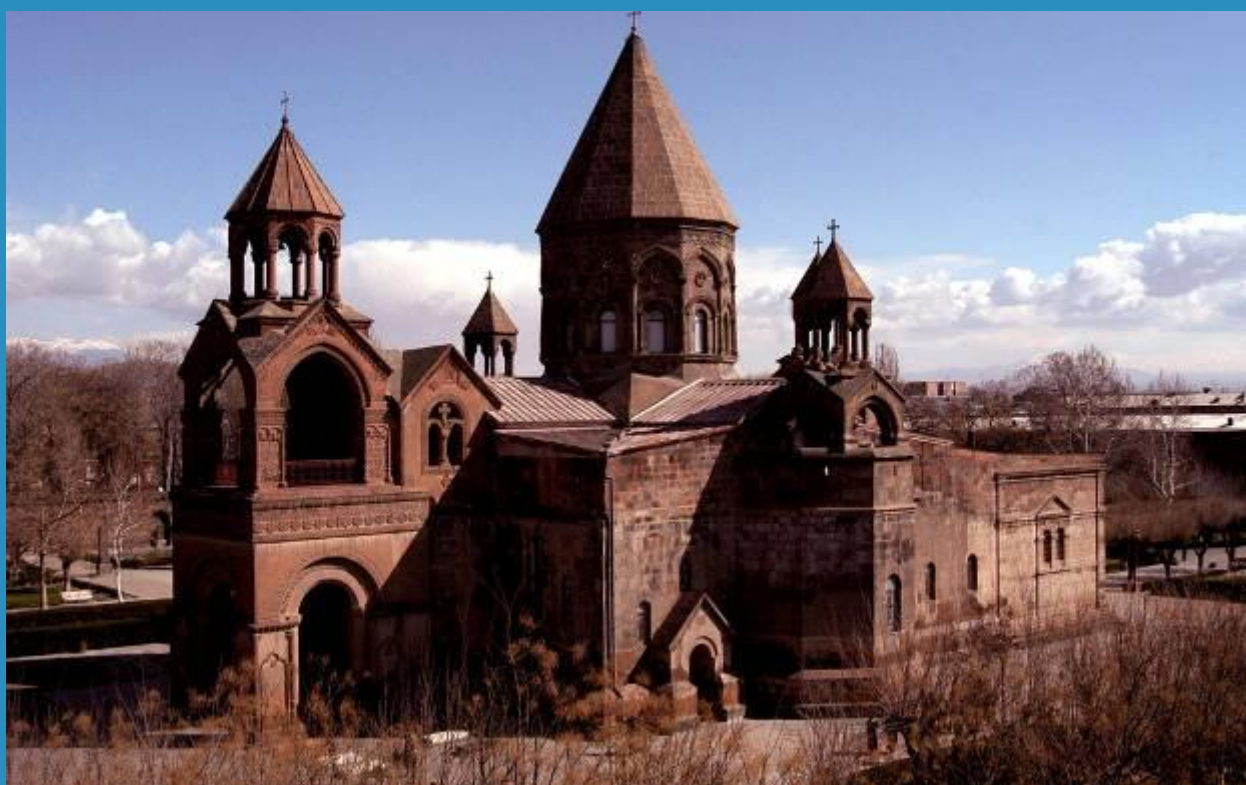


Doing business and investing in Armenia

2010 edition



Guide to doing business and investing in Armenia

2010 Edition

The information in this book is based on taxation law, legislative proposals and current practices, up to and including measures passed into law as of 31 March 2010. It is intended to provide a general guide only on the subject matter and is necessarily in a condensed form. It should not be regarded as a basis for ascertaining the tax liability in specific circumstances. Professional advice should always be taken before acting on any information in the booklet.

USD estimations in this guide are determined using a USD/AMD exchange rate of 400. The official rate on 31 March 2010 was 400.50.

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Partner letter

Armenia is a country with potential. We have demonstrated our belief in this potential by opening an office in Yerevan in 2007 and already have more than 20 expatriate and local professionals working here. We look forward to working with international and local investors who share this view.

There are many positives in Armenia. Before the global financial crisis, the country had enjoyed growth exceeding 10% every year since 2002. The banking sector has undergone significant reform resulting in weaker banks being liquidated, increased transparency, improved quality of assets and services, and strengthening of the banking system generally.

Issues related to the transparency and implementation of the Armenian regulatory system can still make business challenging at times. The application of tax, and regulatory rules can be inconsistent, creating uncertainty for medium-size businesses and market entrants. Ongoing reform to address such issues is anticipated.

A brief guide such as this cannot answer all your questions, but we trust it will provide you with valuable insight into the Armenian market.

We look forward to helping you build your business in Armenia.



Altaf Tapia
Managing Partner and Assurance Leader
for Caucasus

1 Armenia profile

1.1 Introduction

Armenia is located between Asia and Europe and occupies a land area of 29,800 sq km. It neighbours Turkey to the west, Azerbaijan to the east, Georgia to the north and Iran to the south, although the borders with Azerbaijan and Turkey are closed.

Armenia declared independence on 21 September 1991, following the dissolution of the Soviet Union.

1.2 Government structure

The Head of State is the President. He is elected by popular vote for a five-year term, and is eligible to serve two terms. The current President is Serzh Sargsyan, who was sworn in on 9 April 2008.

Legislative power is exercised by a single-chamber Parliament, the National Assembly, which comprises 131 deputies, 41 elected by single-member constituencies and 90 elected by party lists. Elections are held every four years. The last parliamentary elections were held in May 2007.

The highest executive body is the Government, consisting of the Prime Minister and Ministers. The Government is headed by the Prime Minister (currently Tigran Sargsyan). The organisation and rules of operation are determined by a decree issued by the President, upon the recommendation of the Prime Minister.

1.3 Legal system

Armenia is a civil law country.

The Constitution, adopted in 1995 and amended in 2005, sets out the structure of the national government, as well as its powers and functions. The powers of government are divided into three branches – legislative, executive and judicial.

Laws adopted by Parliament are forwarded to the President for signature. If the President signs the law or fails to act within a 21-day period, the law is considered officially promulgated. The President has the right to remand the legislation back to Parliament within the 21-day period for reconsideration. A remanded law may be passed by Parliament with a majority vote, in which case the President is required to sign and publish the remanded law within five days.

The Constitutional Court of Armenia consists of nine members and is the sole organ of constitutional

jurisdiction of Armenia. It mainly addresses such issues as the constitutionality of laws, regulations and other acts, and the compliance of Armenian international treaties with the Constitution.

The court system in Armenia has three branches: Courts of First Instance, Courts of Appeal and the Court of Cassation. First Instance Courts have jurisdiction over all civil, criminal and administrative cases. Decisions from First Instance Courts may be appealed to the courts of appeal, and from there to the Court of Cassation. The Constitution also allows special courts to be established, including the administrative and military courts.

As an alternative to litigation, Armenia allows for third party arbitration. Armenian law also allows foreign companies to include provisions in their contracts (including those with Armenian entities) that allow for arbitration by international arbitration institutions.

1.4 People

Population

The Armenian population is estimated to be 3.2 million.

Language

The national language is Armenian and is spoken by 97.9% of the population. Most Armenians also speak Russian.

Religion

Approximately 94% of the population belong to the Armenian Apostolic Church.

Living standards

Despite ongoing improvement, Armenia remains a poor country. The average (nominal) salary in 2009 was about AMD 101,800 (approximately USD 255) per month, an increase of 10.6% compared with 2008. Salary levels are particularly low in the regions.

The large Armenian Diaspora makes significant personal remittances into Armenia.

Unemployment

The official (registered) unemployment rate at the end of 2009 was 6.9%, which was increased by 0.6% compared with 2008. However, unofficial estimations place the unemployment rate significantly higher.

1.5 Economy

General

Like other Commonwealth of Independent States (CIS) countries, Armenia's economy initially suffered from the legacy of a centrally-planned economy and the breakdown of the former Soviet trading patterns. However, the government was able to carry out wide-ranging economic reforms in the early 1990s. The 1994 cease-fire in the Nagorno-Karabakh conflict also helped. New sectors, such as precious stone processing and jewellery making, information and communication technology, and even tourism began to supplement more traditional sectors in the economy, such as agriculture. This resulted in strong economic growth from 1995.

The GDP growth rate exceeded 10% in every year from 2002 until 2007. This fell to 6.8% in 2008 on the back of the global financial crisis, with the mining sector in particular affected by falling international commodity prices. Economic activity slowed to the point that the country's real GDP contracted by 14.4% in 2009. However, the Armenian authorities have developed a policy package that aims to restore confidence in the currency and financial system. The program's key features include a return to a flexible exchange rate regime, an increase in the refinancing rate, supportive financial sector policies, prudent fiscal policy, continued reforms in tax administration and targeted support for poor.

A summary of key economic indicators for Armenia is provided in Table 1.

Transport

Armenia has a railway network of 845 kilometres and 15,900 kilometres of highways, and effective road and railroad communication exists between all the major regions of Armenia. Because of transport blockages by Turkey and Azerbaijan, almost all cargo shipments

to landlocked Armenia are routed through ports in Georgia.

Almost all international flights go to Zvartnots International Airport, about 10 km west of Yerevan. The airport is capable of handling two million passengers annually.

Communications

Armenia has more than 700,000 fixed-line subscribers. ArmenTel (trading as Beeline), the country's national telecom provider, was granted exclusive rights to provide all telecoms services (apart from data services) until 2013, but the abolishment of these rights in 2007 paved the way for other operators to enter the market. The mobile communications market is growing rapidly. K-Telecom (trading as VivaCell-MTS) entered the market as a second provider in mid-2005, and Orange Armenia started operations in November 2009. Internet services are developing, and more than 50 licenses have been issued for VOIP (Voice Over Internet Protocol) services.

1.6 Foreign trade

Armenia's main trading partners are Belgium, Georgia, Germany, Iran, Netherlands, Russia, Switzerland, UK and the US. Exports include gold and diamonds, aluminium, electrical equipment, scrap metal and processed agricultural products. Imports include grain and other food, fuel and consumer goods.

The Government has adopted a policy of free international trade, and has been a full member in the World Trade Organisation since December 2002. Armenia has also ratified bilateral free trade agreements with Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russian Federation, Tajikistan, Turkmenistan and Ukraine.

Table 1: Key economic indicators

	2007	2008	2009
GDP (USD billion)	9.2	11.9	8.7
GDP growth	13.7%	6.8%	-14.4%
GDP per capita (USD)	2,843	3,686	2,671
Inflation (year-end)	6.6%	5.2%	6.5%
Budget balance (% of GDP)	-0.8%	-1.4%	-7.6
Officially registered unemployment (year-end)	7.1%	6.3%	6.9%
USD/AMD exchange rate (average)	342.1	306.0	363.3
Foreign direct investment (USD million)	582.3	1,132.4	2,606.3
External national debt (USD million)	1,449.1	1,577.1	2,966.7
Exports FOB (USD billion)	1,152.3	1,057.2	697.8
Imports CIF (USD billion)	3,267.8	4,426.1	3,304.1
Foreign Exchange Reserves (USD billion)	1.65	1.41	2.00

Source: National Statistics Service, Central Bank of Armenia, Armenian Development Agency

2 Business and investment environment

2.1 Business climate

From 2002 to 2007, the Armenian economy grew by more than 10% each year. However, this fell to 6.8% in 2008 on the back of the global financial crisis and the economy contracted by 14.4% in 2009.

Armenia encourages foreign trade and investment, and laws allow foreigners to purchase businesses and property, repatriate revenue and profits, and receive compensation if property is nationalised.

Taxes are quite low. Generally a 20% rate applies to companies and individuals. The value-added tax (VAT) rate is also 20%. Armenia does not restrict deductions to the same extent as some other CIS countries, while the aggregate rate of employer and employee social security contributions reduces to 8% for income exceeding AMD 100,000 (approximately USD 250) per month.

Surveys suggest that Armenia is a relatively easy country in which to do business. The World Bank study, *Doing Business 2009*, ranked Armenia as the 44th easiest country to do business out of 181 countries surveyed. Starting a business was estimated to take 18 days. Nevertheless, there are still issues related to the transparency and implementation of the Armenian regulatory system. The application of tax, customs (especially valuation) and regulatory rules (especially in the area of trade) can be inconsistent, creating uncertainty for medium-size businesses and market entrants.

2.2 Regulatory legislation

The following major pieces of legislation (in addition to taxation law) affect foreign investment into Armenia:

- The Civil Code is the main law regulating the legal status of business entities in Armenia, commercial and business entities in Armenia, commercial and business relations, the right to property ownership and other related rights. The Law on Bankruptcy provides the legal basis for liquidation, restructuring or financial rehabilitation of insolvent entities.
- The Law on State Registration of Legal Entities stipulates the procedure for registration of legal entities, branches, representative offices and entrepreneurs, registration of reorganisation of legal entities, and registration of amendments in charters. The Law on Joint Stock Companies

provides the basis for establishing joint-stock companies, operation and termination of their activities, and the distribution of profits among shareholders, while the Law on Limited Liability Companies does similarly for limited liability companies.

- The Law on the Protection of Economic Competition aims to protect and promote competition, prevent unfair competition and abuse of monopoly, create an environment for fair competition, help the development of entrepreneurship, and protect consumer rights.
- The Law on Copyright and Related Rights provides for the legal protection of literary works, musical works, software and other intellectual property rights. The Law on Patents regulates the creation, legal protection and application of inventions, industrial designs and utility models. The Law on Trademarks, Service Marks and Designation of Origin establishes the procedure for registering and protecting service marks, geographical indications and trademarks. The Law on Trade names regulates the registration, legal protection and use of trade names of legal entities.
- The Labour Code governs employment relations, and prescribes such issues as the length of working days, rest time, duration of vacations, calculation of salaries, termination of employment relations, and the duration and payment of special leave.

Businesses such as insurance, banking, public services and nuclear energy are subject to special laws, government decrees, Central Bank and other public administration decrees.

To engage in some types of activity, persons and commercial entities should obtain a license. Approximately 100 activities are subject to licensing.

2.3 Legal environment

The Armenian legal system has improved significantly in recent years. However, there remains a significant gap between the quality of the laws enacted in Armenia and their implementation by government agencies and the courts. Poor enforcement of court decisions is also a problem.

2.4 Foreign investment climate

Investment climate

Foreign investment into Armenia is welcomed. Foreign nationals (other than certain individuals of Armenian origin) may not own land in Armenia. However, they may lease land or acquire it through an Armenian legal entity. Otherwise, there are no restrictions on foreign ownership.

As a general rule, investment permits are not required, but all enterprises must be established according to the form and procedure prescribed by law and registered with appropriate government agencies. Foreign investors are generally not required to seek special approval from authorities for foreign direct investments.

Restrictions on foreign investment

There are no restrictions on the rights of foreign nationals to acquire, establish or dispose of business interests in Armenia.

Investment incentives

Taxpayers engaged in agricultural production are exempt from tax on that income.

Foreign exchange

The Government maintains a free floating and freely convertible currency, the Armenian Dram (AMD).

Transactions within Armenia are generally required to be designated and paid in AMD. However, there are no limitations on the conversion and transfer of money or the repatriation of capital and earnings, including branch profits, dividends, interest, royalties, or management or technical service fees. Most banks can transfer funds internationally within 2-4 days. Maintaining foreign currency accounts in Armenia is also permitted.

Guarantees and rights

Foreign investments are not to be subject to nationalisation, confiscation, expropriation, requisition,

or any other measure of similar effect, except when this is in the public interest. In such cases, compensation must be provided to the investor based on the market value of the property.

2.5 International agreements

Since 1991, the Armenian Government has moved quickly and effectively to establish friendly and close diplomatic and economic ties with the outside world. Many countries have established diplomatic relations with Armenia – 26 States have opened embassies in Armenia, and more than 60 States have ambassadors and charges d' affaires outside of Armenia who are accredited to Armenia. Armenia has a permanent presence (embassy, consulate, or representation) in over 40 countries.

Armenia has also become an active participant in global issues and concerns by becoming a member of prominent international organisations including the United Nations, World Trade Organisation, Council of Europe, Organization for Security and Cooperation in Europe, and the Black Sea Economic Cooperation.

Armenia has signed bilateral treaties on reciprocal promotion and protection of investments with 37 countries.

Armenia has been a member of the World Intellectual Property Organization (WIPO) since 1993 and the Eurasian Patent Office (EAPO) since 1995.

2.6 Further information

The Armenian Development Agency (www.ada.am) was established in 1998 to facilitate foreign direct investments and promote exports in Armenia. Their website contains a lot of information concerning investing into Armenia, as well as an extensive list of links to websites for governmental organisations, NGOs, embassies, international organisations, culture, education, banks, internet service providers, media and other sites of Armenian interest.

3 Banking, finance and insurance

3.1 Banking system

Armenia has a two-tier banking system. The Central Bank of Armenia (CBA) is Armenia's central bank. Commercial banks operate under the authorisation and supervision of the CBA.

Central Bank of Armenia

According to the Central Bank Law, the primary function of the CBA is to ensure price stability in Armenia.

The highest governing body of the CBA is the Board, consisting of the Chairman of the Central Bank, his or her deputy, and five other members. The Chairman is appointed for six years by Parliament upon the recommendation of the President of Armenia. The other Board members are appointed by the President.

Banking sector

At the start of 1993, Armenia had more than 70 banks. Many of these have since been liquidated, as a result of efforts to increase transparency, improve the quality of assets and services, and strengthen the banking system generally. As of 31 December 2009, 22 commercial banks, with total 391 branches, were registered in Armenia, with total assets of USD 3.6 billion (approximately USD 9 million). Many banks have foreign participation. Foreign participation accounts for 67.4% of the banking sector.

The banking sector accounts for approximately 93% of the assets in the Armenian financial system.

Most banking services are available, and consumer credit facilities are expanding rapidly.

Commercial banks require a license from the CBA. The CBA has established requirements for capital adequacy, minimum statutory capital requirements and minimum regulatory capital requirements. The minimum statutory capital required to register a bank is AMD 5 billion (approximately USD 12.5 million).

3.2 Foreign currency rules

Foreign currency operations are regulated by the 2004 Law on Currency Regulation and Currency Control. Some of the main points to note are:

- Prices for transactions between Armenian residents (including branches of foreign companies) must be quoted and paid in Armenian currency.
- Salaries (other than those paid by international organisations) must be paid in Armenian currency.
- There are no restrictions on conversion between Armenian and foreign currency. Foreign currency accounts may be maintained in Armenian banks.

The official exchange rate for the Armenian Dram is set by the CBA, based on the value of the currency in the market.

3.3 Specialised financial institutions

As at 31 December 2009, Armenia had 25 credit organisations with aggregate assets of USD 207 million, as well as two leasing companies.

3.4 Capital markets

Armenia's two self-regulating securities market organisations – the Central Depository of Armenia and the Armenian Stock Exchange – were acquired by the Swedish operator, OMX in June 2009.

As at 31 December 2009, the market capitalisation of the Armenian Stock Exchange was AMD 53 billion (approximately USD 132.5 million). The three largest issuers accounted for 83.7% of the market capitalisation. Liquidity is low. In 2009, there were only twenty seven trades in the equities market, with a total value of AMD 97.9 million (approximately USD 244,750).

3.5 Insurance

As at 31 December 2009, Armenia had 12 insurance companies with aggregate assets of USD 46 million. The market is regulated by the CBA.

4 Importing and exporting

4.1 Trends in customs policy

The current Customs Code took effect in January 2001. Tariffs of 0% or 10% were introduced for all products. All exports and re-exports are exempt from customs duties.

4.2 Import restrictions

The importation of goods into Armenia may be prohibited when those goods endanger state and national security, public order, human life and health, fauna and flora, as well as environment, moral values of population, items of historical, cultural and archaeological values, persons' property (including intellectual property), rights and legal interests.

Import licenses are required for the importation of a number of products, including plant protection chemicals, medicines, radio-electrical equipment, measuring instruments and livestock.

4.3 Customs duties

Classification of goods

Armenia uses the Harmonised Commodity Description and Coding System for tariff classification, in compliance with the 1984 International Convention on Harmonised Commodity Description and Coding System.

Valuation rules

Armenian customs valuation rules comply with the Agreement on Implementation of Article VII of the GATT 1994. This means that in principle:

- The declared customs value should generally be used as the basis for determining customs duties.
- The customs value should be determined in accordance with the six WTO valuation methods.
- The customs authority is entitled to assess duties on a higher value in certain circumstances.

Tariff rates

The tariff rates are 0% or 10%, the 10% rate being applied mainly on consumer and luxury goods. Rates of duty are ad valorem, specific (in monetary units per unit of goods), or a combination. Countervailing duties may also be imposed.

Free trade agreements

Armenia has ratified bilateral free trade agreements with Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russian Federation, Tajikistan, Turkmenistan and Ukraine.

Excise tax

Excise tax is payable on alcoholic beverages, tobacco products, petrol and diesel fuel.

Value added tax

Unless expressly exempted under the law, imported goods are subject to 20% VAT during customs clearance. The taxable base is the customs value of the goods, plus the amount of any import duties and excise duties (if any). VAT is required to be paid within ten days of importation.

Special rules apply to goods that were exported from Armenia to be processed or repaired. In that case, VAT is imposed based on the value of the service performed by the foreign party. If it is not possible to determine the value of the service, VAT is imposed based on the difference between the customs value of the goods after processing or repair and their declared customs value when they were exported.

Customs processing fee

Customs clearance of goods is subject to customs processing fees, including AMD 3,500 (approximately USD 9) for carrying out customs formalities related to goods and other articles, AMD 1,000 (approximately USD 2.50) for carrying out customs control of cargo up to one ton and AMD 300 (approximately USD 0.75) for each additional ton of cargo, and AMD 1,000 for each document provided by the Customs Authorities.

Payment

Import duties and taxes are payable by the importer in local currency within ten days of the goods crossing the Armenian border.

4.4 Customs duties incentives

Contributions to capital

Property (except for re-saleable goods) contributed by a foreign investor to the capital fund of an Armenian entity may be imported free of customs duty, but will still be subject to VAT. Customs duty must be repaid



(plus penalties for delayed customs payment) if the property is disposed within three years of importation.

Toll manufacturing

Raw materials imported into Armenia for processing under toll manufacturing arrangements enjoy exemption from import taxes and duties provided finished products are re-exported from Armenia within a one-year period.

4.5 Documentation and procedures

All goods crossing the border are subject to customs control, which includes specific procedures aimed at ensuring compliance with customs rules. Other types of border control may also be conducted.

The customs authorities may conduct post-entry audits to verify compliance with customs and tax legislation.

Documentation

A customs declaration form must be presented with a pro forma invoice or a contract indicating the specifications, quantity, and value of goods being imported. Certificates of quality or safety issued or accepted by the National Institute of Standards (SARM) are required for tobacco, alcohol, and oil products. Imported pharmaceutical products must be certified by the Ministry of Health. Registrations to import or export pharmaceuticals are issued by the Ministry of Health and are valid for one year.

Declaration of customs value

The customs value is declared by filing a declaration of customs value, including reference to the valuation method used. The importer must also provide relevant documents to evidence the customs value. If these documents are not available or the customs office has grounded doubts about the data provided by the importer, the customs office may determine the customs value based on information available. This may include information available to the authorities on prices for identical or similar goods.

When the customs value requires review or the importer does not agree with the customs value determined by the customs office, the importer may request the customs office to release the goods for free circulation against payment of import taxes. The importer may then appeal the determination of the customs value by the customs authorities to a higher customs office or to the courts.

4.6 Exports

Restrictions

All exporters must present a contract, a certificate of origin, an export license for specific products, and a certificate of conformity for all ferrous and non-ferrous metals.

Export licenses are required for the importation of a number of products, including pharmaceutical products, textiles and clothing exported to EU countries, objects of art considered part of the cultural heritage, and rare plants and animals.

Export duties

Armenia has no export duties. Exported goods and ancillary services are zero rated for VAT purposes.

Customs processing fee

The same customs processing fees apply as for imports.

4.7 Protection of intellectual property rights

Owners of intellectual property rights may request Armenian customs authorities to register goods containing intellectual property to prevent the illegal import or export of pirated or counterfeited goods. In this case, customs authorities may hold customs clearance of such goods until it can be proven that no breach of intellectual property rights has taken place. If the importer or exporter does not submit sufficient evidence, the customs office may seize the goods and impose penalties.

5 Business entities

5.1 Legal framework

Legal framework for business entities

The primary framework for establishing and operating legal entities in Armenia is found in the Civil Code. Legal entities may be established in the form of joint stock companies (JSCs), limited liability companies (LLCs), additional liability companies, general partnerships or limited partnerships.

The Law on Limited Liability Companies deals with the legal status and the rights, duties and responsibilities of participants of a LLC. The Law on Joint Stock Companies deals with JSCs.

Commercial law

Business relationships are governed by the Civil Code.

5.2 Forms of business entities

Establishing a legal entity in Armenia involves registering with the local state registrar and the tax authorities, as well as opening a bank account and other formalities. Registration with the statistics office may also be required upon request by the authorities.

But it's in Armenian law ...

In most countries, any action that is not expressly precluded by the Charter of a company is permissible. Thus, it goes without saying that the company has the power to establish a subsidiary, branch or representative office in another country.

This is not the case under Armenian law. If a foreign company is to establish a subsidiary, branch or representative office, the Charter must clearly confer such rights.

The rules for registration allow the authorities to request such additional information as they believe they need. Thus, in approximately one registration case in ten, the authorities will raise the question of whether a foreign company may establish a subsidiary, branch or representative office in Armenia. The issue should also be relatively straightforward to resolve, but can be a nuisance factor not always appreciated by new investors.

From a foreign investor's perspective, the choice will tend to be either a LLC, a JSC, a branch or a representative office.

For a 100% investment, using a LLC tends to be more convenient. It is easier and quicker to establish and is less regulated. For investment of less than 100%, consideration should be given to whether a JSC should be established to overcome some of the risks associated with establishing a LLC (see next section).

5.3 Limited liability companies

A Limited Liability Company (LLC) is a legal entity with capital divided into shares. There is no mandatory minimum charter capital requirement for a LLC, except when the law envisages minimum capital requirements for certain types of activity. The liability of its owners is limited to the nominal value of their shares. More than 50% of legal entities in Armenia are LLCs.

There are a number of key points that investors need to be aware of before establishing a LLC:

- Participants of a LLC may transfer their participation in the company's capital to third parties (non-participants) only if the other participants do not exercise their priority right to purchase at the price at which the participation will be sold to third parties.
- A participant may withdraw from a LLC at any time. Upon withdrawal, the LLC is required within six months to repay the value of the participant's share.
- A participant in a LLC may be removed by judicial procedure if the participant's activity or inactivity makes the usual activities of the LLC difficult or impossible. The LLC would be required within six months to repay the value of the excluded participant's share.
- A participant's personal creditors may seize the participant's share in the LLC to settle obligations if the participant's other property is insufficient to satisfy the creditors' claims. If the LLC or the other participants do not use their right to acquire the share within one month, the share would be sold through public auction. If the sale is not successful, property in the Charter Capital of the



Company relevant to the share will be separated for seizure.

- Because a participant may withdraw from the LLC, it is unclear whether contributions to such LLCs should be reported as equity or a liability from the LLC to the participant. This issue should not have any implications from a tax or legal perspective, but may impact on the LLC's ability to obtain finance from external sources and could impact the IFRS accounting.
- A LLC does not generally require a financial audit, unless its annual revenues or book value of assets at the end of the reporting year exceed AMD 1 billion (USD 2.5 million).

If a LLC will be 100% owned by a foreign investor, these issues are likely to have little practical implication. If one or more investors will be involved, however, the issues will need to be addressed when the LLC is formed. Some issues, such as the length of notice required for withdrawal from the LLC and the method of compensation, could be addressed by including appropriate timeframes and constraints in the LLC's Charter.

Formation procedures

A LLC may be established by a single shareholder. The governing document of a LLC is its charter. The charter determines the size of the LLC's statutory capital, the composition and competencies of the governing bodies and the rules for decision-making, the rights and obligations of the participants of the LLC, the rules for exit of a participant, and the transfer of shares of a participant to another person.

Generally, incorporation will take seven working days once correct documents are filed. A LLC is deemed to exist as a legal entity from the date of its state registration. Registration with the tax authorities and obtaining a corporate seal is likely to take three additional days.

Capital structure

There is no mandatory minimum charter capital requirement for a LLC, except when the law envisages minimum capital requirements for certain types of activity.

Relationship of participants, directors and officers

LLCs have two corporate bodies.

The General Meeting of the Company Participants consists of the participants of the LLC, each of whom has votes proportionally to its interest in the company capital. Quorum for a participants' assembly requires the presence of participants holding at least 50% of votes. Most resolutions are approved by a simple majority of the votes present at the Participants' Assembly, although resolutions amending the Charter and a limited number of other decisions must be approved by two-thirds majority of all participants' votes.

The General Director or President is the executive body of a LLC, and is responsible for managing the day-to-day activities of the LLC and representing the LLC against third persons.

Liquidation, receivership

A LLC is liquidated if its participants agree to liquidate the LLC, it is ordered to be liquidated by the court, or

the LLC is bankrupt. Preference in distribution is given, in order, to:

1. Claims of creditors secured by pledge of property.
2. Claims of citizens to whom the LLC is liable for causing harm to life or health.
3. Employees' demands connected with labour relations.
4. Taxes and duties.
5. All other demands.

5.4 Joint stock companies

A joint stock company (JSC) is a legal entity whose share capital is divided into a specified number of shares of equal nominal value. The liability of shareholders in a JSC is limited to the value of their capital contribution.

A JSC may be established as an "open" or "closed" JSC. Shares in an open JSC may be offered to the public, freely transferred, and may ultimately be traded on a stock exchange. By contrast, shares in a closed JSC are distributed initially between its founding shareholders. Existing shareholders in a closed JSC also have pre-emptive purchase rights for shares offered for sale by the other shareholders.

The legal framework for JSCs is similar to that for LLCs. Specific points to note are:

Formation

A JSC may have multiple classes of shares carrying different rights for the shareholders of each class.

Capital

There is no mandatory minimum charter capital requirement for a JSC, except when the law envisages minimum capital requirements for certain types of activity.

Corporate bodies

The highest managerial body of a JSC is the Shareholder's General Meeting. Operational management may be delegated to the Chairman (President) or Board of Directors. Companies must also have a Supervisory Board and an Independent Auditor. The Board of Directors must have at least three members. There is no requirement that any of these individuals be Armenian citizens or residents.

Reporting requirements

Generally, a closed JSC generally does not require a financial audit. However, an open JSC must have its annual financial statements audited and published in the media. A JSC that has publicly issued bonds or other securities must also comply with reporting requirements of the Armenia Securities Commission.

Liquidation

A JSC may be liquidated:

- By a decision of the Shareholder's General Meeting (including expiration of the time period or upon attainment of the goal for which the JSC was established). At least two-thirds of all voting shares in the JSC must be represented at the meeting and the decision should be supported with a 75% majority of the represented shares.
- If a court recognises the JSC registration to be invalid, because of violations of law during the JSC's creation.
- On other grounds stipulated in the law.

The liquidator should make an announcement on company liquidation and the conditions and deadline for submission of creditor claims in media publishing information on state registration of legal entities.

5.5 Partnerships and joint ventures

The Civil Code allows for the establishment of general partnerships and limited partnerships as legal entities, but such vehicles are not widely used. Because partnerships are legal entities, there are no regulatory or legal advantages to conducting business through a partnership.

Joint ventures typically involve establishing a separate legal entity (JSC or LLC) in Armenia. The Civil Code does not recognise the concept of a joint venture without the need to establish a separate legal entity.

5.6 Branches and representative offices

Branches and representative offices are not legal persons and operate in Armenia on behalf of the foreign (or local) companies that they represent. The activities of a representative office are limited to representing the interests of its head office. A branch may perform some or all of the normal commercial activities of the entity to which it belongs.

From a tax perspective, local rules for branches and representative offices are broadly in line with those found in other countries. Local tax rules do not distinguish between a branch and a representative office. However, if the foreign entity is resident in a country with which Armenia has a tax treaty, the entity may be entitled to relief from Armenian income tax under the treaty if its activities in Armenia are limited to representation and support activities.

6 Labour relations and social security

6.1 Labour relations and the Labour Code

Employer / employee relations

Employment conditions in Armenia are generally governed by the Labour Code. Although a new Code was enacted in 2004, it still contains many socialist concepts and protections for employees.

Potential employers should familiarise themselves with the general provisions of the law. Although employers can enter into individual labour contracts with employees, the terms of those agreements may not be worse than conditions guaranteed under the Labour Code. Contracting out of the provisions of the Labour Code is not possible.

Unions

Employers and employees are free to create and join trade and employer unions, and the rights and interests of employees may be represented and protected by the trade unions. However, union membership is not widespread in Armenia and most employment relationships are based on individual

agreements.

6.2 Working conditions

Salaries and wages

Minimum wage levels are prescribed in the law. At the end of 2009, the minimum wage was AMD 30,000 (approximately USD 75) per month.

Wages and other payments to employees must be paid in local currency (dram). Salaries should be credited at least once per month, by the 15th day of the following month.

Working hours

In general, working time is restricted to 40 hours per week, with a five-day working week. An employer may introduce a six-day working week.

Under the law, overtime is restricted. The amount of overtime at an employer's request may not exceed four hours in any two-day period or 120 hours in a year. However, excess working hours by managerial



personnel is not treated as overtime work.

The Labour Code requires overtime to be paid at 2.5 times normal labour rates. However, this can be reduced to double the normal rates through negotiation with employees.

Paid holidays

There are 12 official holidays in Armenia. In addition, an employee's minimum annual holiday entitlement is 28 calendar days. When determining the length of a vacation for purposes of complying with the Labour Code, weekends during the vacation period are counted as vacation days but public holidays are excluded.

Vacation pay should be paid at least three calendar days before the vacation starts, otherwise the employer will be obliged to provide additional paid vacation leave.

Employees who are engaged in part-time studies may be entitled to additional vacation leave.

Paid maternity leave is required for between 140 and 180 days, depending on the nature of the delivery. Payment is funded by the Social Security Fund. A mother may also take extended unpaid leave until her child is three-years old. Her position must be kept open during this period.

Equal opportunities

The Constitution of Armenia and the Labour Code both preclude discrimination based on race, colour of skin, political, religious and other beliefs, sex, ethnic and social origin, property status, place of residence, linguistic or other characteristics.

Termination of employment

Employment contracts may be indefinite or for fixed periods. Employees may terminate the employment relationship at any time by giving at least two weeks notice, unless a longer notice period is contemplated in the employment contract.

The Labour Code permits employers to terminate employment relationships for such reasons as reorganisation, unsuitability of the employee for the position held (two weeks notice is required), unsatisfactory results in a trial period, failure to adequately perform duties, and loss of trust in employees. In such cases, the employer is required to pay two-weeks severance pay. However, care must be taken to ensure that all necessary procedures are properly followed and documented. For example, if the employee does not acknowledge receipt of a formal Order of Termination (or the employee's refusal to accept is witnessed by a third party), the employment will still be treated as ongoing.

An employment contract with a pregnant woman may not be terminated from the day on which the employer receives a medical certificate confirming pregnancy through to one month after her maternity leave concludes.

The form of labour contracts is important

Specific requirements for labour contracts are found in Article 84(1) of the Labour Code. A labour contract must include such things as the place of work, the starting and finishing dates for the contract, the name of the position (including the qualification requirements and functions), the rights and obligations of the employee and employer, the conditions for work, and the amount of remuneration.

A visit from the labour inspectors may end up focusing on whether labour contracts are in the right form, rather than whether there are substantive labour concerns in an organisation. Officials also tend to lack any perception of materiality. Even if a company has only one place of business in Armenia, failing to indicate expressly in the contract that the employee's place of work will be at that location may be subject to an administrative penalty of AMD 50,000 (approximately USD 125) for each affected employee.

6.3 Social security system

Coverage

The social security system in Armenia covers pensioners, workers and their dependants for work-related accidents, disability benefits, sickness and maternity benefits, and family allowances.

Contributions

Mandatory contributions to Armenian social security only apply to Armenian citizens.

The taxable base for contributions (both employee and employer) is not capped.

Employees' contributions

Employees who are Armenian nationals make contributions of 3%. This amount is withheld at source by the employer and is deductible for employees to arrive at taxable income.

Employers' contributions

Employers are required to make monthly social insurance contributions at the following rates:

Gross salary (AMD per month)	Contribution
Up to AMD 20,000	AMD 7,000
AMD 20,000 –100,000	AMD 7,000, plus 15% of the amount exceeding AMD 20,000
AMD 100,000 upwards	AMD 19,000, plus 5% of the amount exceeding AMD 100,000.

Payments for social security must be made by the 20th day of the following month.

If an employer had more than five employees in any month of the previous quarter, returns must be submitted on a monthly basis by the 20th day of the following month. Otherwise, returns should be submitted on a quarterly basis by the 20th day of the month following the reporting quarter.

Contributions for entrepreneurs

Individual entrepreneurs are required to pay a minimum social security payment of AMD 5,000 (approximately USD 13) per month, by the 15th day of the following month. On an annual basis, the first AMD 1.2 million (approximately USD 3,000) of gross income is subject to a 15% contribution, subject to a minimum contribution of AMD 60,000 (approximately USD 150), and the excess is taxable at 5%.

A lower rate of 3% applies to entrepreneurs who are non-VAT taxpayers or subject to presumptive tax (subject still to a minimum contribution of AMD 60,000 (USD 150)).

Penalties for non-compliance

Penalties for non-compliance include:

- Failing to submit on time a declaration, return, or other document required by law is subject to a penalty of between AMD 10,000 and AMD 20,000 (approximately USD 25 to USD 50). If a return is filed more than two months late, a penalty of 5% of the amount of contributions not paid as a result of late filing is imposed for each 15 days of delay, up to a maximum penalty of 100%.
- Failing to pay mandatory social insurance contributions on time is subject to a penalty of between AMD 10,000 and AMD 20,000. In addition, the payer is liable to a fine equal to 0.15% of the amount overdue for each day of delay, up to a maximum of 365 days.
- If during an audit the tax authorities determine that the tax liability shown in the taxpayer's return is understated, they will impose penalties of 50% of the tax assessed. A repeat offence within one year is subject to a 100% penalty. If the authorities identify that an employee has not been properly registered (i.e., no written order and/or written employment contract), a special social security contribution of AMD 60,000 (approximately USD 150) must be made.

6.4 Foreign personnel

Visas

Currently, nationals of Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Ukraine and Uzbekistan may enter under a visa waiver program. Nationals of Serbia and Montenegro can also enter under the visa waiver program, if they have an invitation letter.

Nationals from all other countries require visas to enter Armenia. In most cases, the easiest way to do this is to purchase a 120-day visitor visa at the border crossing point for AMD 15,000 (approximately USD

38). However, nationals of Afghanistan, Bangladesh, Cameroon, China (but not the Hong Kong and Macao Special Administrative Regions), Egypt, India, Iraq, Niger, Nigeria, Pakistan, Palestine, Saudi Arabia, Somalia, Sri Lanka, Sudan, Syria and Vietnam require an invitation letter to obtain a visa for Armenia, and may obtain a visa only from an Armenian diplomatic mission or consular post.

Registration and residence permit

Foreign nationals staying in Armenia for more than three months without leaving the country have to register with the appropriate departments of the Police.

Foreign nationals remaining in Armenia for longer periods may apply for a temporary residence certificate. The process takes around six weeks to

complete and is subject to a fee of AMD 105,000 (approximately USD 263). Currently, the foreign national should not need to surrender his or her passport while the application is being processed. The individual will not need a visa to enter Armenia during the validity period of the residence certificate.

Work permit

Foreign nationals do not have to obtain special work permits to work in Armenia.

The Law on Aliens contains a requirement that local employers obtain a work permit before entering into employment agreements with some foreign nationals. Currently, however, the requisites to make this law effective are not yet in place. Further, if the law were in force, a temporary residence card would be sufficient basis for employment without a work permit.

7 Accounting and audit requirements

7.1 Accounting

International Financial Reporting Standards

The Armenian accounting standards were developed in the mid 1990s, essentially as a translation of the International Financial Reporting Standards (IFRS) of that time. Subsequent IFRS developments were generally not incorporated into the Armenian standards on an ongoing basis.

In 2009, however, the government initiated a full transition to IFRS:

- For banks, IFRS reporting is mandatory from January 2009.
- For credit institutions, payment and settlement organisations, issuers of the securities market, investment companies, regulated market operator, the Central Depository, insurance undertakings, reinsurance undertakings, insurance brokers, IFRS reporting is mandatory from January 2010.

Other entities may prepare and present financial statements in accordance with IFRS by making relevant disclosures. IFRS will also become mandatory for these entities from January 2011.

Once mandatory IFRS reporting is implemented, entities with receivable revenue for the previous calendar year not exceeding AMD 100 million (approximately USD 250,000) will be allowed to apply a special regulation for tax accounting defined by the Government instead of IFRS.

The government published an up-to-date Armenian translation of IFRS in March 2010.

Armenian accounting regulations

Until IFRS reporting becomes mandatory Armenian entities, as well as branches and representative offices of foreign entities, must maintain accounting records and financial statements in accordance with Armenian accounting standards.

Financial statements are prepared for a calendar year and must be prepared in Armenian dram as the reporting currency. The financial statements include

the balance sheet, income statement, cash flow statement, statement of changes in equity, and notes to financial statements (after transition the layout of financial statements will be in line with IFRS).

Financial statements should be submitted to the founders or shareholders of a legal entity and to the relevant state authorities. The balance sheet and income statement should also be submitted to the tax authorities together with the annual Profit Tax return.

Organisations must present their annual financial statements to the tax authorities before 15 April of the year following the reporting year. The annual financial statements must be published together with an audit opinion before 1 July of the year following the reporting year

The chief executive of an entity is responsible for organising accounting in compliance with the requirements of the law. The chief executive is entitled to maintain the accounting through:

- (i) an accounting department;
- (ii) an accountant regarded as an employee of the entity;
- (iii) an organisation providing accounting services or through individual entrepreneur; or
- (iv) personally.

Additionally, the chief executive is obliged to define the accounting policy of the entity, ensure that accounting is maintained, and that financial statements are prepared and presented.

Accounting documentation and information – primary accounting documentation, books, financial statements, documents related to accounting policy, accounting software – must be retained by the organisation for at least five years.

7.2 Audit requirements

Auditing is primarily regulated by the Law on Auditing, which outlines requirements for auditing firms and auditors in individual practice and regulates auditing methodology.



Audit companies are licensed by the Ministry of Finance. To receive a license the audit firm should have at least two qualified auditors who have obtained their professional qualification from the Ministry of Finance. The government also accepts audit qualifications provided by the International Federation of Accountants under its training standards (or by Armenian public organisations under those same standards).

The auditing standards of Armenia are based on the International Standards on Auditing as they existed in 2005.

Audits required by law

Under Armenian law, audits are mandatory for a range of enterprises, in particular:

- Open joint-stock companies.
- Banks and similar financial institutions.
- Stock exchange participants.
- Large-scale companies.

Publication of financial statements

Open joint stock companies, banks and branches of foreign banks are required to publish their annual financial statements. The deadline of publishing annual financial statements is 1 July of the year following the reporting year.

With effect from the 2009 reporting year, entities whose revenues for the previous year or the book value of whose assets at the end of the year exceeded AMD 1 billion (approximately USD 2.5 million) must also publish their annual financial statements.

Only qualified chief accountants or qualified auditors have a right to sign the published financial statements of commercial entities.

Financial statements may be published in printed media, internet or disseminated in brochures.

Annual financial statements may be published only after undergoing an audit, and must be published together with the audit opinion.

8 Tax system and administration

8.1 Tax system

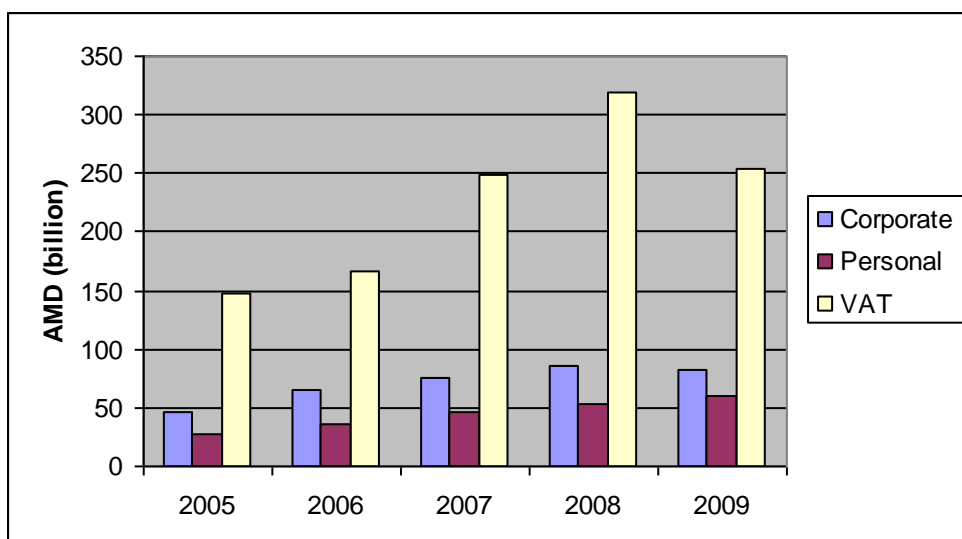
The Armenian tax system is continuing to evolve. There are a number of practices that make compliance challenging. Frequent changes in law create confusion, because it is difficult to taxpayers to keep up to date and old laws are often not updated to ensure consistency with the new laws. Armenian tax laws are adapted from several foreign legal systems (France, United Kingdom, Russia), but are often not adapted to reflect the Armenian legal environment. This can result in inconsistency between Armenian tax laws and internationally accepted practices.

The overall tax rate in Armenia is moderate. The World Bank study, *Paying Taxes 2010: The global picture*, ranked Armenia 69th out of 183 countries.

A presumptive tax regime is available for certain types of businesses. These rules require qualifying entities and private entrepreneurs to pay a fixed amount of tax, instead of accounting for profit tax/income tax or VAT. The rate of tax depends on the activity. However, a Government initiative is underway to transition taxpayers from presumptive tax to the general taxation rules.

From 1 January 2010, most financial organisations, as well as companies with revenue or assets exceeding AMD 1 billion (approximately USD 2.5 million), were required to submit their returns, documents and other information electronically. From 1 July 2010, organisations whose turnover exceeded AMD 100

million (approximately USD 250,000) in the previous



year will also be required to submit tax returns electronically.

8.2 Direct and indirect tax burden

Taxation accounts for almost 90% of government revenues. More than 70% of this is collected through VAT, corporate profits tax and individual income tax.

The trend in income tax and VAT collections for the period 2005 to 2009 is illustrated in diagram 1. Tax collections increased rapidly from 2005 to 2008. Nevertheless, the President was dissatisfied with the State Tax Service, and in August 2008 merged the State Tax Service and the State Customs Committee into a new State Revenue Committee. Collections fell in 2009 in line with the financial crisis.

8.3 Principal taxes

The Law on Taxes, which provides the general framework for taxation in Armenia, provides for six taxes that may be imposed. Profit tax (for companies), income tax (for individuals), excise tax and value-added tax (VAT) are collected at the national level. Property tax and land tax are collected at the municipal level.

Taxpayers subject to presumptive taxation may be relieved from some or all of these taxes.

Employers and employees also make mandatory contributions to the state social security fund.

8.4 Legislative framework

Taxes and levies, as well as penalties for non-compliance, may only be established by laws enacted by Parliament.

The policy intent underpinning the law is not always clear. Consequently, it is not uncommon for the tax authorities, either explicitly through clarifications or implicitly based on common practice, to fill in gaps in the laws to reflect what the tax authorities believe the legislators intended. In principle, the law should override an incorrect issuance or practice of the tax authorities. Nevertheless, it is prudent to consider tax authorities interpretations and the risk of conflict with the tax authorities before taking a position based on the law.

8.5 Tax treaties

Armenia has tax treaties with 30 treaties in force as at 1 January 2010. A tax treaty with Croatia will come into force on 1 January 2011. A summary of withholding rates under the various treaties is provided in the Appendix.

Taxpayers generally require confirmation from the tax authorities before claiming relief under a treaty. As part of the process, the non-resident should obtain a certification of residence from their hold country tax authorities, in the form stipulated by the Armenian government. If the foreign authorities will not certify in the stipulated form, a certificate of tax residence from the foreign tax authorities may be obtained instead. If a certificate of residence is prepared in a language other than English or Russian, it must be properly legalised (apostilled) and then translated into the Armenian language using a notary in Armenia.

Armenia does not honour pre-independence tax treaties entered into by the former Soviet Union.

8.6 Administration of the tax system

All national taxes are administered by the Tax Inspectorates of the State Revenue Committee (SRC). The collection of property tax and land tax is implemented by municipal governments.

8.7 Registration requirements

Taxpayers who obtain state registration are required to register with the Tax Inspectorate within one month from that state registration and to obtain a tax number. The tax registration is undertaken through the local tax inspectorate where the individual or business is located.

8.8 Tax returns and payments

(Corporate) profit tax

The annual profits tax return for resident entities must be filed by 15 April. The corresponding tax is payable by 25 April.

Taxpayers are required to make advance profits tax payments by the 25th day of each month. Each advance payment is equal to 1/16th of the profits tax



paid for the previous year. For payments before the previous year's tax is calculated (e.g., January to March), tax is paid based on the last filed tax return, and an adjustment is made in the first advance tax payment made after the previous year's tax is calculated to correct the amount paid. If advance payments exceed the profits tax liability for the year, the excess may be refunded.

Advance payments are not required if a taxpayer's profit for the proceeding year was less than AMD 500,000 (approximately USD 1,250,) or the taxpayer was not a VAT payer in the preceding year. Thus, newly established companies do not need to make advance payments until 25 April of the year following the start of operations.

Armenia also has a monthly minimum profits tax. If the advance profits tax payable is less than 1.0% of revenues for the previous month less depreciation charges (up to a maximum of 50% of revenues), the excess is paid as a minimum profits tax. The minimum profits tax is applied against profits tax payable for the year. Any excess is applied against the profits tax liability for the subsequent year.

Branches of foreign companies pay advance profits tax bi-annually, but only if their profit for the proceeding year exceeded AMD 2 million (approximately USD 5,000). Each advance payment is equal to 25% of the profits tax paid for the previous year. Branches and representative offices are not subject to the minimum profits tax. The annual tax return for branches and representative offices is filed by 15 April. However, the corresponding tax only needs to be paid within one month of receiving a

payment notification from the tax authorities about the final amount of the calculated profit tax.

(Individual) income tax

Individuals who receive income that has not been subject to Armenian tax at source are required to file a personal tax return by 15 April of the following year. The corresponding tax must be paid by 1 May.

Value added tax

Generally, VAT payers should file VAT returns on a quarterly basis. However, taxpayers with revenues (excluding VAT) in the previous calendar year exceeding AMD 100 million (approximately USD 250,000) are required to file VAT returns monthly.

VAT payments must be made and VAT returns filed within 20 days following the end of the reporting period. A separate report with information on sales and purchase invoices exceeding AMD 100,000 (approximately USD 250) must be filed within 25 days following the end of the reporting period.

8.9 Assessments

With the exception of land tax and property tax, taxpayers make returns and payments on a self-assessment basis. However, if the tax authorities determine that the tax shown on the return is incorrect, they may assess taxes within three years from the end of the year in which the return is filed.

The amount of a tax assessed, as well as any fines and penalties, should be paid within ten days from the Tax Inspectorate presenting the assessment.

8.10 Appeals

Assessments may be appealed administratively or through the court system. The initial appeal at the administrative level is made to the Appeals Committee of the SRC.

An administrative appeal must be filed to the relevant level of the tax administration within 30 calendar days of receiving an assessment, or within one month of receiving official advice that an administrative appeal has been rejected at a lower level.

The tax authorities must respond to the appeal within 30 calendar days from the first working day following the day the written complaint is filed. If a response is not given within that time period, the arguments in the complaint are deemed to have been accepted.

At any stage of the process, or if the SRC rejects the appeal, a taxpayer is entitled to pursue an action through the courts instead.

The tax authorities have a right to suspend the collection of taxes while an assessment is being appealed, but the law does not oblige the authorities to suspend collection.

8.11 Withholding taxes

Employers are required to withhold personal income tax at source on a monthly basis from their employees' salaries.

Commercial organisations non-commercial organisations are required to withhold 11% tax from payments to physical persons, unless the parties have signed a contract that indicates the individual's TIN, passport data, domicile in Armenia and the number of the state registration certificate issued when business activity commenced.

Payments to non-resident individuals and non-resident entities are subject to the following withholding tax rates:

- Payments for insurance, reinsurance, and transportation are taxed at 5%.
- Other income received from Armenian sources is taxed at 10%.

Withholding tax rates for non-residents may be reduced under a relevant tax treaty.

The payment date for individual withholding taxes is the 20th day of the month.

Withholding taxes on payments to foreign legal entities must be paid to the budget by the 5th day of the following month. Reports are filed quarterly by the first day of the second month following the quarter.

8.12 Tax audits

The tax authorities may carry out scheduled audits a maximum of once each year. Business entities must be notified of the audit in writing at least three days

before the scheduled audit. For normal business entities, the scheduled audit should be carried out within 15 business days, although the period may be extended by up to ten business days. For companies whose annual revenue exceeds AMD 3 billion, the period may be extended by up to 75 business days.

Before starting an audit, the tax inspector must present a written order to the taxpayer outlining the scope and period of the tax audit. The written order specifies the names of the officials who may participate in the audit and should be submitted at least three business days before conducting the audit.

The tax authorities currently audit around one-third of active taxpayers each year.

The tax authorities' approach to tax audits can be relatively unsophisticated. For many years, a significant part of the Armenian economy has been outside the formal sector and potentially significant levels of unreported income were relatively common. As a result, many tax inspectors start an audit with a preconceived idea that all taxpayers evade tax and of how much additional tax should be collected. The audit process may then be not so much about substantive tax issues that are identified during the audit, but rather in identifying sufficient disputable points (e.g., documentation quality, whether expenses are necessary) to facilitate an acceptable audit settlement. It is understood that some of the initiatives in the Tax Administration Strategy Program for 2008-2011 (see Chapter 8) aim to address such concerns, but the effects are yet to be observed in practice.

8.13 Tax representatives

From 1 January 2010, the tax authorities may appoint a representative to be stationed in a taxpayer's premises to observe and examine records and documents directly related to the process of delivery, transportation and sale of products.

A tax representative may be appointed if a taxpayer's revenue for the previous year (excluding indirect taxes) exceeded AMD 4 billion (approximately USD 10 million), the customs value of goods imported by the taxpayer under the "Importation for Free Circulation" rules within any three-month period in the year exceeds AMD 500 million (approximately USD 1.3 million), there is a discrepancy of more than AMD 100 million (approximately USD 250,000) between data submitted in a taxpayer's return and measurement procedures conducted by the tax authorities (e.g., estimated revenue based on observing customers), or the taxpayer makes a written request to have a tax representative stationed on its premises.

The total period for supervision may be up to 183 calendar days for one calendar year or 250 working days for two calendar years.

8.14 Penalties

Penalties are often specified in terms of a multiple of the monthly "minimum salary" used for penalty

purposes, which is currently AMD 1,000 (approximately USD 2.50).

Multiple penalties may be imposed. Liability is assessed by the tax authorities.

Some of the more significant penalties are summarised below.

Failing to register with the tax authorities

Failing to register with the tax authorities within one month from state registration is subject to a penalty of between AMD 10,000 and AMD 20,000 (approximately USD 25 to USD 50).

Late filing or reporting

Failing to submit to the tax inspectorate on time a declaration, return, or other document required by law is subject to a penalty of between AMD 10,000 and AMD 20,000 (approximately USD 25 to USD 50). If a tax return is filed more than two months late, a penalty of 5% of the amount of tax not paid as a result of late filing is imposed for each 15 days of delay, up to a maximum penalty of 100%.

Failing to submit (or publish) financial statements to the state authorities on time is subject to a penalty of AMD 50,000 (approximately USD 125). Failing to submit (or publish) the financial statements within 30 days of the penalty is subject to a further penalty of AMD 500,000 (approximately USD 1,250). Publishing financial statements signed by an uncertified accountant is subject to a penalty of AMD 50,000. A person who was assessed for the same violation in the previous year is subject to a penalty of AMD 250,000 (approximately USD 625).

Failing to submit the annual information on income paid to individuals by 15 April of the subsequent year is subject to a penalty of AMD 5,000 (approximately USD 13) for each individual.

If the report on sales and purchase invoices exceeding AMD 100,000 is incorrect or incomplete, a penalty of AMD 5,000 (approximately USD 13) will be charged for each incorrect or missing entry.

Late payment of tax

Failing to pay taxes on time is subject to a penalty of between AMD 10,000 and AMD 20,000 (approximately USD 25 to USD 50). In addition, the taxpayer (or tax agent) is liable to a fine equal to 0.15% of the amount of the tax overdue for each day of delay, up to a maximum of 365 days.

Understated tax liabilities

If during an audit the tax authorities determine that the tax liability shown in the taxpayer's return is understated, they will impose penalties of 50% of the tax assessed. A repeat offence within one year is subject to a 100% penalty.

If losses in a tax return are overstated and are not voluntarily disclosed and corrected before a tax

inspection, a penalty amounting to 20% of the overstated loss is payable.

Tax evasion

Creating false documents for sales or expenses may be subject to a fine of up to AMD 2 million (approximately USD 5,000) or imprisonment for up to five years.

Evading taxes, duties or other mandatory payments by not submitting tax reports, returns or documents or entering clearly false data into those documents, may be subject to a fine of AMD 200,000 to AMD 300,000 (approximately USD 500 to 750), the deprivation of the right to hold certain posts or practice certain activities for up to five years, or imprisonment of up to two years.

Entering clearly distorted data on income and expenses into a tax return declaration by individuals may be subject to a fine of between AMD 100,000 and AMD 500,000 (approximately USD 250 to USD 1,250) or imprisonment of up to two months, if the loss of tax to the authorities exceeds AMD 200,000 (approximately USD 500).

Excise tax

If the tax authorities determine that excise taxes have been underpaid, a 100% penalty will be imposed.

If more than one adjusted excise tax report is filed for each reporting period, a penalty of AMD 200,000 (approximately USD 500) will be imposed for each of the second and subsequent adjusted returns.

Selling goods without appropriate excise tax stamps or with forged excise tax stamps is subject to a penalty of up to AMD 1 million (approximately USD 2,500). The fine depends on the aggregate value of the goods sold.

Illegal and unlicensed activities

A person engaged in activity that is subject to licensing either without holding the requisite license or operating outside of the scope of that license is subject to a fine equal to 50% of the illegal sales. If a repeat offence occurs within one year, a 100% fine will be imposed.

A person engaged in activities prohibited by law will be subject to a fine of 100% of illegal sales.

Failing to display registration details

Businesses failing to display their tax registration details will be subject to a penalty of AMD 50,000 (approximately USD 125) for a first offence, and AMD 500,000 (approximately USD 1,250) for a subsequent offence.

8.15 Tax clarifications

Taxpayers may request written explanations from the tax authorities on the application of specific tax laws. Such explanations are not legally binding and do not provide solid protection against tax assessments and penalties. However, in practice a written explanation

may be useful in resolving disputes with local tax

authorities regarding uncertainty in the tax legislation.

9 Taxation of corporations

9.1 Corporate tax system

Companies

Armenian entities and foreign entities doing business in Armenia through a permanent establishment are liable for corporate income tax. The standard rate is 20%.

Taxpayers engaged in agricultural production are exempt from tax on that income.

Taxpayers engaged in certain activities (e.g., car repair service, casinos, public baths and showers, gas refilling stations for motor vehicles, billiard games, organisation of computer games) are subject to presumptive tax. Under that system, the taxpayer pays a fixed amount of tax based on criteria specified in the law, and will not be required to pay profit tax or VAT. The rate of tax depends on the activity undertaken.

Dividends

Generally, companies must deduct withholding tax from dividends paid to foreign entities at a rate of 10%. A lower rate may apply under a relevant tax treaty.

Territoriality

Resident entities are legal and business entities whose personality or existence is established under Armenian law. Non-resident entities are those whose existence is established under foreign law.

Resident entities are liable to Armenian tax on their worldwide income. Foreign taxes should be available for credit against Armenian tax liabilities, up to the amount of Armenian tax payable on the foreign income. Foreign entities are liable to Armenian tax only on income from sources in Armenia. In broad terms, income will have a source in Armenia if:

- The income arises from activities performed or property located in Armenia; or
- In the case of passive income (e.g., dividends, interest, royalties), financial services and insurance services, the income is paid by a resident of Armenia.

Consolidation

There is no system of group taxation in Armenia. Members of a group must file separate tax returns. There are no provisions to offset the losses of group members against the profits of another group member.



Permanent establishments

The domestic definition for a permanent establishment essentially adopts the definition for permanent establishment found in the OECD Model Tax Convention.

When a foreign company conducts business in Armenia through a permanent establishment and maintains separate accounting records for that permanent establishment, taxable income should be determined on the same basis as for domestic entities. The Law on Profit Tax indicates that a permanent establishment is taxable on dividends received from Armenian companies and may not carry forward losses, which differs from the treatment of domestic entities. However, it may be able to overcome this restriction under a relevant tax treaty.

If it is not possible to determine taxable profit based on the "direct" method (taxable income less deductible expenses), income would be determined based on a method agreed between the taxpayer and the tax authorities. The law explicitly recognises the allocation method (the taxpayer allocates a portion of its worldwide income and expenses to Armenia) as a possible approach.

Armenia has no special tax rules for non-commercial representative offices established to engage in liaison type activities. Such offices are subject to the normal corporate income tax, but an exemption from income

tax may be available under a relevant tax treaty if the activities of the representative office are not sufficient to constitute a permanent establishment for the foreign entity.

9.2 Incentives

Taxpayers engaged in agricultural production are exempt from tax on that income.

To encourage development of the Armenian capital market, Parliament enacted a law in June 2009 that will reduce the profit tax burden of listed companies by up to AMD 300 million (approximately USD 750,000) per year from 2009 to 2012. The incentive applies to resident companies (other than with regulated prices) listed on the Armenian Stock Exchange with at least 20% of their shares publicly held by 100 or more shareholders. Provided such companies prepare and publish their financial statements under IFRS, they will be entitled to a 50% reduction in their profit tax (up to a maximum of AMD 300 million per year).

9.3 Gross income

Accounting period

The reporting year for companies follows the calendar year.

Business profits

Taxable profits are defined to be the difference between a taxpayer's gross income and deductible expenses. Gross income encompasses all revenues received by a taxpayer from all economic activities, unless the revenues are expressly exempted under the law. Deductible expenses encompass all necessary and documented expenses that are directly related to conducting business or earning profit, unless a specific provision in the law restricts the deduction.

Accounting for income

Income should be recognised using the accrual method:

- Income should be recognised when an unconditional right to receive the income exists, or when a taxpayer has fulfilled all of the obligations for a transaction or contract.
- Income from services should be recognised when the provision of services is complete.

Exempt income

Dividends derived by an Armenian entity from another Armenian entity are exempt from tax.

9.4 Deductibility of expenses

Business expenses

Properly documented expenses that are necessarily incurred in the furtherance of a taxpayer's business activities should be deductible, unless a specific provision in the law says otherwise (refer below).

Non-deductible expenses

The following are the main items that are not deductible for corporate income tax purposes:

Expenses that are not supported by relevant documents are not deductible.

- Expenses incurred for advertising outside Armenia are limited to the greater of 3% of gross income or 20% of the value of services or goods exported from Armenia.
- Training of staff outside Armenia is limited to the lesser of 4% of the gross income of the reporting year or AMD 3 million (approximately USD 7,500) per employee.
- Expenses for foreign trips are limited to 5% of the gross income of the reporting year.
- Representative expenses are limited to the lesser of 0.5% of the gross income of the reporting year or AMD 5 million (approximately USD 12,500).

Accounting for expenses

Expenses should be recognised on an accrual basis. Expenses are matched to the sales to which they relate.

Depreciation

Fixed assets are required to be depreciated using the straight-line method. The minimum periods for depreciating fixed assets are:

Description of assets	Minimum depreciation period
Hotels, resorts, rest houses, educational institutions	10 years
Other industrial and commercial buildings, constructions and transmission devices	20 years
Robot equipment and assembly lines	3 years
Calculating devices and computers	1 year
Fixed assets with the value up to AMD 50,000 (approximately USD 125)	1 year
Industrial and commercial buildings, constructions and transmission devices located in a designated disaster area (currently Gyumri)	1 year
Other fixed assets	5 years

Land may not be depreciated. Intangible assets may be amortised using the straight-line method over the lesser of the asset's useful economic life or ten years.

Expenses on fixed assets

Expenses incurred in the repair and maintenance of a fixed asset are deductible, unless the expense improves the condition of the fixed asset. The deduction is limited to 10% of the cost of the asset.

Any excess is capitalised and included in the base for depreciation purposes.

Interest

As a general rule interest will be deductible if the related debt is used to fund business activities of the taxpayer. The maximum deductible interest rate is capped at twice the official CBA rate (at 30 April 2010, the deduction is capped at 26%).

Armenia does not have thin capitalisation rules.

Foreign exchange

Realised foreign exchange gains and losses are taxable/deductible.

Bad and doubtful debts

Bad debts may be claimed as a deduction.

Royalties and services fees

Royalties and service fees are deductible payments.

Leasing

Lease payments on operating leases are deductible. The lessor would claim a deduction for depreciation of the leased assets.

Financial leasing is treated for tax purposes as if a sale had been made. The lessee would include the value of the property in the relevant group of fixed assets and claim depreciation charges. The lessee would also deduct the interest and commission elements of the lease payments in the period in which they are payable. Similarly, the lessor would recognise taxable income for the total principal amount of the lease at the time when the asset is transferred, and would recognise the interest and commission element of the payments over the term of the lease.

Employee remuneration

Employee remuneration is deductible.

Social security contributions

Taxable income is reduced by the amount of mandatory employee contributions for social security.

Other deductions

Expenses incurred on preparatory, drafting and research activities, and geological research for the extraction of natural resources should be capitalised and amortised over their useful life (or over a minimum of 10 years if their useful life cannot be determined).

Expenses on scientific research, experiments and design may be deducted at the time incurred.

Charitable donations and contributions to non-profit organisations are deductible in amounts up to 0.25% of gross income.

Armenian taxes, other than income tax, are generally deductible. Revenues and expenses are determined net of VAT.

Losses

Companies are entitled to carry forward losses to the five subsequent income years.

9.5 Related party transactions

The Profits Tax Law permits the tax authorities to adjust prices for tax purposes when the conditions of a transaction between a non-resident and a third person differ from usual practice. The implementing rules are not well developed, so the rule has limited application in practice.

9.6 Other taxes

Excise tax

Excise tax is payable on alcoholic beverages, tobacco products, petrol and diesel fuel, whether imported or produced domestically.

Land tax

Land tax is paid by landowners and the permanent or temporary users of state owned land. Tax on rented land is levied on the lessor. The land "cadastre" (valuation system) is used to determine the value of the land. Land tax for agricultural lands is calculated at 15% of the net income determined by the "cadastral" evaluation. For non-agricultural land the rate is 0.5% to 1.0% of the "cadastral" value of the land.

Property tax

Property tax is assessed on buildings, motor vehicles and means of water transport. The tax base for buildings is cadastral value determined based on original cost and subsequent three-yearly revaluations by the relevant state authority. The tax rate on public and industrial buildings is 0.3% annually of the property value.

Local taxes and duties

Land and property taxes are assessed by the local authorities. There are no other local taxes and duties affecting business.

9.7 Holding companies

There are no rules to permit the grouping or consolidation of income and losses among a commonly owned group. Dividend income received from another company is not subject to tax.

10 Taxation of individuals

10.1 Territoriality and residence

Individuals are classified into two categories for income tax purposes:

- Residents are liable for tax on their worldwide income. The standard rate is applicable to most types of income, including salary, dividends, royalties and investment income.
- Non-residents are liable for tax only on their Armenian source income.

Tax residence

Individuals are tax resident in Armenia if:

- They are physically present for 183 days or more in any consecutive twelve-month period commencing or ending in the tax year.
- Their centre of vital interests is in Armenia.
- They are in the civil service of Armenia.

Individuals who do not meet these conditions are non-

residents.

10.2 Tax rates

Income from royalties, interest (if not exempt), sale of property (if not exempt) and lease of property is subject to 10% tax. If paid by a tax agent tax should be withheld at source. Tax agents include Armenian legal entities, individual entrepreneurs and branches or representative offices of a foreign company.

Other income paid by a tax agent is subject to final withholding on a monthly basis:

- The first AMD 80,000 (approximately USD 200) per month of taxable income is taxed at 10%.
- The excess is taxed at 20%.

Other income not received from tax agents is taxed on an annual basis:

- The first AMD 960,000 (approximately USD 2,400) per year of taxable income is taxed at 10%.
- The excess is taxed at 20%.

Taxation of benefits

In principle, one would not expect tax issues to arise when an employer makes tea and coffee available to its employees. A prudent employer would consider such an expense to be a necessary cost to maintain the morale of the workforce (meeting the test for deductibility), while the inability to value the benefit to each employee in monetary terms means that no taxable income should arise to the employees.

In practice, the authorities may challenge deductibility on the grounds that the employer is not contractually obliged to provide tea and coffee to its employees (so the expense is not legally necessary). They have also been known to assess personal taxes on the employer, even though the law lacks a mechanism to impose such tax (something that is recognized informally at senior levels of the tax administration).

Because of such practices, some Armenian companies take the path of least resistance and do not deduct expenses for tea and coffee.

10.3 Private entrepreneurs

Taxpayers engaged in certain activities are subject to presumptive tax. Under that system, the taxpayer pays a fixed tax based on the precondition data and ratios defined by law, and will not be required to pay income tax or VAT. The rate of tax depends on the activity undertaken.

10.4 Gross income

Resident taxpayers are liable to pay tax in respect of any income received or credited in Armenia or abroad during the reporting period, except for items specifically exempted from tax under the law.

Employment income

All income received or credited from employment in monetary form or in kind during a calendar year is subject to personal income tax.

Income from independent activities

Income from independent activities is subject to the standard rate, unless the individual is covered by the simplified or presumptive tax rules.

Rental income

Gross revenues from property leases are subject to 10% tax.

Income from prizes and winnings

Income in the form of prizes (other than cash prizes from the state lottery) and winnings in excess of AMD

10,000 (approximately USD 25) per payment is taxed at the standard tax rate.

Investment income

Gains from the sale or exchange of shares or securities are exempt from tax.

Dividends are exempt from tax.

Interest income is exempt if received from state securities. In other cases, a 10% rate applies.

Gross royalties are subject to 10% tax.

Disposal of real estate and movable property

The tax treatment of dispositions of property depends on the tax status of the purchaser. If the purchaser is a legal entity or an individual entrepreneur, a 10% tax should be withheld from the gross sale price. In other cases, the income is exempt from tax.

10.5 Tax-exempt income

In addition to the exemptions indicated in the discussion on gross income, the following are the main items of income that are exempt from taxation:

- State benefits, with the exception of benefits for temporary work disability and for the care after a sick member of the family.
- Pensions.



Taxation of expatriates

There are some interesting quirks in the Armenian tax rules for non-residents:

- Under current practice, an individual is treated as tax resident in the year of arrival only if that person has been in Armenia for 183 days by the end of that tax year.
- Income from labour activities has a source in Armenia only if paid through a local payroll.

Thus, salaries paid through a foreign payroll will not be subject to Armenian tax unless the recipient is tax resident in Armenia.

- Alimony.
- Property and cash received as an inheritance.
- Insurance compensation.

10.6 Deductions

Business

Documented expenses incurred directly and exclusively for the purpose of generating business income are deductible.

Non-business

A taxpayer may deduct the amount of contributions to religious, public and other non-profit organisations, up to a maximum of 5% of taxable income.

An individual is also entitled to a personal allowance deduction of AMD 30,000 (approximately USD 75) for each month income is received.

Social security contributions

Taxable income is reduced by the amount of mandatory employee contributions for social security.

10.7 Foreign tax credits

Tax residents are allowed to credit foreign taxes paid on income received abroad against their Armenian tax liabilities. The amount of foreign tax credit is limited to the amount of Armenian tax that would arise from the equivalent income in Armenia.

10.8 Taxation of non-residents

Non-resident individuals are subject to Armenian tax only on income that has a source in Armenia. For individuals, any income received from Armenian

labour contracts, business activities performed in Armenia, or capital employed or property used in Armenia will have an Armenian source.

Income earned by non-residents from sources in Armenia is generally taxed at the same rate as income derived by residents. Relief from Armenian tax may be available under a relevant tax treaty.

10.9 Tax compliance

Obligations of withholding agents

Any income payment by a tax agent to an individual is subject to withholding, unless the payment is to an individual entrepreneur and the parties have signed a contract that indicates the individual's TIN, passport data, domicile in Armenia and the number of the state registration certificate issued when business activity commenced. If this requirement is not met, payments from commercial organisations and private entrepreneurs are subject to 11% withholding tax.

Currently, withholding tax from payments to individuals must be transferred to the State Budget not later than the 20th day of the following month when income was paid or salary was accrued.

Tax returns for individuals

Armenian tax residents who receive income that has not been subject to Armenian tax at source are required to file a personal tax return by 15 April of the following year. The corresponding tax must be paid by 1 May.

In addition, tax residents who have income for a year (including exempt income) exceeding AMD 8 million (approximately USD 20,000), or are involved in real estate transactions with total value exceeding AMD 50 million (approximately USD 125,000) or movable property transactions with total value exceeding AMD 8 million, must file a declaration of income and net worth by 15 April of the following year.

It appears that the main objective of the declaration is to identify the amount of exempt income derived by Armenian tax residents who otherwise would not file a tax return. Thus, if a declaration is not filed or an incorrect declaration is filed, the main penalty is a 10% charge on the amount of untaxed income that is not reported if the taxpayer cannot prove the source of that income. Administrative penalties for non-compliance apply only if a declaration is not filed, the tax authorities issue a warning, and the taxpayer then fails to file the declaration within 30 days.

11 Value added tax

11.1 Introduction

Armenia's current value-added tax (VAT) law was enacted in 1997 and is based loosely on the principles of the EU Sixth Directive.

Armenia operates the input-output model of VAT. Persons subject to VAT deduct the VAT paid on their inputs from the VAT charged on their sales and account for the difference to the tax authorities.

The standard rate of VAT on domestic sales of goods and services and the importation of goods is 20%. Exported goods and related services are zero-rated.

11.2 Taxable threshold

The liability to account for VAT is based on taxable turnover for transactions implemented in the previous calendar year. If those revenues exceed AMD 58.35 million (approximately USD 145,875), the taxpayer must account for VAT on all sales. If the previous year's revenues were less than AMD 58.35 million (e.g., the taxpayer is in the first year of operations), the taxpayer is obliged to account for VAT only on sales in that year that exceed AMD 58.35 million.

Taxpayers whose revenues are below the AMD 58.35 million threshold may voluntarily elect to account for VAT.

11.3 Scope of VAT

Unless there is an express exemption in the law, VAT applies to:

- Supply of goods and services where the place of supply is in Armenia, including when supply is made without consideration; and
- Importation of goods into Armenia.

Place of supply for goods

The place of supply for goods is the place where the goods are located when they are sold. For goods that are to be delivered, the supply takes place where the goods are located when they are dispatched.

Place of supply for services

The general rule is that services are supplied in the place where the service provider performs the services. If the place of performance is uncertain,

services are considered to be supplied in the place where the person's business is located.

Specific place of supply rules apply to the following services:

- Services related to real estate are supplied in the place where the real estate is located.
- Transportation services are supplied in the place where the transportation passengers or cargo originates.
- Services related to culture, art, sport, science, education and public health, ancillary support for transportation, and the assessment or repair of movable property are supplied in the place where the services are performed.
- The lease of transportation vehicles is supplied in the place where the lessor implements business activity, or if no such place exists, in the place of domicile or residence of the lessor.
- Cross-border postal and telecommunication services are supplied in the country of destination.

Special rules also apply to services related to the transfer of intellectual property rights, advertising, consulting, engineering, legal, accounting, expert, translating, data processing, the provision of software and information, banking, financial and insurance services, and the lease of movable property (other than transportation vehicles). When such services are provided by a VAT payer to a non-resident, or by a

VAT "registration"

The Armenian VAT rules do not explicitly contain the concept of a VAT-registered person. Instead, a person becomes a "VAT-payer" once their revenues exceed a certain threshold or they voluntarily elect to account for VAT.

There are also no transition rules concerning VAT on goods on hand when a person moves in or out of the VAT base.

New businesses need to exercise care to ensure they do not lose the right to recover input tax because the VAT is paid before the business becomes a VAT payer.

non-resident to a VAT payer:

- They are supplied in the place where the recipient of the services implements business activity or has a permanent office (i.e., if the recipient has a permanent office in Armenia, the services are subject to VAT).
- If the recipient does not implement business activity and has no permanent office, the services are supplied in the place of residence of the recipient.

Zero-rating also applies to the supply of international transport services (including transit through Armenia) and toll manufacturing services.

VAT on importation

Unless expressly exempted under the law, imported goods are subject to 20% VAT during customs clearance. The taxable base is the customs value of the goods, plus the amount of any import duties and excise duties (if any). The imposition of VAT by Customs is not affected by whether the importer is registered with the tax authorities. VAT is required to be paid within ten days of importation.

Special rules apply to goods that were earlier exported from Armenia to be processed or repaired. In that case, VAT is imposed based on the value of the service performed by the foreign party. If it is not possible to determine the value of the service, VAT is imposed based on the difference between the customs value of the goods after processing or repair and their declared customs value when they were exported.

11.4 Zero rating

The export of goods and the supply of services that are ancillary to the export of goods are zero-rated.



Advertising, consulting, engineering, legal, accounting, translation, data processing, banking, financial and insurance services provided to non-residents are zero-rated if the non-resident's place of business is outside Armenia.

11.5 Exempt supplies

Armenian law distinguishes VAT-exempt transactions from transactions that are outside the scope of VAT. From a practical perspective, however, the distinction is not important. In either case, a person making such sales will not be entitled to claim an input tax credit against those sales.

A number of transactions are exempt from VAT under Armenian law. Some of the more common exemptions are:

- Most financial operations and transactions carried out by banks and lending organisations. However, exemptions are defined with respect to specific transactions, so transactions must be reviewed individually to confirm whether an exemption applies.
- Tuition for secondary, professional, and high schools.
- Education material such as music books, albums for drawing, children's and school literature, school educational publications, and scientific and research works.
- Sales of veterinary medicines, chemicals used in agricultural production, fertilizers, and agricultural plants and seeds.
- Services related to the care of children in preschool institutions, and the care of persons in boarding-schools, children's homes, institutions caring for disabled children and invalids, and nursing homes.
- Sales of newspapers and magazines.
- Insurance and reinsurance operations, as well as operations related to pension insurance, performed by insurance mediators and agents.
- The supply of goods and services relating to the implementation of approved humanitarian assistance and charitable projects.

The sale of ownership rights in an entity or business, as well as transactions for the reorganisation of an entity or business, are not subject to VAT.

11.6 Taxable amount

In most cases, the amount of VAT will be determined based on the transaction price for the supply of goods or services. However, if the "usual" (market) price exceeds the transaction price, the seller must account for output VAT based on the market price. The law does not provide any guidance concerning how the usual price should be determined. In practice, the rule is often used in relation to the sale of immovable

New VAT invoice requirements

From 1 July 2010, new rules will apply for VAT payers when they issue tax invoices for sales subject to the standard 20% VAT rate.

A tax invoice will need to have a unique series and number. The invoice may be issued electronically (using procedures that are yet to be defined, but that will involve taxpayers linking their accounting system with that of the tax authorities) or using non-transferable numbered forms obtained from the tax authorities.

Invoice violations will be subject to a minimum penalty of AMD 5 million (approximately USD 12,500) for each penalty assessment.

property (as a basis for adjusting the cadastral value of the property), but it is unlikely otherwise that the issue will be raised in practice unless the sales price is clearly non-market.

When goods and services are provided free of charge, the supplier is required to account for VAT based on the market value of the goods or services, unless the supply involves warranty services provided by a seller of goods, replacement of defective goods, or the supply of goods or rendering of services when the value of those goods or services were included in the original cost of goods supplied.

The amount of VAT must be incorporated into the stated sales price (e.g., the shelf price for shop goods is inclusive of VAT).

11.7 Non-deductible input VAT

The general rules for VAT input tax credits are:

- VAT paid on goods and services that will be used to make taxable sales may be claimed as an input tax credit.
- VAT incurred to purchase or import goods and services that will be used to make sales that are VAT-exempt or not subject to VAT may not be claimed as a credit.
- When goods and services will be used to make partly taxable and partly non-taxable sales, the input tax credit is apportioned between the taxable and non-taxable sales based on the proportion of taxable sales to total sales for each reporting period.

A claim for input tax must be supported by a valid VAT invoice issued by a supplier or a duly executed import customs declaration. In addition, for the purchase of goods or services, an input tax credit will generally only arise if payment is remitted through a bank and the goods or services are obtained for commercial purposes. Input tax credits are available for cash purchases, but only up to AMD 300,000 (approximately USD 750) per transaction and up to a maximum of AMD 3 million (approximately USD 7,500) per month, and provided that all necessary VAT information is included on the sales receipt or the VAT invoice.

An input tax credit may not be claimed for VAT paid before a taxpayer is a VAT payer. An input tax credit will also not arise for the purchase or importation of cars that are not acquired for the purpose of resale, although a credit based on the residual value of the vehicle will be allowed when the vehicle is eventually sold. Finally, an input tax credit will not arise on purchases exceeding AMD 100,000 (approximately USD 250) if a taxpayer fails to correctly report those invoices in the report with information on sales and purchase invoices submitted to the tax authorities.

Generally, VAT paid that is not able to be claimed as input tax credit is treated as part of the cost of acquisition for purposes of profit tax or income tax.

11.8 VAT compliance

Registration

The following taxpayers are automatically required to account for VAT:

- Businesses with sales exceeding AMD 58.35 million (approximately USD 145,875) in the preceding calendar year will be required to account for VAT on their sales in the subsequent calendar year.
- Businesses that require a license costing more than AMD 100,000 (approximately USD 250) to operate and businesses producing excisable goods will also be required to account for VAT on their sales.

- Businesses that produce or imports products that are subject to excise tax.
- Other businesses will be required to account for VAT on any sales in a calendar year in excess of AMD 58.35 million.
- Special rules exist that may require interrelated persons (mutual ownership in statutory capital, proportion of income or expenses related to one supplier or customer) to account for VAT because of the relationship.

There is no formal VAT registration process for these businesses. However, a business not subject to mandatory VAT may register voluntarily as a VAT payer.

Accounting requirements

VAT payers are required to keep separate accounts for taxable and VAT-exempt sales and purchases. If it is not possible to keep separate accounts, the amount of VAT input tax credit for each reporting period should be calculated based on the proportion of taxable sales to total sales for that period.

Information on VAT invoice

With the exception of retail sales, A VAT-registered person is required to issue a VAT invoice for every taxable sale of goods or services. For retail sales, a VAT invoice must be issued only upon request.

The invoice must include the following information:

- Serial number and the date of issue;
- Name, address and taxpayer's identification number (TIN) of the seller.
- Name and address of the purchaser.
- Denomination and quantity of goods, or the type and volume of services.
- The price and the total value of goods or the tariff and the total amount of payments for services, excluding VAT.
- The calculated amount of VAT (as a separate line).

A VAT invoice may not be issued for transactions that are exempt or not subject to VAT. Special rules also apply concerning the preparation of invoices for zero-rated sales.

Buyers need to pay particular attention to the information contained in VAT invoices, particularly when the invoiced amount exceeds AMD 100,000 (approximately USD 250), net of VAT. The tax authorities may pay close attention to the details on invoices when they conduct audits, and in some cases will disallow input tax credits even if there are relatively minor defects in the invoice.

From 1 July 2010, new rules will apply for VAT payers when they issue tax invoices for sales subject to the standard 20% VAT rate. A tax invoice will need to have a unique series and number. The invoice may be issued electronically (using procedures that are yet to be defined, but that will involve taxpayers linking their accounting system with that of the tax authorities) or using non-transferable numbered forms obtained from the tax authorities. Invoice violations will be subject to a minimum penalty of AMD 5 million (approximately USD 12,500) for each penalty assessment.

VAT liability

The VAT liability is calculated using the input-output method. The VAT liability in any accounting period will be the total amount of output tax charged on sales, less the input VAT paid relating to taxable sales.

VAT is accounted for as follows:

- VAT on the sale of goods is accounted for when the goods are unloaded or delivered to the purchasers.
- VAT on the sale of services is accounted for when the services are rendered to the customers.
- The entitlement to an input tax credit for purchases arises on the date on which payment is made, provided the VAT invoice is obtained before the end of the reporting period. If the invoice is obtained late, the general practice would be to file an amended return for the period.
- The entitlement to an input tax credit for imported goods arises on the date of importation.

Reverse charge

Services supplied in Armenia by non-residents that are not registered in Armenia are subject to the application of a VAT reverse charge. To support a corresponding claim for an input tax credit, the recipient of the services must self-issue an invoice on behalf of the non-resident, and indicate their own identification number as the supplier of services.

One practical issue that non-resident suppliers need to be conscious of is that the law does not clearly state who should bear the cost of the VAT. To reduce the risk of dispute, the supplier of services should make it clear up front that VAT will be for the account of the local entity (in principle, the local entity will be entitled to claim an input tax credit), and ensure that this is reflected in any contractual arrangements that are concluded.

Returns and payments

Generally, VAT payers should file VAT returns on a quarterly basis. However, taxpayers with sales

Timing can be so important

Armenian VAT rules require sellers to account for VAT on the *earlier* of the invoice date or the payment date. For purchasers, however, the corresponding input tax credit arises on the *later* of the invoice date or the payment date.

This can cause practical problems for reverse charge VAT. If a foreign party issues an invoice for services on 28 June 2009, the recipient is required to account for reverse charge VAT based on a supply made in June 2009.

The entitlement to a corresponding input tax credit arises on the later of the self-invoice date (28 June 2009) or the date the foreign entity is paid. If the foreign supplier is paid in June 2009, the reverse charge VAT and input tax credit will be reported in the same period, cancelling each other out if none of the local party's sales are VAT-exempt. However, if the foreign supplier is paid after 30 June 2009, adverse cash flow consequences could result.

(excluding VAT) in the previous calendar year exceeding AMD 100 million (approximately USD 250,000) are required to file VAT returns monthly.

VAT payments must be made and VAT returns filed within 20 days following the end of the reporting period.

A separate report with information on sales and purchase invoices exceeding AMD 100,000 (approximately USD 250) must be filed within 25 days following the end of the reporting period. If the report is not filed, the authorities are likely to disallow input tax credits.

Refunds

As a general rule, when input tax for a reporting period exceeds output tax for the period, the excess input tax is carried forward and applied against VAT payable in future reporting periods. Refunds are permitted only for purchases and importations that are directly related to zero-rated transactions (other than the export of ferrous and non-ferrous scrap).

According to the law, a refund should be issued within 15 days of the refund application. There is no liability for the government if it does not issue VAT refunds on a timely basis, and obtaining a refund may be difficult in practice and require much more time. It may be easier to have the excess credit applied against other tax liabilities, although confirming the entitlement to a credit may still be a challenge. Investors need to factor these considerations into their financial projections.

12 Introduction to PricewaterhouseCoopers



12.1 PricewaterhouseCoopers worldwide organisation

PricewaterhouseCoopers (www.pwc.com) provides industry-focused assurance, tax and advisory services to build public trust and enhance value for its clients and their stakeholders. More than 163,000 people in 151 countries across our network share their thinking, experience and solutions to develop fresh perspectives and practical advice.

These services include audit, accounting and tax advice; management, information technology and human resource consulting; financial advisory services including mergers and acquisitions, business recovery, project finance, and litigation support; business process outsourcing services; and legal services provided through a global network of affiliated law firms.

“PricewaterhouseCoopers” refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and

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independent legal entity.

12.2 PricewaterhouseCoopers in Armenia

PricewaterhouseCoopers has been serving clients in Armenia since 1996 and in September 2007 opened an office in Yerevan. We now employ more than 20 local and expatriate professional staff. Their local knowledge, coupled with a strong network of global resources, allows us to deliver constructive and efficient advice to meet our clients' specific business needs.

Our team is divided into two service lines: Assurance Services, and Tax and Legal Services. Our Advisory service line is not directly represented in Armenia, but our access to the PricewaterhouseCoopers global network means that we can readily call on professionals in other territories to assist with your Transaction Services, Performance Improvement and Crisis Management service needs

Assurance Services

Assurance Services provides assurance on the financial performance and operations of our clients' business, through external and internal audits, financial and accounting reviews and investigations, regulatory consulting and training courses.

PricewaterhouseCoopers' knowledge and experience enables our specialists to advise not only on assurance matters, but also to put them in context and to advise on the likely impact that the pace and direction of economic and financial change will have on a commercial activity in Armenia.

Available Assurance services include:

Audit: Statutory and regulatory audit and treasury services. Our audit is aligned with business functions, not just financial processes. Businesses need auditors and advisors who understand their strategy and can reflect this in their audit approach. Using our approach and working alongside our clients, our lead partner provides strong control from the centre. We put great emphasis on understanding our clients' strategy and the need to address all risks. This approach represents, we believe, an important step forward in client service, audit quality and efficiency.

Accounting and regulatory advice: Corporate structures, technical accounting advice (supported

by Global Corporate Reporting (GCR)), review of treasury operations, compliance with current and new regulations.

Attest and attest-related services: Independent assessment of financial and non-financial data.

Public services audit and advisory: Audit, internal audit and associated services for government, education and other non-profit organisations.

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Tax Services

Effective tax planning is vital for the growth and development of any organisation. Very few major business decisions can be taken without considering their tax implications. In Armenia, where the tax and legal system is complex and subject to constant revision, professional advice is even more of a necessity to achieve success. Expected tax reforms over the next two years will also challenge businesses, as they seek to understand the changes and what they mean in practical terms.

Our team of local and expatriate professionals have the skills and experience in all areas of taxation – corporate and personal, direct and indirect – to help clients maximise their tax advantages and minimise their exposures. We advise international companies based upon our knowledge of Armenian tax legislation and its interrelationship with national and international laws and also treaties. This knowledge, together with our focus on specific markets and industries, helps us to add value to our clients' businesses and give them the edge they need in the marketplace.

Specific tax areas where we can assist include:

Corporate tax: We advise clients based on Armenian laws and their interpretation by tax

authorities, as well as their interrelation with international regulations and treaties. We advise on all aspects of inward investments into Armenia, and the structuring of those investments in terms of corporate income tax, withholding tax, dividend tax and local tax regulations. The team provides proactive advice on international tax planning and structuring, mergers and restructuring, and undertakes company health checks and due diligence projects, as well as assistance with tax authorities (during tax inspections and lodging of objections).

Value added tax (VAT): We help clients resolve complex issues related to indirect taxes, including VAT consultancy and tax reviews, VAT planning and efficiency schemes for domestic and cross-border operations, assistance during tax inspections, and support and advice during appeals.

Personal tax: Our services related to individuals range from assisting with obtaining residence permits to advice and assistance with all matters regarding Armenia's personal income taxation legislation and social security system.

Compliance services: With the increasing focus on governance and regulation, tax compliance has never been so important. Compliance failure represents not only a financial risk but also a serious business risk, as it can damage the reputation of a business with the authorities and the public. PricewaterhouseCoopers can help you manage your tax compliance issues, risks and opportunities, allowing you to have firm control. We can help you, both within Armenia and cross-border, with preparing and reviewing tax returns and computations, negotiating with tax authorities, corporate income tax, indirect tax, property and land tax compliance, and payroll.

For further information, please contact:

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Appendix – Withholding taxes at 1 January 2010

Country	Dividends		Interest (1)	Royalties
	Non-portfolio %	Portfolio %	%	%
Non-treaty	0 / 10 (2)	10	10	10
Austria	5 (3)	10	0 / 10 (4)	5
Belarus	10	10	10	10
Belgium	5 (3)	10	0 / 10 (4)	8
Bulgaria	5 (5)	10	10	10
Canada	5 (6)	10	10	10
China (People's Rep.)	5 (7)	10	10	10
Czech Republic	10	10	5 / 10 (8)	5 / 10 (9)
Estonia	5 (7)	10	10	10
Finland	5 (7)	10	5	5 / 10 (10)
France	5 (3)	10	0 / 10 (4)	5 / 10 (11)
Georgia	5 (7)	10	10	5
Greece	10	10	10	5
India	10	10	10	10
Iran	10	10	10	5
Italy	5 (12)	10	0 / 10 (13)	7
Latvia	5 (7)	10	10	10
Lebanon	5 (7)	10	8	5
Lithuania	5 (7)	10	10	10
Moldova	5 (7)	10	10	10
Netherlands	0 / 5 (14)	10	0 / 5 (4)	5
Poland	10	10	5	10
Qatar	5 (15)	10	5	5
Romania	5 (7)	10	10	10
Russia	5 (5)	10	0	0
Switzerland	5 (16)	10	0 / 10 (4)	5
Syria	10	10	10	10
Thailand	10	10	10	10
Turkmenistan	5 (7)	10	10	10
Ukraine	5 (7)	10	10	0
United Arab Emirates	3	3	0	5

- Several treaties contain a 0% rate on interest paid to or guaranteed by a government or one of its agencies. The table does not analyse such provisions.
- The 0% rate applies if the dividends are paid to a foreign company that has owned more than 25% of the Armenian company for at least two calendar years preceding the distribution, and the dividends are not subject to tax in the foreign company's country of residence. The Government has published a long list of exceptions to this rule.
- The ownership threshold for the non-portfolio rate is 10%.
- The 0% rate applies to interest in connection with the sale on credit of any industrial, commercial or scientific equipment or capital goods, and to interest on a loan granted by a banking enterprise.
- The ownership threshold for the non-portfolio rate is direct investment of USD 40,000.
- The ownership threshold for the non-portfolio rate is 25% and the direct investment must exceed USD 100,000.
- The ownership threshold for the non-portfolio rate is 25%.
- The 5% rate applies to interest on loans or credit granted by banks.
- The lower rate applies to payments for the use of, or the right to use, any copyright, cinematograph films, or films or tapes for television or radio broadcasting.
- The lower rate applies to consideration for the use of, or the right to use, any computer software, patent, trade mark, design or model or plan, secret formula or process, or information concerning industrial, commercial or scientific experience (know-how).
- The lower rate applies to royalties paid for the use of, or the right to use, any copyright.
- The ownership threshold for the non-portfolio rate is 10% and the direct investment must exceed USD 100,000.
- The 0% rate applies to interest on a loan granted by a banking enterprise.
- The ownership threshold for the 5% non-portfolio rate is 10%. The 0% rate applies if the dividends out of which the profits are paid have been effectively taxed at the normal rate for profits tax and the dividends are exempt income to the Dutch recipient.
- The ownership threshold for the non-portfolio rate is direct investment of USD 100,000.
- The ownership threshold for the non-portfolio rate is 25% and the direct investment must exceed CHF 200,000.

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