

Tax reforms in Armenia are aimed at developing SME

By Samvel Sargsian

The Armenian government has launched tax reforms "on a wide front", while their assessments are contradictory. Gagik Poghosian, the Deputy Chairman of the Board of the Association for Foreign Investment and Cooperation (AFIC) NGO, expressed his opinion about these reforms in an interview with NT correspondent. The NGO has participated in the preparatory work and discussions of the tax reforms.

NT: Mr. Poghosian, what was the participation of your association in the reforms being implemented in Armenia's tax sector now?

G.P.: We published our recommendations on tax reforms last year when in 2006-2007 we implemented a project on these problems with the assistance of the Center for International Private Enterprise (CIPE), affiliate of the US Chamber of Commerce. I should note with satisfaction that several of our recommendations were reflected in the RA government's program approved in July 2007 (NT: the current president Serzh Sargsyan

was the prime minister at that time), as well as were included in the package of tax legislation reforms which was adopted recently.

After the formation of the present government, special importance was attached to the implementation of second-generation economic reforms, during the preparation for which a number of meetings and discussions with representatives of the structures representing the business community were held. AFIC also took an active part in these discussions. In May, a timetable of actions for tax sector reforms was approved by Prime Minister Tigran Sargsyan. In particular, great attention was paid to the problems whose solution would create favorable conditions for operation of small and medium enterprises. As a result, a package of legislative amendments (18 bills) developed by the government was submitted to the National Assembly. The package was passed at an extraordinary session of the National Assembly in August. The majority of the amendments will take effect on January 1, 2009.

The most important amendment is that instead of the previ-

ously used simplified tax, and improved form of taxation will be introduced for small business entities which will ensure favorable conditions for them. Hereby, the minimum level of annual turnover for being considered as a small entity has been changed: from January 1, 2009, it will make 58 million drams or over 190 thousand dollars. Enterprises with lower turnover will not pay value added tax which will considerably simplify the red tape and tax statements of SMEs.

NT: When can the results of the new changes be expected?

G.P.: I think that some progress has been made in tax reforms. Of course, their result and impact on small entrepreneurship can be assessed only at the end of the coming year of the new legislation's application, but the general picture will be clear within the first few months. AFIC plans a monitoring activity with the aim of assessing the indicated impact.

In any case, I hope that this impact will be a positive one as in fact, the Law on Simplified Tax often provided big businesses with an opportunity to abuse: an opportunity to pay simplified tax by splitting up their businesses. Whereas these tax reforms aim to promote the growth and development of small enterprises - such enterprises that have no opportunity to have an accounting unit and deal with the red tape related to complicated tax statements. The abuses of the Law on Simplified Tax were the reason that the number of those liable to this tax was strictly limited last year which, naturally, caused discontent of small and medium entrepreneurs.

Foundation for Small and Medium Businesses, "Armenian Entrepreneurship" SME Union, the Small and Medium Entrepreneurship Development National Center (SME DNC) of Armenia and other structures.

NT: Are there any by-laws necessary for the use of the new tax legislation?

G.P.: It happened that in late August, on the day when the National Assembly passed the above mentioned legislative pack-



Gagik Poghosian

age, Armenian President signed a decree on uniting the RA government-adjunct State Tax Service and State Customs Committee into a State Revenue Committee. Personnel and structural changes are currently underway at this structure. I think that after these changes are over and everything settles down, the mechanisms for using the new legislative package will be worked out.

NT: The correct application of the Law on Simplified Tax was impeded by the fact that it was impossible to use records of com-

have to evade taxes.

We want to do so that entrepreneur - tax body relations will not be tax evader - punishing body relations but so that when providing a service, the tax body will control and help an entrepreneur pay his/her taxes in time and properly.

During one of our latest discussions, it was confirmed once again that both phenomena are realities which is the consequence of entrepreneurs' fear to fix their activities in some way. Perhaps it bears evidence of the low level of their business education.

We will continue explaining to such entrepreneurs that the more transparent their work, the fewer reasons to fear tax bodies they will have. I assure you that now the state does everything so that tax payers will not make mistakes. In particular, the ministry of economy jointly with the Association of Accountants and Auditors is implementing a program, under which accounting courses are organized free or at low prices for SMEs.

NT: How do you assess the Armenian government's step aimed at connecting the cash registers of all sales subjects to a united system, as well as the opinions of those who oppose this step?

G.P.: As regards cash registers, an idea has been adopted, that is, the business conditions should be equal and fair for everybody, irrespective of their workplace, and if a cash register is used in a small shop, it must be used at a fair. The answer to the question about why many entities operating at fairs are reluctant to introduce cash registers is simple: because they operate in the shadow sector.

KPMG is a global network of professional firms providing Audit, Tax and Advisory services. We operate in 145 countries and have more than 123,000 professionals working in member firms around the world.

KPMG has operated a full service office in Armenia, Yerevan since 1997 and is licensed by the Government to service clients in the enterprise and banking sectors of the Armenian economy.

Our staff in Armenia is now in excess of 80 and we have the necessary combination of in-depth knowledge of local business and international practical experience.

Our services include:

AUDIT

- Financial statements audit (IFRS, US GAAP, ASRA)
- Compilation of Financial Information
- Agreed Upon Procedures
- Audit related services

TAX

- General tax advisory services
- Tax and accounting outsourcing
- Operational reviews
- Expatriate tax returns
- Mergers and acquisitions
- Tax due diligence
- Company formation and registration

ADVISORY

Risk Advisory Services

- Business performance improvement and management
- Accounting advisory services
- Financial planning and budgeting
- Corporate governance
- Internal audit and risk management
- Information risk management
- Building management information systems
- Strategy review and improvement

Financial Advisory Services

- Pre-investment analysis and transaction evaluation (due diligence assistance)
- Business valuation
- Preparation of business plans
- Contract assistance
- Corporate recovery services
- Anti-money laundering review

Tel/fax: 374 (10) 566 762
E-mail: general@kpmg.co.am
www.kpmg.am

KPMG Armenia cjsc
8th floor, Erebuni Plaza Business Center,
26/1 Vazgen Sargsyan Street
Yerevan 0010, Armenia

AUDIT • TAX • ADVISORY



© 2008 KPMG Armenia cjsc, a company incorporated under the Laws of the Republic of Armenia and a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative. All rights reserved. Printed in Armenia

Naturally, the tax legislation package contains some provisions which aim to restrict the entry of big enterprises into the field of SME taxation. It is also natural that there are problems with ensuring budgetary revenues that should be taken into account as well.

In any case, quite an interesting atmosphere of cooperation of business associations and business support organizations with state government bodies has already formed, and I hope that this cooperation will be lasting. The information gained by the business NGOs and their ability to conduct monitoring represent quite a serious resource of efficient work of state bodies. For example, we actively work with the RA Ministry of Economy and the government-adjunct State Revenue Committee and participate in all discussions organized by these departments. We envisage joining our efforts with several other NGOs to create a Business Advocacy Network for economic reforms.

By the way, our association together with several partner structures took quite an active part in the discussion of the draft concept and action plan "Armenia as a Center of Excellence" in accordance with "Doing Business" indicators initiated by the Ministry of Economy. The approval and implementation of the concept will be a step forward in the development of entrepreneurship, particularly SME sector, in our country. After publication of the final version of the draft concept, we envisage organizing work on the draft amendment within the framework of the Business Advocacy Network. In this respect AFIC closely cooperates with the Chamber of Commerce and Industry of Yerevan, the

modity purchases and sales for the calculation of real turnover of an enterprise because considerable part of its turnover was done at fairs, without cash registers. By the new amendments, the use of cash registers at fairs is mandatory. What impact will it have on regulating the documentation in the chain "import - production - sale - export"?

GP: The solution to this problem is given in the tax legislative package passed by the National Assembly in August.

The inhibition of undocumented turnover is a serious problem. For example, we explained during our meetings with SME representatives that to keep documents while operating is to their advantage. Under the new law, SMEs are already profit tax payers. I would like to remind you that simplified tax substituted for VAT and profit tax. Starting from January 1, 2009, all enterprises are liable to profit tax: each month they shall make a prepayment in the amount of 1% of turnover of the previous month, and a final calculation shall be made by the results at the end of the given year. This will put an end to the arbitrary practice of tax prepayment collection. The availability of documents confirming the amounts of sold and purchased values is very important from the viewpoint of reducing the profit tax to be paid.

However, many are used to working in the "shadow" sector, although they can reduce the profit tax to be paid by substantiating their expenses based on documents. Many of the small and medium entrepreneurs say that they are ready to pay taxes if the tax rates are affordable, and the order and mechanisms of tax payment are simple. That is, because of the current conditions, they

use of cash registers at trade facilities pursued the goal of rectifying this situation. Indeed, no developed state would allow its economic entities to work in the shadow economy. The issue of tax rates' being high or low is another matter. The program of tax sector reforms already envisages their reduction. Why not, if the number of tax payers increases?

I should mention that the legislative package adopted in August also aims to reduce corruption risks. For instance, an entrepreneur working in the shadow sector is a corruption risk by himself as the tax inspector knows very well that he operates in the shadow sector. But if an entrepreneur works transparently, what danger may the tax inspector pose to him?

The creation of the opportunity to submit electronic tax statements in Armenia (this method was introduced in the civilized world long ago) was great progress in terms of reducing corruption risks in our country.

As for the introduction of a united network of cash registers, the problem here lies in finding technical solutions. It is early to speak about how much time it will take to form such a network. The major goal here is to reduce the shadow turnover to a minimum. If the cash register of an economic entity is connected to the network, its turnover will be recorded every day, and it will become impossible to submit a tax statement with data not corresponding to the reality.

To sum up what was said above, I note once again that purpose of the tax reforms being implemented in Armenia now is to improve and simplify the mechanisms of taxation, document circulation and statement presentation of SMEs.