

## LEGISLATIVE AND LEGAL SUPPORT OF THE TAX SYSTEM OF THE REPUBLIC OF ARMENIA

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**Introduction.** Clarity of tax legislation, simplification and improvement of tax administration are closely interrelated. There are still approaches in the tax legislation that significantly hinder the development and stability of the economy. The tax system will be more effective if the emerging issues are simple, stable and predictable. There is a unified tax system in The Republic of Armenia (RA), which is based on the principles of simplicity and clarity, cohesion, equality, non-discrimination, joint obligation, transparency and accountability, self-declaration and tax discipline, balanced tax administration, inevitability of responsibility, proportionality of responsibility, pluralism and publicity, modernity, competitiveness, efficiency [The Tax Code of RA, Articles 3].

**Methodology.** The theoretical, informative and methodological basis for the scientific article was the legal acts regulating tax relations: The Tax Code of RA (Code), The Law of the RA “On Non-cash transactions” as well as research conducted based on international experience. The latter made it possible to highlight a number of problems of violation of tax principles during the implementation of legal acts regulating tax relations, as well as non-observance of the requirements of the legislation, which undermined the transparency of taxpayers' activities and the opportunities to avoid taxation, as well as the development and stability of the economy.

**Literature review.** It is noteworthy to present the mechanisms operating in a number of countries that aim to solve the problems of violation of tax principles which arise during the implementation of legal acts regulating tax relations of RA.

In the case of renting out an apartment in the Russian Federation, there are 3 tax payment options: personal income tax, residential rental license system, self-employment tax [Federal Agency, 2021]. The declaration can be filled out manually when appearing at the tax office in person or electronically. Based on the submitted declaration and the attached documents, the tax authority will collect the amount of personal income tax payable - 13% of the income received from renting the apartment. If a person rents an apartment and lives in Russia for more than 183 days per year, he must pay personal income tax at the rate of 13%. If the person is in Russia for less than 183 days per year, the tax rate will be 30%. Another way to declare leasing of apartments is to use the franchise tax system. This option is available only to individual entrepreneurs. The cost of the

license is set by the state and is 6% of the approximate annual income that the entrepreneur can get from renting out the real estate. There is no need to pay personal income tax, income tax from the use of property and property tax when obtaining a license. The cost of a rental license is calculated based on its area and location. According to the clarifications of the Ministry of Finance of the Russian Federation, a non-resident taxpayer of the Russian Federation living abroad can continue business activities in the Russian Federation as a self-employed person. In this case, the income received from renting apartments in the Russian Federation will be taxed at the rate of 4%. In Russia, there is a fine for apartment owners for not paying tax on income from renting an apartment, as well as for late payment of tax and failure to submit a declaration.

Malta is subject to a 15% tax on rental income, which applies to both residential (from 1 January 2014) and commercial property (from 1 January 2016). 15% must be paid from the gross rental income. This rate applies to both resident and non-resident individuals. Any undeclared rental income is subject to tax at 35% of the gross rental income [Income Tax Law in Malta, Article 31, Government of Malta, 2023].

India has a “Fair Rent” rule, according to which the rent charged by the landlord should be 8% to 10% of the property value. If the landlord demands more rent, the tenant can appeal the claim in court for compensation. The owner has the right to raise the rent annually, can do so by about 5% each year. The tax exemption is allowed to be applied to the interest of acquired, repaired, constructed, reconstructed property [Pawani, M. 2023].

In Cyprus, rental income is consolidated with other taxable income streams and is taxed at rates on a progressive scale of income tax ranging from 0-35% after allowing for appropriate tax deductions [Delloite, 2022].

**Scientific novelty.** The main scientific novelty of the article refer to the presentation of new and applicable ways to increase the effectiveness of the RA tax system. In particular, in order to maintain the principles of taxation in the RA tax system, to ensure legislative and legal security, we have proposed to promote the implementation of transactions in a cashless way and reduce the volume of cash circulation, to simplify the system of declaring the remuneration contract, to establish certain privileges for those who lease the property, lessors, and tenants, as well as to apply responsibility strict measures for non-declaration of real estate rental income.

**Analysis.** When implementing the legal acts regulating tax relations of RA, sometimes the principles of the tax system are not observed. Most of the problems of the tax system, as a rule, are the result of inconsistency, ambiguity of the regulatory framework and ineffective interaction of executive and legislative bodies. In particular, under the Law on Cashless Transactions, a cashless quote or price offer cannot imply a higher price than a cash quote. However, a number of traders make a lower quote or offer when paying in

cash and this is often done publicly. The State Revenue Committee supervises and applies measures of responsibility over compliance with the requirements of this law or normative legal acts adopted on its basis. However, as a result of improper control, the principle of equality of taxation is violated, and unequal competition arises in the business field, which can lead a businessman to violate the requirements of the law, restoring the principle of equality of competition.

1. In order to solve the above problem, we propose to promote the implementation of transactions in a cashless way and to reduce the volume of cash circulation. The use of cash in Armenia is still a hot topic of debate and it is fertile ground for tax evasion. In order to solve this problem, it is necessary to undertake a comprehensive package of measures aimed at reducing cash. In particular:

❖ We suggest introducing the “Cashback” system as a compensation system. In case of non-cash transactions, provide cashback to the buyers, as a result of which they will force the sellers to make the transaction cashless through POS-terminals, and in the absence of the latter, the buyers will submit a corresponding claim.

❖ In order to avoid double “Cashback” in the case of cashless purchases by the same person with several cards we propose to create a unified electronic platform, where any person who wants to use the “Cashback” program can enter his personal data, including the card account number, which later can be considered as a “cashback” refund account.

2. According to Article 156 of the Code, natural persons should submit annual income tax calculations (declarations) to the tax authority with respect to the income specified in Article 151 the Code in accordance with the established procedure up to and including May 1 of the tax year following each reporting period in accordance with Article 53 of the Code. Citizens of RA who are considered residents of RA and who do not submit annual income tax calculations (declarations) in accordance with the above-mentioned clause of Part 4.1 submit annual income tax calculations (statements) to the tax authority in accordance with the procedure established by Article 53 of the Code, up to and including May 1 of the tax year following each accounting period. In other words, it turns out that in the case of the above two regulations, both natural persons and citizens of RA who are residents of RA must submit annual income tax calculations (declarations) to the tax authority.

The Code stipulates that the tax calculation written information about any transaction or operation during the reporting period considered to being the object of taxation defined by the Code, submitted by a taxpayer to the tax authority, while the declaration only contains information about income. Thus, we can state that in the case of such regulations, the principle of simplicity and clarity of the tax system is violated, because the legal acts regulating tax relations should be clearly defined for taxpayers and the tax authority, and should not contain contradictions and ambiguities. In order to solve the problem, as well as to avoid discrepancies, we propose in paragraph 2 of Part 4 of Article

156 of the Code to replace the words “annual income tax calculations (declarations)” with the words “annual income tax calculations and social payments”, and in Part 4.1, replace the words “calculations (declarations)” with the words “declarations” so that the calculations (declarations) established in paragraph 2 of Part 4 and Part 4.1 differ. In other words, it turns out that natural persons must submit annual income tax and social contribution calculations to the tax authority up to and including May 1 of the tax year following each accounting period, and citizens of RA who are residents of RA who do not submit the above calculations, annual income tax declarations.

3. From the legal point of view, there are also a number of problems, the solution of which will preserve the tax principles regulating tax relations, as well as increase tax revenues. In particular, the legal relations related to the lease of real estate in RA are regulated by the Code. According to Article 150, Part 7 of the Code, the rate of income tax calculated by an individual for rental payments is set at 10%, and in case the sum of rental payments received during the tax year exceeds AMD 60 million, the individual calculates additional income tax for the excess part: at a rate of 10%. According to part 1 of Article 258, the turnover tax is calculated at the rate of 10% in relation to the taxation base of the transactions considered as the object of taxation with the turnover tax in terms of rental payments. Despite the existing regulations, there are quite a lot of cases of non-declaration of the income received from the rental of real estate, the implementation of mechanisms to identify all cases requires large resources and costs. In other words, it turns out that not all taxpayers calculate and pay taxes in the cases, order and amount defined by the legislation, violating the principle of joint obligation of the tax system.

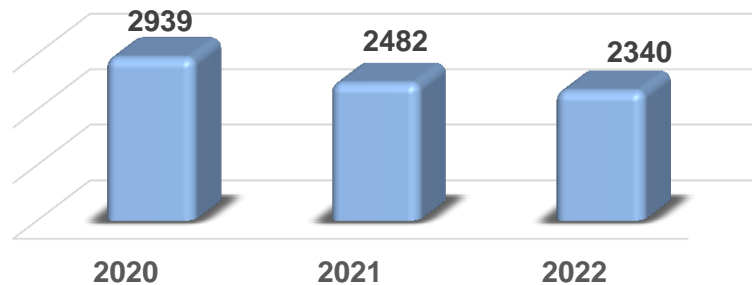
**Table 1.** The number of transactions for renting apartments and individual residential buildings in the real estate market of the Republic of Armenia by year<sup>1</sup>

| Property type                   | 2020 year   | 2021 year   | 2022 year   |
|---------------------------------|-------------|-------------|-------------|
| Apartment                       | 2119        | 1695        | 1761        |
| Individual residential building | 820         | 787         | 579         |
| <b>Total</b>                    | <b>2939</b> | <b>2482</b> | <b>2340</b> |

A study of the residential rental market shows that in 2020-2022 there is a decrease in the number of registered lease agreements.

Meanwhile, the growth in demand for apartment rentals during the study period (due to the influx of foreigners in 2022, in particular citizens of the Russian Federation, Ukraine and Belarus to Armenia) and supply (including due to newly commissioned residential buildings) also implies an increase in actually concluded lease agreements. Therefore, it can be assumed that market participants avoid entering into a lease agreement in accordance with the current legislation.

<sup>1</sup> Analysis of the real estate market of the Republic of Armenia, 2020-2022



**Graph 1.** Data on rental transactions in the real estate market of the Republic of Armenia by years

In order to solve the problematic issues, to introduce more effective mechanisms in the tax system, we propose to implement changes in the following 3 directions:

1) Simplify the system of declaring the remuneration contract.

❖ Create a new application, including a mobile one, to facilitate registration for the lessor. The contract concluded with the appendix will have legal force and will be available for the interested state bodies, as a result of which there will be no need to visit the Cadastre Committee. Based on the available information, the tax authority will be able to automatically complete the tax calculation.

❖ As an alternative option, apply the tax collection mechanism based on the patent (certificate) (example of the Russian Federation). In particular, the persons renting the apartment acquire a license in advance, depending on the rental period, for a certain constant, fixed amount. In case of implementation of this system, there will be no need to submit additional calculations. Another alternative option could be to determine the amount of tax based on the value of the real estate (example of India). In other words, we have the exact amount of tax estimated based on the value of the apartment.

2) Establish certain privileges for the lessors and tenants of the property.

❖ Provide a real estate tax abatement or refund to the lessor for income tax paid.

❖ The state reimburses the tenant a certain part of the utility payments for the first 2 months or transfers a lump sum as an advance payment.

❖ Adopt the principle of zoning, if the property is located in provinces, reduce the monthly 10% to 5% tax rate, and exempt property owners from taxes in border areas.

3) Apply strict liability measures.

❖ Equate non-declaration of income from real estate rental to illegal business activity or undocumented supply of goods, applying the measures of responsibility established for these violations.

❖ Establish special controls for non-resident citizens, for example, when entering RA and leaving the territory of RA, if a non-resident citizen has lived in RA for more than a certain period of time, he must show his rental agreement and how much rent he paid.

**Conclusion.** Thus, we can state that tax reforms should imply, on the one hand, easing of tax pressure and solving fundamental problems for business, and on the other hand, transparency of taxpayers' activities for the state and exclusion of opportunities for tax evasion. The implementation of reforms in the tax system should not be limited only to the improvement of tax legislation. Those reforms should also include the implementation of operational control over compliance with the requirements of existing laws and the implementation of steps aimed at the prevention of shadow economic transactions that are not taxed and illegal, informing the general public about the dangerous consequences of tax offenses for the economy, and raising the level of their legal awareness.

Thus, we believe that the procedures developed on the basis of the recommendations in the article will make it possible to achieve the clarity and simplification of the tax legislation, as well as the improvement and efficiency of the tax administration, creating the necessary economic conditions for the development of investment and innovative activities in individual sectors of the economy, as well as promoting provision of services, production of goods, use of financial resources in the direction of expansion and renewal of socio-economic development programs.

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The article is dedicated to the study of legal acts regulating tax relations and principles of taxation. The latter has shown that the principles of the tax system are sometimes not observed or not fully observed when implementing legal acts regulating tax relations. Most of the problems of the tax system are, as a rule, the result of the ambiguity and inconsistency of the regulatory framework. For this purpose, the article also carried out a study of the mechanisms for solving similar problems applied in different countries and presented recommendations for solving a number of legislative problems based on international best practices. As a result, the tax principles regulating tax relations will be preserved, the shadow economy will decrease, tax revenues will increase, making it possible to achieve the clarity and simplification of tax legislation, as well as the improvement and efficiency of tax administration.