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EU4Youth

EU4Youth SEAG project

Social Entrepreneurship in Armenia and Georgia

RESEARCH PAPER

Opportunities to build a legal framework for the development of the Social Entrepreneurship model

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EU4Youth

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Abbreviations

CC	Civil Code
DP	Development Principles
LC	Labor Code
MC	Mercy Corps
NGO	Non-Governmental organization
RA	Republic of Armenia
SE	Social entrepreneurship
SEAG	Social Entrepreneurship in Armenia and Georgia
TC	Tax Code
VAT	Value-added tax

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1. BRIEF SUMMARY

Within the framework of the EU-supported EU4Youth Initiative, the Armenian Development Principles NGO, in partnership with Mercy Corps International and the Georgian Association of Business Consulting Organizations (ABCO), has implemented Social Entrepreneurship in Armenia and Georgia (SEAG) project to involve young people in initiating social change through social entrepreneurship.

The methodology of this paper included the analysis of the experience of international SEs, the current RA legal framework, the study of the "SOCIAL ENTREPRENEURSHIP DEVELOPMENT CONCEPT" draft decision of the RA Government, the holding of some focus group and consultative meetings.

Main provisions

Despite the increase in the number of SEs in recent years, there is still no unified and comprehensive definition of SE, reflecting the current SE status in Armenia. To this day, SE is confused with charity, sometimes with corporate social responsibility. Although most experts are convinced that there is no need to develop specific legislation for SEs today, however, according to the same experts, it is necessary to develop a working regulation of the SE concept with key criteria & features that will allow the state and key stakeholders to differentiate and approach similar organizations.

For that purpose, the "SOCIAL ENTREPRENEURSHIP DEVELOPMENT CONCEPT" draft decision of the RA Government has been developed and put into circulation by specialists, which aims to define SE organizations, the criteria by which it will be possible to differentiate them and accordingly, give a working regulation, which has been studied by specialists within the framework of this document, giving respective proposals and remarks. To ensure the completeness of the study, a separate overview was made of the peculiarities of the tax sphere, with respective proposals.

According to experts, there are about 100 SMEs in Armenia today. None of their organizational legal form accurately reflects the nature thereof, which further proves the need for regulation and development of the SE sector. Most of these organizations operate for 3-5 years on average and survive mainly on the support of donor organizations, as they do not have the financial product or service specifically designed for social entrepreneurship organizations to be able to generate financial income by their own activities.

As for the education system, the involvement of women and youth therein, there is a lot to do here, from promoting entrepreneurship education, developing the SE ecosystem, to conducting courses, master classes, and other similar events to enhance legal education.

2. Part I. INTRODUCTION

This study was conducted within the Development Principles NGO's "Social Entrepreneurship in Armenia and Georgia" program (hereinafter referred to as the Project), funded by the European Union.

Within the framework of the EU-supported EU4Youth initiative, the Armenian Development Principles NGO, in cooperation with Mercy Corps International and Georgian Association of Business Consulting Organizations (ABCO) aims through the program of Social Entrepreneurship in Armenia and Georgia (SEAG) to involve the youth in initiating social change through social entrepreneurship.

The duration of the program in Armenia is 28 months, from February 6, 2020 to June 6, 2022. The goal of the project is to strengthen the entrepreneurial youth (18-35 years old) potential in the field of social entrepreneurship in Armenia and Georgia, reducing inequality, and promote youth unification and involvement.

The main goal of the program is to involve the most vulnerable groups of young people in Armenia and Georgia, in particular, the enterprises that work to solve the most crucial social and environmental problems, to achieve 3 main results:

- Improve the skills of young social entrepreneurs, gaining fresh knowledge and opportunities in the field of social entrepreneurship.
- Record youth social entrepreneurship success, including financial management, strengthening of business systems, networking, and core market areas.
- Enhance the social entrepreneurship ecosystem among young people in Armenia and Georgia.

The Project will monitor and assess the impact of the increase in the economic performance of young social entrepreneurs to ensure the continued nature of these social activities after project completion.

The purpose of this study is to analyze, evaluate and propose legal status options for the establishment of SEs which will be created within the framework of the project in all RA regions of and in Yerevan.

Based on the objectives of the project, the following activities were performed within the framework of this study:

- international SEs experiences were studied, based on EU regulations and the experience of EU member & non-member countries;
- the status, scope of activities, strengths, and weaknesses, key differences were studied of commercial and non-commercial organizations acting under RA Civil Code and other RA legal acts, as well as the possibility of creating or reorganizing SEs through a simple procedure;
- current RA tax legislation and other related acts, which regulate the activities of both commercial and non-commercial organizations, were studied, a separate overview of the specifics of the tax sector, with respective proposals, was made.
- organizations operating in RA were studied whose activities are the same or similar to studied SEs.

- proposals were developed concerning legal model of establishment/activity of organization engaged in SE (acceptable version).
- “SOCIAL ENTREPRENEURSHIP DEVELOPMENT CONCEPT” draft decision of the RA Government was studied, suggestions, remarks, main concerns were presented.
- groups and consulting meetings were organized on the process of creating SEs with the target stakeholders, which are SEs from Shirak, Tavush, and Lori marzes, representatives of the business sector and community, as well as representatives of the DP project team, whose positions and opinions were summarized and presented in the framework of this study.

2.1 SE concept, general description, the current situation in RA

The concept of SE became popular in the mid-20th century as a new trend to combine business with a social mission. With its development, it became necessary to have a general idea of the SE concept, which can reflect its goals and main criteria to distinguish them as SE.

That is why different approaches to the concept of SE and its definition have been put forward by scientists and state institutes, which, however, pursue the same goal - to give the most comprehensive and accurate definition of SE.

Thus, the European Commission’s Social Entrepreneurship Initiative Communication proposed the concept of social business / social entrepreneurship, according to which social entrepreneurship is the types of entrepreneurial activity:

- For whom the general well-being of society is considered a sufficient reason to operate for profit, often through social innovation;
- Who use the surplus of money mainly to achieve these social goals;
- Which are governed by social entrepreneurs in an accountable, transparent, and innovative way, in particular by involving employees, customers, and beneficiaries who have been affected by the business.¹

Despite the different definitions proposed by scientists and experts, there is still a gap of having a common approach, i.e., there is no single and comprehensive definition that can be applied in every country, taking into account different national regulations, characteristics, needs, and concerns.

Given that the SE concept has just been developed in RA, it still needs to be developed and regulated to avoid confusion with charity, and sometimes corporate social responsibility.

¹ https://ec.europa.eu/growth/sectors/social-economy/enterprises_en

Government agencies such as the Ministry of Labor and Social Affairs, the Tax Service, the Ministry of Justice, the Ministry of Education, Science, Culture and Sport, and the Ministry of Economy today, unfortunately play no actual, role in guiding, consulting, or advising social entrepreneurs in the early stages of SE to provide some useful information, which is a consequence of the lack of understanding of the SE concept and some regulation (whether it is a labor or legal definition). As a result, organizations registered in the RA that are more or less engaged in social entrepreneurship choose their organizational legal form guided by the principle of minimum risks, taking into account the legislation in the RA on tax, accounting, state registration, audit requirements, etc.

According to the report “The Overview of the Social Economy of Armenia”, SEs in RA are de facto “hidden” under various types of organizational and legal forms, mainly private companies, limited liability companies, non-profit organizations, foundations, and cooperatives.²

However, none of the forms listed above accurately reflects the essence of SE: to make a profit to achieve social goals or to fulfill a social mission.

According to most experts, currently, there is no need for a specific regulatory framework for SEs in the RA (considering the potential risks of ethical violations and corrupt practices by commercial organizations, most of which is likely to register as “social” to obtain all defined and possible tax benefits provided by law without the intention to have any social impact).

Nevertheless, the experts unanimously agree that it is necessary to develop a working concept of the SE with the main criteria and possible features. The state and the main beneficiaries will be able to distinguish and approach such organizations correctly.

2.2 Legislative study

Within the framework of this document, several legal acts have been studied, the provisions of which in one way or another apply to the activities of SEs and are one of the organizational and legal types of SE registration and which, with appropriate quotations and summaries, are listed below.

2.2.1 RA Civil Code

RA CC defines the following types of legal entities:

- Legal entities whose founders (participants) must participate in the formation of their property and
- Legal entities whose founders (participants) do not have such rights in connection with their property formation.

The first includes economic associations and companies, and the latter includes public associations and foundations.

² The Overview of the Social Economy of Armenia: Social Enterprises of Shirak, Tavush and Lori marzes, May 2020, p.4

At the same time, CC legal entities are differentiated based on the criterion of pursuing a profit (commercial) or non-profit and not distributing the (non-commercial) profit among the participants. The main “entrepreneurial” difference between these two types is the possibility of profit distribution / non-distribution (in the form of dividends).

Below are the studies conducted on each of the listed organizational forms with appropriate comments.

2.2.2 Non-profit organizations

2.2.2.1 Public association

According to Article 50 of RA CC, public associations belong to the number of legal entities to which their founders have no obligations. In this way, mainly non-commercial organizations are created.

2.2.2.2 Foundation

According to Article 152 of the RA CC and Article 3 of the RA Law on Foundations, “a foundation is a non-member organization created based on voluntary property payments of citizens and (or) legal entities and which pursues social, charitable, cultural, educational or other socially useful purposes”.

The Foundation's the highest governing and supervisory body is the Board of trustees of the foundation, which is formed under the procedure established by the charter of the foundation, in case such procedure is not established, on the principle of one member of each founding Board of trustees. The quantitative composition of the Board may not be less than 3 members. Among the competencies of the Board of Trustees is the approval of the strategic plan(s) of the foundation, the definition of the types of business activities (including personal) carried out by the foundation, the approval of the fund budget and its changes, annual financial reports and annual reports of the foundation; making decisions on reorganization, making decisions on the establishment or participation of economic companies, as well as the establishment of separate subdivisions and institutions and the approval of their charters, etc.

The regulations on the fund’s business activities are relatively stricter, for example, the type of business activity should be provided by the fund’s charter, in terms of state control, they are classified as a group of organizations with the highest risk criteria, etc.

2.2.2.3 Cooperative (agricultural, consumer, etc.)

According to Article 117 of RA CC, “A cooperative is a voluntary association created to meet the material and other needs of the participants, based on the membership of citizens and legal entities by the joint contribution of their property or other assets of its members.”

Cooperatives can be for-profit (commercial) or non-commercial (non-commercial) organizations, depending on the nature of their activities. Except for certain types of cooperatives (consumer cooperatives, agricultural cooperatives), the features and legal status of which are defined by RA CC and other laws, no other types of cooperatives are defined.

For the purposes of this paper, we have examined non-commercial cooperatives, considering the fact that consumer cooperatives differ in their subject matter from non-commercial cooperatives. For example, in a consumer cooperative, the participants (members) may be citizens and (or) sole proprietors and citizens engaged in agricultural production who have signed a joint venture agreement. It should be noted that RA Supreme Council adopted the law regulating consumer cooperation on December 13, 1993. Յ.Ն-0966-Լ.

As for agricultural cooperatives, according to article 3, paragraph 1, sub-paragraph 2 of RA Law on Agricultural Cooperatives, Agricultural Cooperative is based on the membership of citizens and legal entities operating in the agri-food system and is aimed at meeting the material, social and other needs of businesses more effectively.

Agricultural cooperatives have a special status in terms of tax legislation: regulations relating to non-commercial organizations apply to agricultural organizations in the general taxation system. However, such organizations may operate in special taxation systems, which are intended as preferential systems for the activities of commercial organizations. It turns out that the peculiarities of both non-commercial and commercial organizations apply to agricultural organizations (including cooperatives), by RA Law on Agricultural Cooperatives only a cooperative union is considered a non-commercial organization. However, if we take into account the fact that the cooperative provides for the distribution of property among its members, the surplus of the cooperative can be distributed as compensation, the cooperative is established only to meet the material and other needs of its members, as well as the fact that the institution of an investing member is envisaged here, etc., it should be noted that in terms of content, the cooperative is characterized by the attributes of both commercial and non-commercial organizations.

2.2.2.4 Non-governmental organizations

The RA Law on Non-Governmental Organizations defines a non-governmental organization (hereinafter referred to as an NGO) as a public association of RA citizens, foreign nationals, persons without citizenship (hereinafter referred to as individuals), and (or) legal entities having the status of a non-commercial organization.

The ability of NGOs to engage in entrepreneurial activities is in line with international standards, according to which NGOs should be able to engage in any legal activity. It should be noted here that until 2017 Only foundations were allowed to do business directly under their legislation. However, Article 8 RA 1 of the RA Law on Non-Governmental Organizations was finally amended after a long period of effort and extensive effort, stating that: "The organization has the right to carry out business activities by the goals defined by its charter, to manage its property and results of activities for that purpose, as well as to establish a commercial organization or become a member," thus, in fact, for the first time in the history of Armenian legislation allowing them to engage in direct business activities and eliminating discrimination against them.

NGOs: the opportunity to do business is in line with international standards, according to which NGOs should have the opportunity to engage in any legal activity. It should be noted here that until 2017 only foundations were allowed to do business directly under their legislation. But paragraph 1 of Article 8 of RA Law "On Non-Governmental Organizations" was finally changed after extensive experiments and efforts, defining that "organization has the right to carry out

business activities by the goals defined by the charter, to manage its property and results of activities for that purpose, and to create a commercial organization or become a member of it in the manner prescribed by law” thus, for the first time in the history of Armenian legislation, NGOs were allowed to engage in direct business activities, and the discriminatory attitude towards them was eliminated.

International experience shows that business income is one of the most important sources of income for NGOs worldwide. However, by allowing NGOs to engage in business activities, the legislature has placed an additional burden on the organization, including the obligation to maintain separate business records: including information on it in the reports provided by law and, at the same time stipulating that the profits from the business activities of the organization should be used only for the statutory purposes of the organization.

There is some concern with the definition of “compliance of business activities with the statutory objectives”, as the latter may in practice give rise to a wide and spatial interpretation and qualify as an act under Article 169.27 of the RA Code on Administrative Offenses, i.e.: Implementation of activities by the NGO by the goals of the charter, which may lead to the forced liquidation of the organization.

Therefore, we consider it expedient to clearly define at least the minimum compliance criteria: to avoid arbitrary interpretation of the norm, based on the approach that the implemented business activities should not contradict the mission and goals set by the charter of the organization. Therefore, as a solution (i.e., the need for change in other legal acts conditioned by the adoption of the SE concept) we propose to make changes and amendments to the RA Law on Non-Governmental Organizations stating that the activity is considered by the charter if it does not contradict the NGO charter.

Otherwise, it turns out that this provision allows the NGO to engage in business activities, to ensure its financial stability, but not by regulatory law, nor does TC use any preferential tax regimes to engage in such activities. It should be added that the mentioned provision restricts engaging in entrepreneurial activity on the condition that the income received from it will be directed only to be spent for the statutory purposes of the organization. In this regard, we think that some clarification is needed, as it is necessary to take into account the following circumstance: the organization, engaging in business activities and spending it only for its statutory purposes, will be obliged to have proper justifications and reports that confirm the fulfillment of the given requirement. As for the tax authorities, the latter, to exclude possible frauds and abuses, may start to demand additional documents, which, especially in the case of NGO SEs, will contribute to the growth of administration and unnecessary paperwork, thus appearing in the focus of tax authorities. Here we consider the best solution to remove the word “commercial” in the phrase “commercial organization” in the relevant parts of Article 254 and Article 267 of the TC.

It should be added that following point 8 of Section 1 of the Recommendation “Basic Principles” of the Recommendation, the state should pursue a preferential tax policy to promote the right of the organization to do business ³.

According to Article 26 of the RA Law on Non-Governmental Organizations: if the organization was financed from public funds in the amount of five million and more AMD during the reporting

³ https://search.coe.int/cm/Pages/result_details.aspx?ObjectID=09000016805d534d

year, then its annual financial reports submitted to state bodies following the law shall be subject to mandatory audit in terms of financing from public funds.

It is necessary to assess the justification of the requirement to fulfill the obligation under the RA Law on Non-Governmental Organizations in the case when the amount of funds provided during public funding does not include separately the amount of funding required for mandatory auditing, which later becomes an additional burden for NGOs. In many cases, the amount of funds paid to independent auditing firms is quite large compared to the amount of public funds provided to the organization.

It should be noted that international donor organizations usually allocate a certain amount of money for the audit of the programs implemented by the organization, we suggest fixing this approach in case of attracting public funds.

The above regulation causes problems especially in terms of SE context in the case when an NGO entitled to engage in business activities to achieve its statutory objectives, is engaged in entrepreneurial activity in the manner prescribed by law and participates in procurement for state needs and supply of goods within any procurement procedure; state or community funds are the source of the organization's income for the purchase of goods for state needs and the implementation of contracts for the supply of goods, works or services within the framework of any procurement procedure. In this case, the legal requirement for a mandatory audit of the NGO becomes applicable, as the income received is also considered a public asset. The existence of such a requirement, in our opinion, is discriminatory, because unlike other commercial organizations operating in the same factual circumstances, in the case of an NGO, the price of a product/service overburdened with a mandatory audit requirement increases by the cost of the audit service and the cost of time and resources. There is no such requirement for entities with other organizational and legal statuses.

Proposal. To eliminate existing discrimination, increase transparency and improve the efficiency of the use of public funds, we propose to eliminate the requirement of mandatory audit of publicly funded projects, if necessary, include them only in state-funded contracts.

2.2.3 Commercial Organizations

They belong to some legal entities considered to be commercial organizations: full partnership, trust partnership, limited liability company, additional liability company, joint-stock company.

For the convenience of reading, a detailed description of each of the most common organizational forms in the RA is attached to this document in Table A.

2.2.3.1 Limited Liability Companies, Joint Stock Companies

Under Article 95 of RA CC and RA Law on Limited Liability Companies, a limited liability company is a company established by one or more persons, the share capital of which is divided into shares in the amount defined by the charter. The participants of the limited liability company are not responsible for its liabilities and bear the risk of losses related to the activities of the company within the limits of the value of their contributions."

In the case of joint-stock companies, according to Article 95 of the RA CC and RA Law on Joint Stock Companies, this is a company whose share capital is divided into a certain number of shares. Joint-stock companies can be open and closed.

2.2.3.2 Individual entrepreneurs

RA CC gave the citizen the right to engage in entrepreneurial activity from the moment of registration as a sole proprietor, without forming a legal entity.

Moreover, citizens have the right to engage in entrepreneurial activity without state registration or registration (without forming a legal entity or being registered as a sole proprietor) if they have been registered with the tax authority in accordance with the law and have signed a joint activity contract to produce agricultural products, as well as in other cases prescribed by law. Citizens engaged in agricultural production are subject to entrepreneurial activity only within the limits of the given joint activity contract.

The rules governing the activities of legal entities that are considered commercial organizations by law shall apply to individual entrepreneurs unless otherwise provided by law, other legal acts, or the essence of the legal relationship.

2.2.4 Charity Law

The Charity Law defines charity as the provision of voluntary, philanthropic, material, and in-kind assistance to individuals, health, and non-profit organizations by individuals and legal entities for the implementation of charitable purposes. The same law does not consider charity to provide money and other material resources to parties and commercial organizations (except for healthcare organizations).

It is noteworthy that Article 2 of the Law on Charity covers the following broad scope under the purpose of charity:

- 1) to support individuals (disabled, orphans, unemployed), well as low-income families who are unable to provide for themselves financially and emotionally;
- 2) to support other non-profit organizations;
 - 2.1) to support the development of healthcare;
- 3) to provide material assistance to victims of war, natural disasters, infectious diseases, epidemics, and other emergencies and participate in their elimination;
- 4) to assist the unemployed in need of social assistance in finding employment through job creation or training of the unemployed;
- 5) to support the implementation of programs in the fields of science, education, art, literature, healthcare, sports, and physical culture;
- 6) to support the implementation of programs for the preservation and restoration of historical, architectural, cultural, and art monuments;
- 7) to support the implementation of nature and environment protection and improvement works;
- 8) to support the implementation of social programs approved by the RA Government.

2.2.5 RA Labor Code

RA LC has no special regulation defining SE as a specific type of employer.

Article 102 of RA LC regulates voluntary work and assistance, which according to RA LC can not be considered illegal. The procedure and conditions for such work are defined by law.

In other words, RA LC envisages the regulation of voluntary activities by law, such as the Law on Charity and the Law on Non-Governmental Organizations.

Thus, according to Article 9 of the Law on Charity: "Volunteers are individuals who, for the purposes of this law, perform unpaid work for the benefit of charities." According to Article 10 of the same law: "Recipients of charity are individuals and legal entities who, with their consent receive charitable support."

The next regulation on volunteers is defined by Article 17 of the Law on Non-Governmental Organizations, according to which: "The organization can have beneficiaries in accordance with its goals, as well as involve volunteers in its work."

The RA Law on Charity and RA LC apply to legal relations involving volunteers to the extent that these regulations do not contradict the Law on Non-Governmental Organizations, as follows:

If volunteer work exceeds 20 hours per week, then the organization signs a volunteer contract with the volunteers. Moreover, the organization provides compensation to the volunteer for the expenses actually incurred by the latter as a result of the voluntary work. Here, however, it should be noted that RA TC does not allow volunteers to exercise any right to a reduced income to volunteer, considering the ban on involving volunteers in the organization's business activities.

Concerns: Based on the analysis of the following legal regulations, there are grounds to conclude that:

- there is a risk that those who volunteer for up to 20 hours per week will be considered unregistered workers if they do not sign voluntary employment contracts, under provisions of Article 412 of the TC and Government decision N 1214-Ū of September 28, 2017.
- There is a real restriction on the freedom to involve volunteers in volunteer work if the organization or program is not classified as "charitable" in accordance with the law.

Proposal: We propose defining the term "voluntary", providing clarification on the possibility of using volunteer work: prior to its legislative regulation, as for TC: under Part 6 of Article 17 of the Law on Non-Governmental Organization to add a compensation rate to be paid to volunteers in the "Normalized Expenses" section of the TC or in the section of cash amounts to include volunteers among other accountable persons.

In addition, we propose considering the possibility of relevant legislative changes, where SE will be allowed to engage volunteers in for-profit activities if SE has signed respective voluntary employment contracts with the latter, thus allowing volunteers to exercise their right to deduct income from volunteering and remove the ban on involving volunteers in the organization's business activities.

2.2.6 RA Tax Code

The involvement of active grant programs characterized the initial stage of SE development. However, organizations often face uncertainties in grant taxation. The term “grant” is defined in RA legislation by Government Decision N 1934 as of 2003, according to which: “A grant is a non-refundable, non-repayable disbursement from the budget to an organization for the implementation of its statutory objectives for any branch of the economy or activity.”

According to Part 5 of Article 5 of the TC. “The concepts used in civil, administrative, criminal, labor, family, land, natural resources use and environmental protection, licensing, notification, permitting and other special spheres are used in the Code with the meaning and significance used in the relevant legal acts unless otherwise provided by the Code unless otherwise provided by the Code.”

In terms of application, it is not clear what is considered a grant in the sense of TC, when it comes to non-state budget funds, that in the context of the constitutional arrangements and a result of the analysis of the relevant provisions of the TC to be considered a tax at the same time it is necessary to define the elements of its content by law clearly, and the absence of at least one of them means that the tax is considered undefined.

The Constitutional Court also noted that the phrase “taxes prescribed by the law” implies the definition of both the tax and its constituent elements exclusively by law. In each case, the law will consider the tax liability, if not only it is fixed by law in purely legal terms, but also its constituent elements are fully reflected in the law.

However, in this case, the content of the element considered as income (in particular, the grant) is revealed not by TC, but by the subjective assessment, which may lead to unlawful interference with a person’s property rights.

The term in question was considered in terms of legal correctness and within the context of the positions expressed herein, we state that it is not clear from the mentioned term to whom it is addressed, and what actions should be taken by its addressees.

Proposal: In the context of SME development, we suggest considering the clarification of the term “Grant” in terms of funds received from the non-state budget. As an example, we offer the following definition: “The grant is a means of gratuitous & non-refundable support of a specific purpose endowed with program accountability. To record the expenditures of the grant funds, the organization is obliged to keep separate records for all operations of the targeted use of the received funds.”

It should also be noted that according to the Armenian Legislation, when calculating the profit tax, the employer already has the opportunity to reduce the salary by additional 150%, which can be used in terms of the connection between the SE social problem and the tax exemption⁴, and the clause 6 of the same part envisages deduction from the tax base in the amount of assets provided to non-commercial organizations, the amount of work performed for them and (or) the services provided to them, but not more than 0.25% of the gross income of the tax year.

⁴ Pursuant to Article 123, Part 1, Clause 6 of the Law on Profit Tax, when calculating the tax base profit taxpayers may deduct 150 percent of the total sum of the salary calculated and other equivalent payments, as well as the amount of income from a civil contract for each disabled person considered a hired worker, as well as a person working on the basis of a civil contract or a service provider to a profit taxpayer under a civil law contract.

Another regulation is also defined in Part 4 of Article 159 of the TC, according to which RA resident organizations are eligible for a certain tax privilege: dividend tax refund in the amount of the tax, the procedure and conditions of which are defined by the RA Government ⁵. See the sample calculation below:

Assuming a trading XYZ SE announces a profit of 50 million AMD for the reporting year 2020 approved by the Annual General Meeting of Shareholders on April 15, 2021, with a decision on further distribution of profits, according to which 30% of the profit to be distributed among three shareholders (individuals with equal shares), and the remaining 70% should be directed to the replenishment of organization's capital for the implementation of social and other development programs.

According to the decision, the organization calculates the dividends payable to the participants as of May 15, 2021 ((50 million x 30%) / 3 persons = 15 million / 3 persons = 5 million AMD gross per participant), withholds income tax from dividends at a rate of 5% (for each shareholder - 5 million x 5% = 0.25 million drams), and transfers the amount due to each shareholder in the amount of 4.75 million drams (5 million - 0.25 million taxes), total collected income tax is 0.75 million drams. According to the business development imperative, the participants decided to invest 2 million AMD of the dividend they received from each participant, and the state registration of the investment amount was carried out by the State Register Agency of Legal Entities of the RA Ministry of Justice on June 20. In this case, after June 20, each participant by submitting the necessary documents acquires the privilege of dividend tax refund for the investment amount, but not more than the amount of tax collected. As the participant made the investment in the amount of 2 million AMD, but was charged only 0.25 million AMD income tax, 0.25 million AMD is subject to refund (if the participants decided to invest 0.2 million AMD, only the investment of 0,2 million AMD would be refunded, and the 0.05 million AMD of the tax paid (0.25 million - 0.2 million) would not be refundable).

This provision, in our opinion, is applicable to the organizations operating in form of SE and this is serious financial support for them.

2.2.7 Law on Advertising

The Law on Advertising establishes quite favorable regulations for social advertising, which is welcome. So for example, "The Law on Advertising defines social advertising as non-commercial in nature (not for profit): human rights & responsibilities, public health, as well as information disseminated to inform the public about healthy lifestyles and social protection, volunteering, nature conservation, educational programs, patriotic upbringing, cultural preservation, dissemination and development, disaster management, protection of national interests and other areas, which is legally recognized as a social advertisement.

Thus, RA already has a precedent for qualifying any type of activity as social. Moreover, using the privileged status of social advertising, a wide range of SE awareness and cognitive programs and campaigns can be implemented.

⁵ <https://www.arlis.am/DocumentView.aspx?DocID=117147>

It is necessary to refer separately to the procedure of advertising as social recognition. Thus, external social advertising, which will be spread within the administrative boundaries of one community, can be recognized as a social advertisement by a community commission set up by the mayor. Three members of the community commission established by the community head are nominated from the representatives of the local self-government bodies, and five members from civil society. The mayor informs the applicant about the decision of the community commission set up by the mayor after the advertisement is recognized as social within three days. After the advertisement is recognized as social, it can be distributed in the whole territory of the Republic of Armenia or within any administrative-territorial unit of the Republic of Armenia that is exempt from road tax.

Thus, Armenia already has a precedent in, to qualify a type of activity as social. Moreover, using the privileged status of social advertising, a wide range of SE awareness and cognitive programs and campaigns can be implemented.

Proposal: To develop and promote SE, we propose to provide certain additions and regulations to the Law on Advertising, through which the products produced by SEs and/or the services provided, and/or the opportunity to engage in work/volunteering, usage of the trademark or other means of identification of an SE organization may also be considered as social advertising.

2.2.8 RA Law on Local Self-Government

According to Article 180 of the RA Constitution, “a community is a community of residents of one or several settlements and is a legal entity under public law.” As such, the term “legal entity under public law” is not regulated by the RA legislation.

The RA law “On Local Self-Government” article 12, part 1: a) According to the sub-clause, one of the obligatory tasks of the community is, among other things, the promotion of charity: the establishment and financing of cultural, educational, scientific, health, sports, social and other institutions in the community; as well as to ensure their financial independence.

According to article 18 of the same law, part 1, sub-clause 15, one of the powers of the community council is to trade with community institutions and the community and establishment non-profit organizations, making decisions on reorganization or liquidation; and sub-clause 24 of the same article stipulates membership in unions established by communities and the authority of the community council to make decisions about paying their membership fees.

3. PART II

Below are the results of the revision of the draft of the "SOCIAL ENTREPRENEURSHIP DEVELOPMENT CONCEPT" project submitted to the RA Government and proposals and amendments thereto.

3.1 Concept Review

The "SOCIAL ENTREPRENEURSHIP DEVELOPMENT CONCEPT" draft decision of the RA Government (hereinafter referred to as the Concept) consists of the following sections: EXECUTIVE SUMMARY, INTRODUCTION, BACKGROUND, PROBLEMS AND OBJECTIVES, INTERNATIONAL EXPERIENCE, FINANCIAL ASSESSMENT, SOLUTIONS SUPPLIED, EXPECTED.

The authors of the Concept refer in detail to the current situation and problems in the field of SE, the main directions of problem-solving and necessary measures, the resources required to implement the necessary measures to solve the problems, and the expected results. In this regard, our suggestions and changes are presented in Section 3.2 of this Study.

3.2 Proposals, changes

Proposals and changes to the concept are the following:

- It is recommended to send the Concept to the Legal Acts Expertise Agency of the RA Ministry of Justice to clarify the legal terms and concepts used, to avoid possible contradictions and ambiguity with the current legislative acts. It is worth noting, that according to the experts elaborated the Concept, the mentioned body has already revised the latter, nevertheless, in our opinion, there are still some lacks that are recommended to make up.
- For example, terms used in the Concept within the context of legal certainty shall be expressed in a way that allows avoiding the contradiction with terms used in other legal terms, that are being used not within the same meaning (for example: there is a high probability that some terms used in the Concept could be interpreted within the meaning of the RA law 'On Social Assistance', that could raise contradiction while interpreting them in case of disputes or practic implementation of the Concept). It is recommended to send the Concept for proofreading, taking into account the linguistic inaccuracies and mistakes in the Concept.
- Add that the adoption of the Concept is aimed at solving the existing legislative problems and further development of the sphere.
- Recommended to add in the Concept the relevant provisions on the need to adopt other legal acts in connection with the decision of the RA Government, as it is not clear whether there is a need to adopt or amend other legal acts, or it is stated that current provisions need to be amended and changed, which will stimulate the development of the SE sector.

- It is proposed to make changes in the charter of the organization through the Agency of the State Register of Legal Entities of the RA Ministry of Justice, to classify the organizations with the help of the current legislation, based on the decision of the founder (founders/participants), adding relevant provisions to distribute business profits in the areas intended for SEs and to assume other procedural obligations for SEs.
- It is proposed with the help of provisions of the current legislation to classify organizations as SE through the Agency of the State Register of Legal Entities of the RA Ministry of Justice, based on the decision of the founder (founders/participants), make changes in the charter of the organization, by adding relevant provisions on the commitment to social entrepreneurship, which will clearly define the distribution of business profits by the organization in the areas intended for SEs and to assume other procedural responsibilities for SE.
- It is proposed to add the part related to the required means, which is referred to in point 3 of the BRIEF SUMMARY of the Concept, which is missing in the document.
- It is proposed to amend the Concept with the Financial Impact Assessment.
- It is proposed to develop an accountability system that will not create a disproportionate burden on SEs and provide useful and necessary information to the public and state. This information should be fast and accessible to the public, as the accountability objectives of SEs include public oversight of their activities & the protection of the rights of individual donors and beneficiaries.
- Add a mechanism for involving young people and women in SE, the importance & promotion of which was also emphasized in the "Armenia Development Strategy 2014-2025"⁶, it should include a clear guide to business skills and capacity development.
- It is proposed to update Brief Summary of the Concept, which proposes to redistribute a portion of the funds of state foundations/funds providing the viability of socially vulnerable groups through various payments to the SEs that provide employment to the latter: taking into account the fact that at the time of drafting this paper, such practice already exists (for example, in regional communities, entrepreneurs establish organizations and hire employees to create additional jobs, which in turn coincides with the territorial centers of the Unified Social Service, former employment centers). Very often, at the initiative of the regional centers of the Unified Social Service, the latter provides financial assistance to these entrepreneurs without additional procedural requirements & paperwork.
- It is proposed to revise point 2 (c) of the Concept, which proposes to set certain preferences for SE representatives in the framework of public procurement, taking into account its risk and the possibility of abuse, which will certainly be the result of discrimination. Nevertheless, it is proposed to give some preference to those SEs that apply to participate in public procurement, setting certain criteria for granting pre-emption.

⁶ <https://www.gov.am/am/prsp/>

- In the Brief Summary of the Concept, it is recommended to revise the proposal for income tax reduction for people with disabilities enrolled in SE after assessing possible positive and negative consequences.
- It is proposed to rewrite the sentence “Establish a more flexible system for involving volunteers on a free basis” in Section 1 (1) of the Concept as follows: “Establish a more flexible system for SEs for involving volunteers in social programs on a free basis.”

4. PART III

4.1 Proposals for effective business and ecosystem development in SE today. Legal overview, tax, and legal aspects of SE and ecosystem development

In general, taking into account the importance of SE and ecosystem development and the need to involve youth and women, it is recommended to organize courses and masterclasses on raising legal education, during which young people and women will be introduced to business start-ups, legal and tax aspects, SE specifics and potential points for start-ups, including but not limited to:

- Establishment of the organization, selection of organizational and legal form;
- Accounting basics;
- Labor legislation;
- Tax legislation;
- Financial Assistance Programs, Donor Relations, and Accountability.

Obvious caution should be exercised in the issue of state support. In any case, discrimination harms the business environment and leads to an unhealthy atmosphere and the creation of unequal competition.

In our opinion, in the context of the application of tax benefits, it is important that the implementation of social policy by the State coincides with the goals of the SE and if the social activities carried out by the SE coincide with the social programs implemented by the State, it is possible to raise the issue of the privilege at the point of intersection of these two programs, for example, when the scope of SE activities intersects with the measures of state regulation of social assistance provided by the RA Law on Social Assistance, and the provision of social services itself coincides with the objectives of SE. Thus, according to the provisions of Article 34 of the RA Law on Social Assistance, the authorized state body, state territorial bodies, local self-government bodies, territorial bodies cooperate with organizations providing social services in implementing the state policy of Social Assistance. The authorized state body, state bodies of territorial administration, local self-government bodies, territorial bodies, as well as organizations providing social services shall exchange information on the recipients of social assistance and the social services provided by them in the manner and the cases defined by the legislation of the Republic of Armenia. The authorized state body, state territorial bodies, local self-government bodies, territorial bodies, as well as organizations providing social services shall cooperate within the framework of the social cooperation agreement adopted for that purpose, which is provided by the RA Law on Social Assistance and includes the goals and principles of cooperation, social assistance network, social work, etc.

In other words, in the above-mentioned case, the State will have certain cost savings for the given social programs, and it will be possible to negotiate tax privileges without an unsubstantiated burden on the state budget.

In addition to the above, let us add that RA Government Decision N 910-N of July 27, 2017 provides for exemption from VAT within the framework of subsidies, subventions and grant programs (supply of goods, performance of work and / or provision of services (ie business activities)), if these activities include programs in the fields of information technology, tourism, agriculture, science, education, energy and environment, which promote the development of the RA economy.

In response to our inquiry on the statistics on the use of the privilege, it turned out that only 2 organizations have used the opportunities provided by the above-mentioned normative legal act during the last four or more years. However, even this small number, as a precedent, suggests that the RA Government Decision N 910-N of July 27, 2017, is in itself a very important and potential opportunity to discuss certain privileges in the context of SE legislation and to build a public-private dialogue.

4.2 Minutes of focus group and consultative meetings on the process of creating SEs

During 2021, certain focus group and consultative meetings were held, the brief protocols of which are given below ⁷.

During the consultative meetings, representatives of NGOs and the business community were asked pre-designed questions. Was discussed the experience of Armenian SEs and the processes of providing them legal status, strengths, and weaknesses of various organizational structures, the main differences. Representatives of NGOs with experience in launching SE took part in the meetings. The purpose of the surveys was: to identify experiences of running SEs, including successes and failures, how to find out the approaches to possible models for creating SEs, to understand the preferred model of SEs, and outline the most efficient format.

Representatives of Tavush region community leaders and other representatives of Ayrum, Berd, Noyemberyan, and Ijjan, enlarged communities of the Tavush region, and their rural communities took part in the survey. The purpose of the meeting was to identify the experience of launching SEs in the community management process, including successes and failures, how to figure out the approaches which model is needed to create SEs: outlining the most efficient form and the ratio of NGOs, business and state participation in them.

Armen Amiraghyan noted that in addition to the existing agricultural problems in the community, the border communities also have security and defense issues. He spoke positively about the idea of creating SEs, emphasizing that NGOs should have a great deal of involvement and decision-making authority. The latter added that community and business representatives should be involved in the implementation of program activities.

Hasmik Melikyan said that the Berd community initiates a lot of community development programs, mainly to improve the social sphere. As for the initiatives of other entities, she stressed the community's readiness for cooperation. In her opinion, it is more important to separate the areas of program activities, each area to be managed by a competent organization/community.

⁷ <https://developmentprinciples.org/hy/հավելված-3-սձ-ների-ստեղծման-գործընթացի/>

The participants also touched upon financial and tax issues. Hasmik Melikyan noted that the organization should act transparently and accountably in any case. Armen Amiraghyan suggested creating a website within the framework of the programs, where all the activities and their financial reports will be posted, which will ensure the transparency and accountability of SEs.

4.3 General considerations of SE financing (soft loans, etc.), financial components

The state, the Central Bank, and financial institutions work together through special lending programs to support various beneficiary groups (students, youth, scientists, soldiers, civil servants, etc.) to obtain affordable lending.

Special lending programs are mainly related to mortgage loans. Such loans are provided to acquire, renovate or construct real estate, pledging the given real estate, and in case of construction of a land plot, also the right to build a land plot. The goal is to create conditions that will facilitate the repayment of loans and interest payments, provided that the funds provided to finance the acquisition of goods, services or works are available to middle- and low-income people to improve their housing conditions through mortgage lending.

Another possible type of government-sponsored loan is an education loan, which aims to help young people get paid higher education through affordable loans. Other types of loans are aimed at helping young people solve other everyday problems.

Such support is mainly provided through the provision of funds to repay the loan and pay interest on financing the acquisition of goods, services, or works, mainly through interest rate subsidies, reduction of down payment, and extension of the term. However, different programs have their own conditions.

“Apartment for Youth” and “National Mortgage Company” organizations refinance these loans. They do not work directly with customers, but cooperate with banks and credit organizations, providing them with low-interest long-term loans.

The goal of the National Mortgage Company is to make mortgages available to anyone who needs financing to improve their housing stock.

The mission of the Housing for Youth program is to provide favorable lending conditions for young people by providing low-interest-rate lending opportunities to address housing, education, and other everyday issues.

The implementation of all the programs described above is based on the social component, and state support was aimed solely at promoting that social component. Given all this, we think that there are already precedent support mechanisms in SE public assistance programs, & using the above operating models as a precedent; it will be possible to provide state support to the companies involved in the SE sector in the issue of providing other loans.

As for the development of credit-specific & other products for SEs, in our estimation, there will be no need for additional work, as the RA banking market is well-established, self-regulating, & experience shows that based on the direction of social programs implemented by the state: banks & credit organizations respond rather quickly to current market demands.

This study would not be complete if it did not address the international experience, in particular the experience of countries such as Georgia, Australia, Poland, Lithuania, and Slovenia. It should be noted that in all of these countries, there is no specific legal framework for SEs.⁸

However, it should be noted, for example, that Lithuanian legislation (the Law on Social Enterprises) defines SE as a unit focused on creating new jobs for members of vulnerable groups/communities. To obtain SE status, the founding documents of the organization must clearly state the purpose of the employment of the beneficiaries or their social integration, and these organizations must not operate in areas prohibited for SEs.

Enterprises with such status (Work Integration Social Enterprise (WISE)) are eligible for government funding and other benefits, including tax benefits.

Another type of enterprise, the Community Interest Company (CIC), was introduced by the United Kingdom in 2004, initially allowing charities to do business, but is currently only used for SEs.⁹

The CIC has a structure similar to that of a traditional company but is subject to the principle of “asset blocking”, i.e., a specific asset limit and a well-defined threshold for the distribution of dividends for this type of company.¹⁰

In particular, in this type of organization, only 35% of the profit can be distributed in the form of dividends. The CIC structure is of particular interest to socially responsible lenders or investors, as entities investing in these types of organizations enjoy appropriate tax benefits. Some Canadian states have a special legal framework that focuses on the introduction of social missions in business based on the CIC principle. This legal form allows the social mission to be carried out through business activities, directing the excess profit to the satisfaction of social interests and imposing restrictions on the distribution of dividends and capital.¹¹

5.SUMMARY

Summarizing the challenges in the field, we believe that the fact that SE promotion in RA started with the active support of international organizations, the initial beneficiaries of which were non-profit organizations, in turn, led to certain systemic problems. In particular:

- The main problem is that the skills of the staff of non-profit organizations do not correspond to the necessary business thinking (business thinking), which in turn always leads to failure of business activities;
- Lack of experience in resource planning, work for an organization, and production capacity calculation leads to incorrect management of non-profit organizations;
- By emphasizing the social component of SE, the business component is pushed out, which in turn damages the stability of the organization;

⁸ Social Entrepreneurship in Georgia – Legislative Environment, Challenges and International Practice

⁹ Doeringer, MF. Fostering Social Enterprise: a Historical and International Analysis. See. Source: <http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=1052&context=djcil>.

¹⁰ Desk Research on International Experience in State Support Mechanisms for Social Enterprise Development p.110:

¹¹ <http://www.fin.gov.bc.ca/prs/ccs/>

- SEs usually 'survived', i.e., succeeded for the most part as long as there was donor support, but after the end of grant funding, business activity gradually declined, leading to complete exhaustion of grant funding;
- Support through grants, in turn, has led to the formation of a "parasite" mentality; most failures are the result of expected support;
- Support through grants, in turn, has led to discrimination and unhealthy competition in the sector, thus disrupting existing market relations and rules.

Given the systemic problems described, we believe that at this stage in terms of SE development in RA it is necessary to:

- At this stage, SE should be considered as a successful enterprise; then, after ensuring stability, it is necessary to establish more detailed control over the social component and accountability.
- It is necessary to devote a lot of space to awareness-raising activities as a part of donor support, here the promotion of social advertisements by law is a great help, which has already been mentioned in this document.
- Donor support should largely be directed to developing and improving of SE staff's entrepreneurial knowledge.
- Any form of discrimination that could undermine healthy competition must be ruled out.
- Donors should not form an expectation of sustainable support for SE through their actions.
- State support should be very limited, with a maximum emphasis on community support, discussing and developing possible options.

We believe that described measures and proposals are sufficient to overcome these key barriers to SE development at this stage.

As for the current RA legal framework and existing regulations, based on their study, it is worth noting that there is currently no vital need to adopt a separate law on SEs, especially considering the UK, Australia experience where SEs have been successfully set up and developed without special regulation . And, at the same time, there is no legal impediment to its adoption. However, we think that prior to regulating the sphere through a separate legislative act, it is necessary to take into account the following: in countries where SE has been established as a separate type of entrepreneurship (Spain, Czech Republic, Slovenia, some of the USA states), the legal regulation of SE activity has been carried out after the SE field has more or less stabilized, i.e., after some time has passed, which was enough to assess the pros and cons of the industry, identify gaps and develop appropriate arrangements. It is desirable to keep in mind that at this stage if the option of adopting a separate law is chosen, it will take quite a long time to draft the law, hold public discussions and hearings, advocate, and lobby. In addition, at this stage in the development of SEs, as long as the gaps and risks that need to be addressed are not clear, the choice of this option may delay the organic development of SEs. However, we believe that the creation of separate legislation may be the long-term goal of the program at the Impact level.

¹² Social enterprises and their ecosystems in Europe - Comparative synthesis report; <https://ec.europa.eu/social/main.jsp?catId=738&langId=en&pubId=8274>

¹³ Social Entrepreneurship in Georgia – Legislative Environment, Challenges and International Practice

Table A to RESEARCH PAPER

OPPORTUNITIES TO BUILD A LEGAL FRAMEWORK FOR THE DEVELOPMENT OF THE SOCIAL ENTREPRENEURSHIP MODEL

The most common organizational forms in RA, description, details

Limited liability company	Joint-Stock Company	Foundation	Private Entrepreneur or PE	Non-Governmental organization
<ul style="list-style-type: none"> - a company established by one or more persons; - up to 49 participants - there is no minimum rate for authorized capital 	<ul style="list-style-type: none"> - a company established by one or more persons - complicated registration procedure - a separate requirement to maintain a register of shareholders - request of the audit committee 	<ul style="list-style-type: none"> - non-membership organization created based on voluntary property payments of citizens and (or) legal entities - pursues social, charitable, cultural, educational, or other socially useful goals 	<ul style="list-style-type: none"> - Individual - independently, on its own behalf and at its own risk, carries out activities aimed at obtaining profit (income). 	<ul style="list-style-type: none"> - public association of individuals and (or) legal entities - non-commercial organization
All applicable tax fields, depending on the type of activity and turnover	All applicable tax fields, depending on the type of activity and turnover	General field of taxation	All applicable tax fields, depending on the type of activity and turnover	General field of taxation
Advantages: <ul style="list-style-type: none"> - Quick registration - Minimum requirements for document circulation - for-profit activities of any kind - most flexible form - restrictions on privileges & rights: on the rights & obligations of the founders 	Advantages: <ul style="list-style-type: none"> - Extensive management & accountability capabilities - for-profit activities of any kind 	Advantages: <ul style="list-style-type: none"> - Quick registration - Extensive management & accountability capabilities 	Advantages: <ul style="list-style-type: none"> - Quick registration - Minimum requirements for document circulation 	Advantages: <ul style="list-style-type: none"> - Quick registration - easy administration
Disadvantages: <ul style="list-style-type: none"> - In case of change of participants, mandatory registration in the state register - Mandatory registration in the state register in case of capital change 	Disadvantages: <ul style="list-style-type: none"> - complicated document circulation & requirement to maintain a register of shareholders - no obligation to acquire the founder's share in case the founder wants to leave the business 	Disadvantages: <ul style="list-style-type: none"> - Entrepreneurial activity is very limited - requirement to keep separate reports 	Disadvantages: <ul style="list-style-type: none"> - Wide range of liabilities, liability with own property - not possible to run business with several participants 	Disadvantages: <ul style="list-style-type: none"> - The carried out business activity must not contradict the charter of the organization - requirement to keep separate reports

Table B to RESEARCH PAPER

OPPORTUNITIES TO BUILD A LEGAL FRAMEWORK FOR THE DEVELOPMENT OF THE SOCIAL ENTREPRENEURSHIP MODEL

Taxation regimes applicable in RA, forms, description, and details

There are general and special taxation regimes in RA. Under the general taxation regime, organizations, SEs, and notaries are taxed in particular with VAT and (or) profit tax.

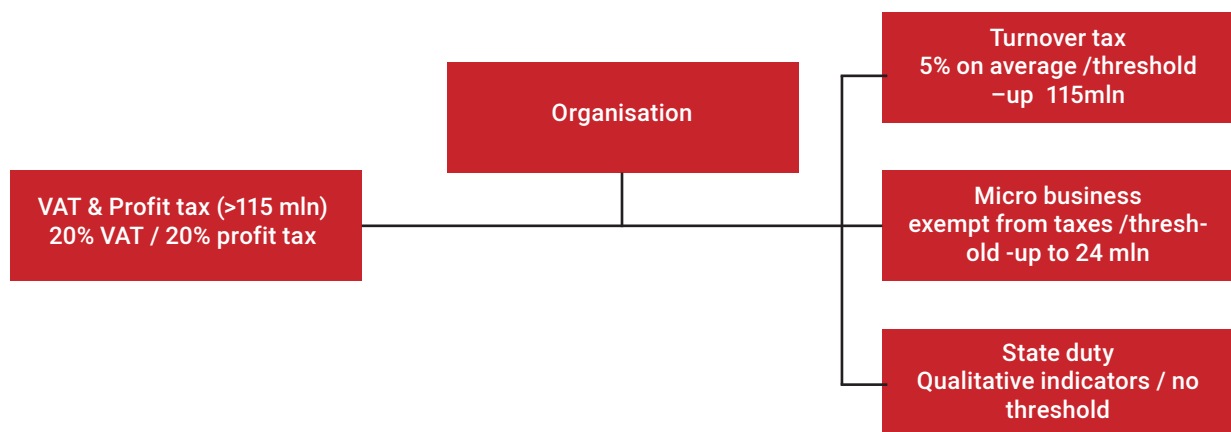
Special taxation regimes:

1) Within the framework of the micro-business regime, organizations and individuals are exempted in certain cases, in particular, from VAT and/or profit tax, as well as from turnover tax.

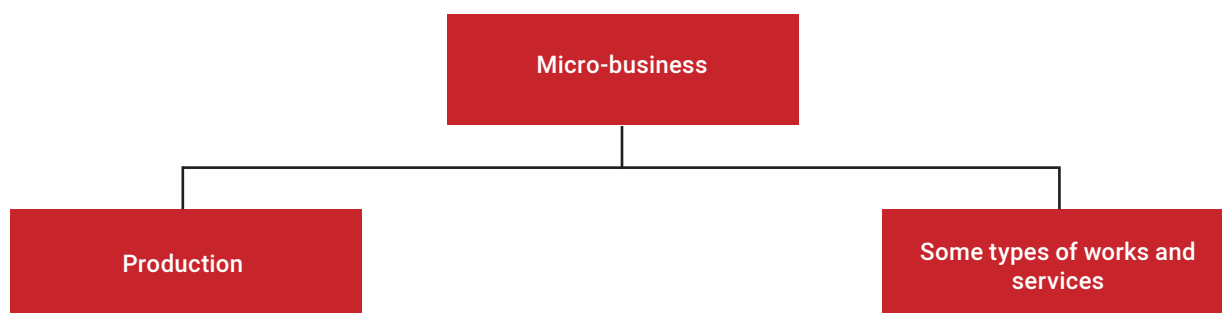
2) Within the framework of the turnover tax regime, the organizations are taxed with the turnover tax, which replaces the VAT and (or) profit tax, and the individual entrepreneurs and notaries with the profit tax and the turnover tax, which replaces the VAT.

Other taxes & fees (which are not replaced by turnover tax, or from which micro-enterprises are not exempted) related to special regimes for organizations operating in special tax regimes, SEs & notaries are calculated and paid in the prescribed manner.

The current tax regimes in RA can be schematically represented as follows:



Under the tax regimes provided by law, the possibility of micro-business is relatively new and defines a rather preferential tax framework, which has the following schematic.



Let's take a brief look at each of the regimes, describing their features.

1. Micro-business regime

- Businesses operating in this system are exempt from the obligation to calculate all state taxes and pay to the state budget, and as a tax agent - from the obligation to calculate, withhold and transfer the tax to the state budget.
- A monthly income tax of 5,000 AMD is subject to payment for each hired employee from the income paid (calculated) for hired workers engaged in micro-business
- To become eligible and enjoy a preferential taxation regime an application should be submitted to the tax office to declare the status as a micro-business

Eligible for this regime categories:

- Individual entrepreneurs
- PEs or individuals not registered as a notary (see the list in Annex 3),
- commercial organizations before state registration.
- Within 20 days following the registration.
- If already registered in previous years, by February 20 of the reporting year.

The micro-businesses submit an annual report on the activities of the previous year by February 1 of the following year.

There are other restrictions on operating in this regime which is provided in Article 267, part 5 of the TC.

2. Turnover tax

- Applies to a base with a turnover of up to 115 million, has operating restrictions,
- Tax is calculated on turnover and not profit,
- No accounting is required,
- Reports: quarterly, in case of PE, also annual,
- The tax rate is on average 5% (the scale of other applicable rates is defined in Article 258 of the TC),
- Businesses operating under this regime are not exempt from agent duties in terms of income tax and profit tax,
- An application should be submitted every year to be considered as a turnover taxpayer,
- PE operating under this regime pays monthly AMD 5,000 profit tax and AMD 5,000 social fee as business tax and fee,
- This regime applies to commercial companies only.

Other restrictions for operating under this regime are presented in part 3 of article 254 of the TC.

3. VAT and profit tax

- Applies to a base with a turnover of more than 115 million and has specific features of activity;
- VAT is calculated on turnover, profit tax - on profit;
- Accounting is required;
- Types of reports to be submitted: VAT monthly, annual profit tax report;
- VAT tax rate - 20%, Profit tax rate - 18%;
- Businesses operating under this regime are not exempt from the agent obligations in respect of all taxes (including all non-resident taxes);
- To take advantage of the system, it is necessary to submit a Declaration to be a VAT payer in some cases to obtain the right of offsetting VAT;
- VAT privilege is defined only for non-commercial organizations operating in this system for threshold up to 115 million (ie not considered VAT payers);
- VAT is an indirect tax, profit tax is a direct one.

4. Excise tax, other taxes

Excise tax is calculated based on physical volumes (not rate) only for goods subject to excise tax. The rates of the excise tax are provisioned by Article 88 of the TC.

For two types of activities, which are:

a. Organization of inter-regional, intra-regional & intra-city route operation or direct passenger transportation by light car,
and

b. The above taxation regimes do not apply to food trade through coin-operated and (or) banknote vending machines, as well as to the organization of games (other than gambling and casino activities) using coin-operated vending machines. Instead, a state duty is levied at rates under the RA Law on State Duties (Articles 19.7 & 19.8).

Other mandatory taxes (environmental tax, road tax, real estate tax, property tax, nature use fee, social payment, local payment, etc.) do not depend on the type of legal organization and tax regime but are calculated based on a specific transaction.



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RESEARCH PAPER

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