Non-Official Translation

IN THE NAME OF THE REPUBLIC OF ARMENIA

DECISION OF THE CONSTITUTIONAL COURT OF

THE REPUBLIC OF ARMENIA

ON THE CASE OF CONFORMITY OF SUB-CLAUSE "A" OF CLAUSE 11 OF PART 4 OF ARTICLE 109 AND SUB-CLAUSE "B" OF CLAUSE 2 OF PART 1 OF ARTICLE 123 OF THE TAX CODE OF THE REPUBLIC OF ARMENIA AND SUB-CLAUSE 2 OF CLAUSE 3 AND SUB-CLAUSE 2 OF CLAUSE 15 OF THE PROCEEDING PRESCRIBED BY N 1 ANNEX APPROVED BY THE DECISION N 1373–N OF THE RA GOVERNMENT OF 5 OCTOBER 2017 WITH THE CONSTITUTION OF THE REPUBLIC OF ARMENIA ON THE BASIS OF THE APPLICATION OF THE HUMAN RIGHTS DEFENDER

Yerevan November 27, 2018

The Constitutional Court composed of H. Tovmasyan (Chairman), A. Gyulumyan, A. Dilanyan, F. Tokhyan, A. Tunyan, A. Khachatryan (Rapporteur), H. Nazaryan, A. Petrosyan,

with the participation (in the framework of the written procedure):

the applicant: A. Tatoyan, Human Rights Defender,

parties engaged as respondents in the case: the National Assembly of the Republic of Armenia and the Government of the Republic of Armenia,

pursuant to Clause 1 of Article 168, Clause 10 of Part 1 of Article 169 of the Constitution, Part 1 of Article 23, Article 35 and Article 68 of the Constitutional Law on the Constitutional Court,

examined in a public hearing by a written procedure the case on conformity of Sub-clause "a" of Clause 11 of Part 4 of Article 109 and Sub-clause "b" of Clause 2 of Part 1 of Article 123 of the Tax Code of the Republic of Armenia and Sub-clause 2 of Clause 3 and Sub-clause 2 of Clause 15 of the Proceeding prescribed by N 1 Annex approved by the Decision N 1373–N of the RA Government of 5 October 2017 with the Constitution of the Republic of Armenia on the basis of the application of the Human Rights Defender.

Tax Code of the Republic of Armenia (hereinafter referred to as the Code) was adopted by the National Assembly on 4 October 2016, signed by the President of the Republic on 1 November 2016, and entered into force on 1 January 2018.

Sub-clause "a" of Clause 11 of Part 4 of Article 109 of the Code, titled **"Peculiarities of record-keeping of certain types of income"** prescribes:

"For the purpose of determination of profit tax base, the following shall also be considered as income for profit taxpayers:

(…)

11) by profit taxpayers (except for cases prescribed by Clause 12 of this Part), in accordance with the procedure established by the Government:

a. cancelled amounts of payables to be cancelled for taxation purposes …".

The above-mentioned provision of the Code was amended by the Law HO-266-N adopted by the National Assembly on December 21, 2017, according to which: the word "uncollectible" prescribed in Sub-clause "a" of Clause 11 was replaced by the words "to be cancelled for taxation purposes".

Sub-clause "b" of Clause 2 of Part 1 of Article 123 of the Code, titled **"Other deductions"** prescribes:

"1. For the purpose of determination of the tax base for resident profit taxpayers, as well as non-resident profit taxpayers carrying out activities in the Republic of Armenia through a permanent establishment, the following shall be deducted from the gross income:

(…)

2) by profit taxpayers (except for cases prescribed by Clause 3 of this Part), in accordance with the procedure established by the Government:

(…)

b. in the case of cancelling uncollectible receivables - the amounts exceeding the deductions made to the reserve established for that purpose …".

The above-mentioned provision of the Code has not been amended.

The Decision N 1373-N "On approval of the procedure for creating a reserve (reserve fund) of possible losses of receivables of income taxpayers (with the exception of banks, credit institutions, insurance companies and specialists of the securities market), recognition of receivables and payables as uncollectible, their cancellation, and on declaring invalid the Decision N 2052-N of the Government of the Republic of Armenia dated December 19, 2002" (hereinafter - the Decision) was adopted by the Government on 5 October 2017, signed by the Prime Minister on 3 November 2017 and entered into force on 1 January 2018.

Sub-clause 2 of Clause 3 of the Proceeding prescribed by N 1 Annex approved by the mentioned Decision stipulates:

"3. In the aspect of the application of this Proceeding:

…

2) payables (including those under wages, other equivalent payments and dividends) is the amount of debt payable (reimbursed in another form) to other persons (creditors) by the taxpayer".

Sub-clause 2 of Clause 15 of the Proceeding prescribed by the given Annex stipulates:

"15. Receivables established by Sub-clause 1 of Clause 3 of this Proceeding shall be considered uncollectible:

…

2) from the date of entry into force of the judicial act (judgment, decision or order, with the exception of a judgment, decision or order issued concerning the forgiveness of the amount of receivables or the refusal to claim it on any basis) to satisfy the claim for the recovery of receivables or refusal to meet this requirement, if the total amount of debt of the certain debtor exceeds 100 thousand AMD ...".

The above-mentioned provisions have not been amended.

The case was initiated on the basis of the application of the Human Rights Defender submitted to the Constitutional Court on 6 January 2018.

Having examined the application, the written explanation of the applicant and the respondent, as well as having analyzed the relevant provisions of the Code, the Decision N 1373-N of the Government of 5 October 2017, other norms of the legislation interrelated with the latter, and other documents of the case, the Constitutional Court **ESTABLISHES:**

1. Positions of the applicant

The applicant considered the raised constitutional legal dispute from the perspective of legal certainty and the possibility of restricting the right to property solely on the basis of law.

The main question of the applicant in the aspect of legal certainty is that the legislator, using the terms "payables" and "uncollectible payables", did not disclose their content in the Code. The definition of the aforementioned terms is nevertheless given in the Decision, however, according to the applicant, this definition "goes beyond the scope of the subject of regulation delegated by the Code".

According to the applicant, the problem is that according to the definition in the Decision, the amount of debt payable (reimbursed in another form) by the organization to other persons (creditors) under the dividends is also considered as payables. However, the amount of dividends, payable in accordance with Clause 1 of Part 1 of Article 112 of the Code, is not considered as an expenditure element, and therefore has no influence on the determination of taxable income. The result is that, without

considering this amount in the Code as an expense, which has no influence on the process of determining taxable income, in the case of an interpretation given to it in the Decision, it can be considered as uncollectible payables and taxed. The applicant believes that in this situation this raises an issue of legal certainty, and in this regard the applicant refers to legal positions expressed in the decisions of both the Constitutional Court and the European Court of Human Rights, on the basis of which the applicant concluded that the restriction of the right to property on the basis of law is out of the question, if this law does not comply with the rules of legal certainty, and the person is not capable to behave in accordance with the requirements of the law.

Another issue raised by the applicant concerns the possibility of restricting the right to property solely on the basis of law, which, according to the applicant, is violated in this situation. In particular, Sub-clause "b" of Clause 2 of Part 1 of Article 123 of the Code establishes the range of issues that should be regulated by the Government Decision. According to this Article, the Government should establish a procedure for reducing gross income in the amount of deductions made to the reserve fund, and in the case of cancellation of these debts - in the amount exceeding the deductions made to the reserve fund created for this purpose. In view of the above, the applicant believes that the Government is not empowered to establish when receivables should be recognized as uncollectible, that is, the procedure for the implementation of the right should be established, although the law enforcement practice of the tax authority shows that the Government has actually established this procedure. According to the applicant, in accordance with Clause 1 of the Proceeding prescribed by the Decision, the said Proceeding shall regulate relations in connection with the formation of a reserve of possible losses of receivables, recognition of receivables and payables as uncollectible, and cancelling them when determining taxable income. It turns out that the Government has gone beyond the powers granted to it by the law because of the absence of the concept of "uncollectible receivables" at the level of the law.

Considering the raised issue in the scope of Article 60 of the Constitution, the applicant considers it necessary to establish whether the interference with the right to property is proportionate within the framework of the law and the Decision of the Government, and whether a fair balance between public and private interests is observed.

Presenting the legal positions of the Constitutional Court and the European Court of Human Rights, the applicant concludes that in cases where the duty to pay taxes is not established by law, an illegitimate interference with the implementation of the right to property of the person occurs.

The applicant expressed concerns on the provisions challenged in the present case is due to the fact that the Code does not stipulate the concept of "receivables", and, for recognizing the receivables as uncollectible, the Decision imposes an obligation on an economic entity to have a relevant court judgment on the recovery of the amount of receivables in part of the amount exceeding 100 thousand AMD. The applicant believes that the requirement on the recovery, stipulated by the Decision, does not explicitly ensure the balance between the public and private interests. In support of his position, the applicant also presents the study of international experience (Georgia, Russia, and Latvia) on the subject of the dispute.

Summarizing his reasoning, the applicant concludes that the challenged provisions contradict Part 2 of Article 6, Article 39, Parts 1, 3 and 8 of Article 60 and Article 79 of the Constitution, insofar as the concepts of "payables" and "receivables" are disclosed not in the law but in the Government Decision (which does not follow from the law), thereby leading to interference with the right to property in a manner not prescribed by law.

2. Positions of the respondent

2.1. The National Assembly, engaged as a respondent in the present case, considers that the legal regulations, following from the content of the challenged provisions, contain a legal gap that created legal uncertainty for the law enforcer.

Proceeding from the necessity of fully-fledged implementation of the regulations stipulated in the challenged provisions, as well as the requirements of the Constitution, resulting from a systematic and comprehensive analysis of the relevant legal regulations following from the provisions of the present constitutional legal dispute, according to which a person shall not bear responsibilities which are not prescribed by the law and must pay taxes and duties only prescribed in law, the respondent believes that the Code contains a legal gap, and accordingly an uncertainty resulting from the definitions of the concepts contained in the Annex to the Decision, which, due to diverse interpretations and in terms of the absence of a tax obligation, can jeopardize the fulfilment of the tax obligations in respect to the value added tax and the income tax prescribed by constitutional legal norms.

The respondent substantiates the above judgments referring to the legal positions of the Constitutional Court and the European Court of Human Rights regarding the legal gap and legal certainty.

Summarizing the findings, the respondent concluded that the existing legislative gap in terms of the principle of legal certainty within this constitutional legal dispute jeopardizes the proper implementation of the right of a person to act freely and the right to property stipulated by Articles 39 and 60 of the Constitution, thus creating the possibility of violation of the mentioned constitutional rights, which cannot be resolved by other legal guarantees prescribed by the legislation.

Based on the foregoing, the respondent considers that the challenged provisions of the Code contradict the requirements of the Constitution.

2.2. The Government, engaged as a respondent in the case, in the terms of the provisions of the Decision challenged in this case, considers that non-definition of the terms "receivables" and "payables" does not lead to diverse interpretations of these terms and limits their application in accordance with international standards. Therefore, the usage of the terms "receivables" and "payables" in the Decision is consistent with the Constitution, with the justification that they were borrowed from international accounting standards and, at the same time, they are well-known terms, hence their further reinforcement is simply due to the reasons of ensuring the principle of legal certainty.

Referring to the position of the applicant, according to which the concepts of “payables” and “uncollectible receivables” are applied within the context of the Government Decision, the respondent argues that such a regulation is legitimate due to the following reasoning.

According to Clause 11 of Part 4 of Article 109 of the Code, the Government is empowered to establish a procedure for cancellation of payables subjected to cancelation for taxation purposes. Therefore, for the establishment by the respective Government decision of the procedure for cancellation of uncollectible payables, first of all, it is necessary for the Government to define the concept of “payables”, then also to establish cases where payables are considered as uncollectible, otherwise, in the legal aspect, it will be impossible to specify which relations are generally considered as the subject of regulation of the procedure established by the Government. In this aspect, based on the principle of legal certainty, in the Proceeding prescribed by N 1 Annex approved by the Decision, firstly, the definition of “payables” is stipulated, then the cases when payables are considered as uncollectible are prescribed, as relationships that are regulated by the above-mentioned Proceeding.

Referring to the position of the applicant, according to which the Government is empowered to establish the procedure for reducing the gross income from deductions made to the reserve fund for cancelling uncollectible receivables, and in the case of cancelling these debts, the amounts exceeding the deductions made to the reserve created for this purpose, the respondent believes that it does not follow from the provisions of Section 6 of the Code, since according to the Code, Government is empowered to establish both the procedure for making deductions to the reserve and the procedure for recognition of receivables as uncollectible.

At the same time, the entire procedure for cancelling receivables has been approved by the Decision, and the recognition of receivables as uncollectible is one of the stages of the procedure. In this aspect, the respondent believes that the provision of appropriate conditions for recognizing the receivables as uncollectible - in particular the existence of a relevant court judgment on the recovery of the amount of receivables for recognizing the receivables exceeding 100 thousand AMD as uncollectible - does not contradict the constitutionally stipulated provision on the restriction of the right to property solely on the basis of law, and this does not violate the principle of inviolability of the right to property.

Summarizing his judgments, the respondent believes that the dispute regarding the unconstitutionality of the provisions at issue is unreasonable.

3. Circumstances to be clarified within the framework of the case

The legal dispute in the framework of the present case concerns the constitutionality of the authorizing norms of the law and, on the basis of the latter, the establishment by the Government Decision of the concepts of “payables and receivables” and their contents, as well as the procedure for recognizing the receivables as uncollectible.

In assessing the constitutionality of the challenged norms, the Constitutional Court considers it necessary to clarify the following questions:

a) Do the legal regulations established by the challenged provisions of the Code comply with the principle of legal certainty?

b) Are the constitutional requirements for restrictions on the right to property followed under the legal regulations stipulated by the challenged provisions of the Code?

c) Is the Government authorized by the Constitution to make such regulations as the challenged provisions of the Decision?

4. Legal analysis and positions of the Constitutional Court

4.1. The provision prescribed in Sub-clause "a" of Clause 11 of Part 4 of Article 109 of the Code challenged by the applicant concerns the peculiarities of record-keeping of certain types of income when determining the profit tax base. This provision, inter alia, establishes that, for the purpose of determination of profit tax base, the amounts of payables to be cancelled for taxation purposes that were cancelled by profit taxpayers shall also be considered as income for profit taxpayers, in accordance with the procedure established by the Government.

Within the framework of the logic of the challenged provision, the Constitutional Court considers it necessary to refer to the analysis of the legal regulations on profit taxation envisaged in Chapter 22 of the Code, titled: "Object to be taxed under profit tax, tax base and tax rate".

Thus, Part 1 of Article 104 of the Code, titled: "Object to be taxed under profit tax", establishes that objects to be taxed under profit tax shall be for resident organisations, individual entrepreneurs record-registered in the Republic of Armenia and notaries - gross income derived or to be derived from sources of and/or outside the Republic of Armenia, except for personal income of individual entrepreneurs registered in the Republic of Armenia and notaries. Profit tax base shall be, inter alia, for resident profit taxpayers - taxable profit, which is determined as a positive difference of the gross income prescribed by Clause 1 of Part 1 of Article 104 of the Code and deductions prescribed by Article 110 of the Code (Clause 1 of Part 1 of Article 105 of the Code).

At the same time, Clause 27 of Part 1 of Article 4 of the same Code, titled: "Main concepts used in the Code", also prescribes the notion of gross income, namely, "the sum total of the incomes prescribed by the Code, received or to be received during the reporting period". The same Article establishes that entrepreneurial income, personal income and/or passive income are also considered as income. The Code also establishes the principles of determination of profit tax base, which are as follows: "When determining the profit tax base: 1) accounting shall be conducted based on the principles and rules prescribed by laws and other legal acts regulating accounting and the drawing up of financial statements, unless peculiarities of the application thereof are prescribed by this Section of the Code and the general part of the Code ..." (Clause 1 of Part 1 of Article 106 of the Code).

As for the specifics of accounting, Part 1 of Article 15 of the Code establishes that taxes or fees for the use of natural resources shall be calculated by the accrual basis accounting method unless the Code

provides that the taxes or fees for the use of natural resources shall be calculated by cash basis accounting method. According to Clause 1 of Part 1 of the same Article, "For the purposes of the Code: 1) accrual basis accounting method shall mean that: a. a taxpayer keeps records of the income and expenses from the moment of obtaining the right to receive the income or from the moment of recognizing the expenses, irrespective of the time of receiving compensation or making a payment; b. a taxpayer keeps records of taxes, fees for the use of natural resources and the amounts offset (reduced) from taxes from the moment of arising of tax liability or generation of the amounts offset (reduced) from taxes, irrespective of the moment of receiving compensation for the transactions effected by him or her or making fees to the suppliers or tax or customs authorities with regard to the offset (reduced) amounts ... ".

Based on the systems analysis of the above provisions and other related norms, the Constitutional Court states that for profit taxpayers the taxable profit is the positive difference of the gross income and deductions, and in the case when entrepreneurial costs, loses and other deductions are deducted from gross income, and income and expenses are taken into account when determining taxable income, then the "items not considered as income" and the "items not considered as expenses" are not record-kept and are not reflected in profit tax calculation reports submitted to the tax authority.

4.2. By virtue of Article 1 of the Constitution, the Republic of Armenia is proclaimed as a rule of law State, which per se also implies the existence of a law consonant with the principle of legal certainty. At the same time, Part 2 of Article 6 of the Constitution, titled: "The Principle of Legality", in particular, establishes that the bodies foreseen by the Constitution, based on the Constitution and laws and with the purpose of ensuring their implementation, may be authorized by the law to adopt sub-legislative normative legal acts.

Article 79 of the Constitution, titled: "The Principle of Certainty", states: "In case of restriction of fundamental rights and freedoms, the laws shall define the grounds and scope of restrictions and be sufficiently certain to enable the holders of such rights and freedoms and the addressees to regulate their behavior accordingly".

In connection with the significance of the aforementioned constitutional principles, the Constitutional Court deems it necessary to consider the challenged provisions primarily in the context of the said principles.

In a number of decisions, the Constitutional Court referred to the principle of legal certainty, in particular noting that:

- "... the law must also comply with the legal position expressed in a number of judgments of the European Court of Human Rights, according to which no legal norm can be considered as "law" unless it does not comply with the principle of legal certainty (res judicata), i.e. it is not formulated with sufficient precision to enable the citizen to regulate his or her behavior accordingly." (DCC-630);

- “The principle of the rule of law State, inter alia, requires the existence of a legal law. The latter should be sufficiently accessible, i.e. in certain circumstances the legal entities should be able to get oriented, which legal norms in a certain case are applied. The norm cannot be considered as “law” unless it is not formulated with sufficient accuracy to enable natural persons and legal entities to behave accordingly, and they should be able to foresee the consequences that may arise from this action.” (DCC-753);

- “... from the perspective of ensuring legal certainty, the concepts used in the legislation should be certain, definite and should not lead to diverse interpretations and confusion ...” (DCC-1176);

- “The legal regulations enshrined in the law, especially in the framework of the recognition of the principle of the rule of law, should make the legitimate expectations of the person foreseeable. In addition, as one of the fundamental principles of the rule of law State, the principle of legal certainty also implies that the actions of all subjects of legal relations, including the holder of power, must be foreseeable and lawful.” (DCC-1213);

- “Judicial interpretation is not excluded even in the case when the legal norm is the most precisely formulated. The need for clarification of legal provisions and bringing them in line with changing circumstances, i.e. evolving social relations, always exists. Consequently, the certainty and accuracy of legislative regulation cannot be absolutized, and even insufficient preciseness can be complemented by court interpretations.”(DCC-1270);

- “... the principle of legal certainty also implies the certainty and foreseeability of court decisions, which provides the participants of legal relations an overview of the possible consequences of their behavior” (DCC-1270).

The European Court of Human Rights has also expressed a number of positions on legal certainty, in particular, in the Judgment of Busuek v. Moldova (Case of Busuioc v. Moldova, application no. 61513/00, 21/12/2004), the Court found that one of the requirements flowing from the expression “prescribed by law” is the foreseeability of the measure concerned. A norm cannot be regarded as a “law” unless it is formulated with sufficient precision to enable the person to behave accordingly: he or she must be able to foresee, to a degree that is reasonable in the circumstances, the consequences which a given action may entail. Those consequences need not be foreseeable with absolute certainty: experience shows this to be unattainable. Whilst certainty in the law is highly desirable, it may bring in its train excessive rigidity and the law must be able to keep pace with changing circumstances. Accordingly, many laws are inevitably couched in terms which, to a greater or lesser extent, are vague and whose interpretation and application are questions of practice.

At the same time, the European Court of Human Rights stated in another judgment that “...whilst certainty is highly desirable, it may bring in its train excessive rigidity and the law must be able to keep pace with changing circumstances. Accordingly, many laws are inevitably couched in terms which, to a greater or lesser extent, are vague and whose interpretation and application are questions of practice” (The Sunday Times v. the United Kingdom (Application no. 6538/74, 26/04/79, § 49).

In the context of the aforementioned positions, the Constitutional Court, regarding the provisions challenged in the present case, states the following:

The challenged provision of Sub-clause "a" of Clause 11 of Part 4 of Article 109 of the Code establishes that, for the purpose of determination of profit tax base, the amounts of payables to be cancelled for taxation purposes, that were cancelled by profit taxpayers, shall also be considered as income for profit taxpayers, in accordance with the procedure established by the Government. That is, by virtue of the provision in question, the amounts of payables to be cancelled for taxation purposes **shall be considered as income** for profit taxpayers, and these amounts are subject to taxation. It also follows from this provision that the legislator has authorized the Government to establish only **the procedure for cancelling** the amounts of payables to be cancelled for taxation purposes. It turns out that the provision in question establishes a tax liability for profit taxpayers, which implies the need for certain and acceptable wording of all the conditions relating to the imposition of this obligation. It follows that the challenged provision authorizes the Government to establish **the procedure for cancelling** the amounts of payables, but there can be no question of giving the Government any authority in disclosing the content of the term "payables".

Taking into account the requirements of the norm enshrined in the second sentence of Part 2 of Article 6 of the Constitution, i.e. the authorizing norms shall comply with the principle of legal certainty, as a result of consideration of the challenged norms prescribed in Sub-clause"a" of Clause 11 of Part 4 of Article 109 of the Code, the Constitutional Court considers that they are formulated with sufficient precision, and **on the basis of the challenged provision, the Government is authorized to establish exclusively the procedure for cancelling the amounts of payables.**

4.3. The positions of the Constitutional Court with respect to regulating tax relations exclusively by law are as follows:

Part 1 of Article 60 of the Constitution, titled: "The Right to Property", establishes that everyone shall have the right to own, use and dispose at his discretion the legally acquired property. Part 3 of the same Article establishes that the right to property may be restricted only by law with the aim of protecting the interests of the public or the fundamental rights and freedoms of others. And Part 8 stipulates that everyone shall be obliged to pay taxes, duties and make other compulsory payments to the State or community budget prescribed in accordance with law.

Subsequently, referring to the issue of restriction of the right to property, the Constitutional Court, in the Decision DCC-1340 of 31 January 2017, expressed the legal position that Part 3 of Article 60 of the Constitution establishes the possibility of restriction of the right to property, according to which this right may be limited only by law with the aim of protecting the interests of the public or the fundamental rights and freedoms of others, this restriction must comply with the constitutional principles of certainty and proportionality and may not exceed the limits established by the international agreements of the Republic of Armenia.

At the same time, in the same Decision the Constitutional Court emphasized the existence of the mentioned conditions for a lawful limitation of the right.

In a number of judgments, the European Court of Human Rights has also addressed the right to property, stating that Article 1 of Protocol No. 1 to the European Convention for the Protection of Human Rights and Fundamental Freedoms, by proclaiming the right to property, at the same time provides for the possibility of limitation of the right to property in the public interest, if the restriction is provided for by law and by general principles of international law, and for exercising control over the use of property in accordance with the general interests or ensuring the payment of taxes or other contributions or penalties. At the same time, the European Court of Human Rights stated that in any instance of interference with the right to peaceful enjoyment of property, this can be justified only in cases when it was carried out in the public interest. In connection with this rationale, the European Court of Human Rights stated that there must be a reasonable relationship of proportionality between the means employed and the aim sought to be realised in order the interference was considered as justified, i.e. **an interference must strike a fair balance between the demands of the general interests of the community and the requirements of the protection of the individual's fundamental rights** (Beyeler v. Italy, judgment of 5 January 2000, §98, §107; Sporrong and Lonnroth v. Sweden, judgment of 23 September 1982, §61, §69).

Within the framework of the logic of the mentioned positions, both the Constitution and the European Convention for the Protection of Human Rights and Fundamental Freedoms, together with the protection of the right to property, also envisage the duty to pay statutory taxes, duties and other mandatory payments. However, any restriction of the right to property, including the establishment of a tax, must be provided for by law and comply with the principle of legal certainty, and this restriction must pursue a legitimate aim and be fair and reasonable.

In this aspect, the constitutionality of the challenged provisions should be considered in the context of full disclosure of the content of the phrase **"taxes established in accordance with the law"**. So, it follows from the content of the provision "taxes established in accordance with the law" prescribed in the aforementioned constitutional regulations, that only the law may establish taxes and the elements constituting their content. **In the context of Article 6 of the Constitution, titled: "The Principle of Legality", with the purpose of ensuring the implementation of laws, the Government may adopt sub-legislative normative legal acts, but they cannot amend or supplement the content of the tax and the amount of tax liabilities, which means that any concept used in the Code and on the content of which the amount of tax liabilities also depends, must be set forth exclusively by law.**

According to Clause 1 of Part 1 of Article 4 of the Code, **tax** is a mandatory and non-repayable amount which is paid by taxpayers to the State and/or community budgets of the Republic of Armenia in the manner, amount and within the terms prescribed by the Code for the purpose of satisfying State and/or public needs. It follows from the content of Article 6 that taxes not prescribed by the same Code cannot be defined in the Republic of Armenia.

At the same time, Part 1 of Article 9 of the Code, titled: "General conditions for setting taxes and fees", states that "Taxes and fees shall be considered to be set only if the following elements have been set, except for cases prescribed by Part 3 of this Article:1) scope of taxpayers, 2) taxable object, 3) tax base, 4) tax rate, 5) method of calculation of the tax, 6) procedure and time limits for paying the tax".

According to Part 1 of Article 10 of the Code, titled: “Taxable object”, taxable object shall mean any transaction, **profit**, property, type of activity (including any action or function) or any other object the existence whereof or the existence of the right of ownership over which or the exercise of this right in accordance with the Code entails for the taxpayer the obligation of calculating or paying the tax.

The challenged provision of the Code stipulates that for profit taxpayers the amounts of payables are also considered as income, meanwhile, the Code does not disclose the content of the term “payables”. It turns out that payables are considered as income, and in order to consider the tax to be established, it is necessary that the law also prescribes the taxable object, in particular the income. Meanwhile, in this case, the content of the term “payables” is disclosed not in the Code, but in the Government Decision.

In the context of the aforementioned constitutional regulations and as a result of the analysis of the relevant provisions of the Code, it becomes clear that in order to consider the tax to be established, it is necessary, at the same time, to clearly establish by law the elements constituting its content, and the absence of at least one of these elements means that the tax is considered as non-established. That is, **in order to consider the tax to be established, these elements must be as precise that there is no need for their additional clarification or detailing, and in case of such need, such clarification also should be carried out by law, since the establishment of tax per se is carried out exclusively in accordance with the law.**

Hence, taking into account the above-mentioned, **the Constitutional Court states that in this case the expression “taxes established in accordance with the law” implies the establishment of both the tax and the elements** constituting its content **exclusively by law. In each certain case, the tax liability will be considered as established in accordance with the law, if it is established by law not only in a strictly formal aspect, but also the elements constituting its content are fully reflected in the law. Meanwhile, in this case, the content of the element considered as income is disclosed not in the Code, but in the Government Decision, which may cause interference, unforeseen by law, with the right to property of a person.**

This approach is also justified in the positions of the European Court of Human Rights, in particular, in the case of Lelas v. Croatia, 10.05.2010 the Court noted that in case the interference was not established by law, the proportionality is not a matter at issue and the violation of the right to property is established automatically.

Considering the above, the Constitutional Court considers that the limitation of the right to property in part of the payables, established by Sub-clause 2 of Clause 3 of the Proceeding prescribed by N 1 Annex approved by the mentioned Decision, the restriction of the right to property was carried out in accordance with the procedure prescribed by the Government Decision instead of the procedure prescribed by law, which leads to the establishment of tax liability in accordance with the sub-legislative legal act, but not the law.

Consequently, the Constitutional Court considers that there is an unlawful interference with the right to property without taking into account other conditions for limitation of the right to property.

At the same time, the Constitutional Court states that the provision stipulating the concept of "payables" prescribed in Sub-clause 1 of Clause 3 of the Decision is also systemically interrelated with the challenged provision, according to which: "In the aspect of the application of this Proceeding: 1) receivables is the amount of debt payable (reimbursed in another form) to the taxpayer by other persons (debtors)".

Based on Part 10 of Article 68 of the Constitutional Law on the Constitutional Court, the Constitutional Court considers that the above-mentioned positions are equally applicable to Sub-clause 1 of Clause 3 of the Proceeding prescribed by N 1 Annex approved by the Government Decision.

4.4. The next provision challenged by the applicant concerns other deductions from gross income for the purpose of determining the tax base for profit taxpayers. In particular, Sub-clause "b" of Clause 2 of Part 1 of Article 123 of the Code states that when determining taxable income, gross income shall be deducted by profit taxpayers (except for cases prescribed by Clause 3 of the same Part) in the case of cancelling uncollectible receivables, in accordance with the procedure established by the Government, and in the case of cancelling these debts - the amount exceeding the deductions made to the reserve established for that purpose.

This Article also establishes the scope of issues that should be regulated by the Government Decision. It turns out that the Government is not empowered to establish when receivables should be recognized as uncollectible, that is, the procedure for the implementation of the right should be established, although the law enforcement practice of the tax authority shows that the Government has actually established this procedure and in practice it is implemented in that sense, going beyond the scope of the powers granted by law.

As a result of consideration of the challenged provision in the context of the presented positions regarding legal certainty, the Constitutional Court states that it becomes clear from this provision who it is addressed to and what actions its addressees should take. Therefore, in the aspect of legal certainty, the provision regarding deductions from the gross income in order to determine the object to be taxed for profit taxpayers, Part 1 of Article 123 of the Code also does not raise the issue of constitutionality. The Decision, rendered on the basis of the above-mentioned provision, establishes the procedure for creating a reserve of possible losses of receivables of income taxpayers, recognition of receivables and payables as uncollectible, and their cancellation, in the framework of which not only the concept of receivables is disclosed, but also the cases are indicated when this debt becomes uncollectible. In this regard, Sub-clause 1 of Clause 3 of the Proceeding prescribed by N 1 Annex approved by the Decision establishes that receivables is the amount of debt payable (reimbursed in another form) to the taxpayer by other persons (debtors), and Clause 15 of the same Proceeding establishes that "... receivables shall be considered as uncollectible: 1) from the 366th day, as it became overdue, if the total amount of debt of the debtor does not exceed 100 thousand AMD; 2) from the date of entry into force of the judicial act (judgment, decision or order, with the exception of a judgment, decision or order issued concerning the forgiveness of the amount of receivables or the refusal to claim it on any basis) to satisfy the claim for the recovery of receivables or refusal to meet this requirement, if the total amount of debt of the certain debtor exceeds 100 thousand AMD; 3) in

cases of declaring the debtor insolvent (bankrupt) in accordance with the procedure established by the legislation of the Republic of Armenia or liquidating the debtor organization, or death of a debtor individual entrepreneur removed from state registration, or a debtor notary the activities whereof have been suspended, or a debtor natural person, regardless of the time period for debt repayment".

The positions of the applicant are based on the rationale that for recognizing the receivables as uncollectible, this regulation imposes an obligation on the taxpayer to have a court judgment to satisfy the claim for the recovery of receivables or refusal to meet this requirement in part of the amount exceeding 100 thousand AMD.

The Constitutional Court considers that the procedure for recognizing the receivables as uncollectible should also be established by law but not the Government Decision, since the object to be taxed also depends on the recognition of the receivables as uncollectible, therefore, the amount of tax liabilities of the person, which means that the conditions for recognizing the receivables as uncollectible should be established by law, and no other body provided for in the Constitution is competent to regulate the conditions for recognizing the receivables as uncollectible by a sub-legislative normative legal act having a lower legal force.

Consequently, the Constitutional Court considers that in part of Sub-clause 2 of Clause 15 of the Proceeding prescribed by N 1 Annex approved by the Decision, there is also an unlawful interference with the right to property without taking into account other conditions for limitation of the right to property.

Based on the review of the case and governed by Clause 1 of Article 168, Clause 10 of Part 1 of Article 169, Parts 1-4 of Article 170 of the Constitution, Articles 63, 64 and 68 of the Constitutional Law on the Constitutional Court, the Constitutional Court **HOLDS:**

1. Sub-clause "a" of Clause 11 of Part 4 of Article 109 of the Tax Code of the Republic of Armenia is in conformity with the Constitution.

2. Sub-clause "b" of Clause 2 of Part 1 of Article 123 of the Tax Code of the Republic of Armenia is in conformity with the Constitution.

3. To declare Sub-clause 2 of Clause 3 of the Proceeding prescribed by N 1 Annex approved by the Decision N 1373–N of the Government of the Republic of Armenia of 5 October 2017 contradicting Parts 3 and 8 of Article 60 of the Constitution and void.

4. To declare Sub-clause 1 systemically interrelated with Sub-clause 2 of Clause 3 of the Proceeding prescribed by N 1 Annex approved by the Decision N 1373–N of the Government of the Republic of Armenia of 5 October 2017 contradicting Parts 3 and 8 of Article 60 of the Constitution and void.

5. To declare Sub-clause 2 of Clause 15 of the Proceeding prescribed by N 1 Annex approved by the Decision N 1373–N of the Government of the Republic of Armenia of 5 October 2017 contradicting Parts 3 and 8 of Article 60 of the Constitution and void.

6. Based on the requirements of Part 3 of Article 170 of the Constitution, Clause 4 of Part 9 and Part 19 of Article 68 of the Constitutional Law on the Constitutional Court, and also bearing in mind the circumstance that the declaration of the challenged provisions referred to in Causes 3, 4 and 5 of the final part of this Decision as contradicting the Constitution will inevitably hinder the **determination of the object to be taxed under profit tax**, the declaration of Sub-clause 2 of Clause 3 of the Proceeding prescribed by N 1 Annex approved by the Decision N 1373–N of the RA Government of 5 October 2017, as well as Sub-clause 1 and Sub-clause 2 of Clause 15 systemically interrelated with the latter, as contradicting the Constitution and void upon the promulgation of the Decision of the Constitutional Court will inevitably create such serious consequences for the State or society, thereby violating the legal security established by repealing the current normative legal act, to define May 1, 2019 for the final invalidation of the provisions declared by this Decision as contradicting the Constitution, providing the National Assembly the possibility to reconcile the legal regulations of the Tax Code of the Republic of Armenia with the requirements of this Decision.

7. Pursuant to Part 2 of Article 170 of the Constitution this Decision shall be final and shall enter into force upon its promulgation.

Chairman **H. Tovmasyan**

November 27, 2018

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