

The Brief

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New Tax Code Adopted by the Ukrainian Parliament

This newsletter gives a brief overview of the most important points of the new Tax Code which was adopted by the Ukrainian Parliament on 2 December 2010, and signed into law by the President the next day. The Code will come into effect on 1 January 2011.

The text of the Code contains strong points, such as the reduction of the rate of or even exemption from some taxes for certain taxpayers, as well as sensitive points which are considered by some commentators either as disadvantageous in comparison with the current situation or as likely to lead to ambiguities.

The new Tax Code is the result of the political will to develop the Ukrainian economy and to introduce clear tax regulations. The Tax Code has been object of comments and suggestions made by international organisations such as the IMF and many other lobbying institutions which took part into the discussions prior to the Code's adoption. It should be noted that the corporate profits tax will be reduced by 2% in 2011 following the advice of the IMF instead of by 6% as was originally suggested in the first draft of the Code.

It should be stressed that the Code has strong political and social ramifications, as evidenced in the protests by SME (small and medium enterprises) representatives outside Parliament due to fears about deteriorations in their fiscal situation. As a result, the entire Chapter introducing a new, by far less favourable, simplified taxation system was dropped from the final draft of the New Tax Code. Therefore, the existing simplified taxation and accounting system is here to stay for the time being. However, the President stressed that a new version of Section 1 of Chapter XIV regulating the simplified taxation system will be adopted in the foreseeable future.



Gide Loyrette Nouel

Algiers
Tel. +213 (0)21 23 94 94
gln.algiers@gide.com

Beijing
Tel. +86 10 6597 4511
gln.beijing@gide.com

Belgrade
Tel. +381 (0)11 30 24 900
gln.belgrade@gide.com

Brussels
Tel. +32 (0)2 231 11 40
gln.brussels@gide.com

Bucharest
Tel. +40 21 223 03 10
gln.bucharest@gide.com

Budapest
Tel. +36 1 411 74 00
gln.budapest@gide.com

Casablanca
Tel. +212 (0)5 22 27 46 28
gln.casablanca@gide.com

Hanoi
Tel. +84 4 3946 2350
gln.hanoi@gide.com

Ho Chi Minh City
Tel. +84 8 3823 8599
gln.hcmc@gide.com

Hong Kong
Tel. +852 2536 9110
gln.hongkong@gide.com

Istanbul
Tel. +90 212 385 04 00
gln.istanbul@gide.com

Kyiv
Tel. +380 44 206 0980
gln.kyiv@gide.com

London
Tel. +44 (0)20 7382 5500
gln.london@gide.com

Moscow
Tel. +7 495 258 31 00
gln.moscow@gide.com

New York
Tel. +1 212 403 6700
gln.newyork@gide.com

Paris
Tel. +33 (0)1 40 75 60 00
info@gide.com

Prague
Tel. +420 222 871 111
gln.prague@gide.com

Saint Petersburg
Tel. +7 812 303 6900
gln.saintpetersburg@gide.com

Shanghai
Tel. +86 21 5306 8899
gln.shanghai@gide.com

Tunis
Tel. +216 71 891 993
gln.tunis@gide.com

Warsaw
Tel. +48 (0)22 344 00 00
gln.warsaw@gide.com



STRONG POINTS

The following strong points of the new Code should be highlighted:

- A political will to reduce some tax rates;
- Banning the practice of tax authorities refusing to accept documents related to tax return;
- The possibility for each legal entity to ask the tax authorities for written or oral opinions. The opinion is valid for a specific case; a legal entity cannot be sanctioned if it acts in compliance with such an opinion.

Decreases in tax rates

Corporate profits tax (CPT)

- (a) The CPT rate will be decreased progressively from 25% to 16% as follows:
- 23% from 1 April 2011
 - 21% from 1 January 2012
 - 19% from 1 January 2013
 - 16% from 1 January 2014
- (b) From 1 April 2011 to 1 January 2016 a 0% CPT rate will be applied to the following SMEs:
- Existing legal entities which, during the three preceding years, had an annual turnover of less than UAH 3 million UAH and which employed at least 20 persons.
 - Legal entities which satisfy the same criteria (turnover of less than UAH 3 million and at least 20 employees) and which are created after 1 April 2011, except those legal entities which are created through reorganisation, privatisation or purchase.
 - Legal entities – payers of a single tax with annual turnover not exceeding UAH 1 million and employing not more than 50 persons.
- (c) During the ten year period, starting from the 1 January 2011, the following legal entities will benefit from the 0% CPT rate:
- 3, 4, and 5 star hotels;
 - legal entities in the sphere of light industry;
 - ship and aircraft manufacturers.
- (d) Legal entities specialising in the field of alternative energies will benefit from an 80% exemption of the CPT during ten years starting from 1 January 2011.
- (e) Humanitarian aid will be totally exempt from the CPT.
- (f) Total exemption of financial aid given by a mother company and which should be repaid over 12 months.

Value added tax (VAT)

The following points related to VAT should be highlighted:

- (a) The tax rate is reduced from 20% to 17% with effect from 1 January 2014. A 20% rate will be applicable from 2011 to 2013.
- (b) A legal entity must be registered as a VAT payer if the aggregate amount from transactions relating to supply of goods/services, which are subject to VAT, accrued (paid) to such person during the last 12 calendar months exceeds UAH 300,000 (excluding the value added tax).
- (c) A legal entity may ask to be registered as a VAT payer if at least 50% of the goods or services produced are supplied to persons who are VAT payers.



- (d) VAT is applied to a transfer price which should not be less than the market price.
- (e) Reorganisation of legal entities will not lead to VAT consequences.
- (f) In order to report VAT credit, VAT invoices can be included in VAT input only within 12 months from the date of their issuance.
- (g) The validity of VAT invoices is subject to their registration by the seller/supplier into the Unified Register of VAT invoices. This obligation is introduced gradually as follows:
 - VAT invoices of more than UAH 1 million shall be registered from 1 January 2011;
 - VAT invoices of more than UAH 500,000- from 1 April 2011;
 - VAT invoices of more than UAH 100,000- from 1 July 2011;
 - VAT invoices of more than UAH 10, 000- from 1 January 2012.
- (h) In order to benefit from a VAT refund, the person should be registered as a VAT taxpayer at least 12 months prior to the reimbursement date.
- (i) An automatic VAT refund procedure is introduced in respect of some eligible taxpayers.

Personal income tax

- (a) The Code introduces a new term of "tax resident" applicable to foreign persons in such cases:
 - If they receive a permanent residence permit;
 - If they receive a working permit;
 - If they spend at least 183 days in Ukraine within a calendar year;
 - If they register as private entrepreneurs.
- (b) Residents and non-residents are taxed at 15%. However, income above ten minimum monthly wages (currently UAH 9,220) is taxed at 17%.
- (c) Income from the sale of one object of immovable property per year is exempt from tax.
- (d) Income from the sale of one car or motorbike per year is exempt from tax.

Decrease in fine rates

It should be noted that the Code foresees a symbolic amount of the UAH 1 fine applicable from 1 January to 30 June 2011 for the breach of its provisions. However, there remain criminal and administrative sanctions.

We can conclude from the general decrease in fine rates that the minimal fine rate does not exceed a 75% rate instead of a 200% rate which existed before the new Code. Sanctions for a breach of tax rules can be applied during 1,095 days (i.e. 3 years) after a deadline for a tax return submission.

- (a) The fine rates vary between UAH 85 and 1700. The amounts add up in cases of two or more violations.
- (b) In cases when a taxpayer himself corrects the mistakes concerning taxes related to previous fiscal periods, the fine rates will be as follows:
 - 3% of a tax amount if the mistake is corrected before the tax authorities are notified about the mistake;
 - 5% of a tax amount if the mistake is declared in the tax return.
- (c) It is important to note that the fine cannot be applied if the tax return is corrected before the deadline for tax returns.
- (d) A fine which amounts to 25% of non-paid taxes is applied to individuals who falsified the information in a tax return or in the event of non-submission of a tax return.



- (e) As to legal entities, in cases in which the exact amount of non-paid tax is determined during a tax audit, the Code foresees the fine rates as follows:
- 25% of non-paid taxes;
 - 50% of non-paid taxes if the breach has been discovered for the second time during the three-year period ;
 - 75% of non-paid taxes if the breach has been discovered for the third time during the three-year period.

A single taxpayer is subject to a fine which amounts to 50% of non-paid taxes.

SENSITIVE POINTS

The Tax Code evokes some pre-existing problems in Ukraine but without putting forward any remedies. Examples include the deduction of corporate expenses such as business trip expenses or taxi fares.

The problems of deducting corporate expenses in Ukraine

The following may not be included into expenses in accordance with The Tax Code:

- (a) Royalties accrued in favour of non-resident entities (save for accruals in favour of their permanent establishment taxed in Ukraine, accruals made by business entities in the field of television and radio-broadcasting pursuant to the Law of Ukraine On Television and Radio-Broadcasting, and accruals for granting of rights to use copyrights and neighbouring rights to foreign cinematic films, musical and literary works) when any of the five conditions set out below has been met:
- The amount exceeding 4% of the income from the sale of goods, works, services;
 - A non-resident entity has offshore status taking into account provisions of clause 161.3 of the Code;
 - A non-resident entity is not a beneficial recipient of such payments, except in instances when the beneficiary authorises other persons to receive such remuneration;
 - The royalties are paid for objects, with respect to which the intellectual property rights initially arose with a resident of Ukraine;
 - The person, in whose favour the royalties are accrued, is not subject to taxation with regards thereto in the jurisdiction of his residency.
- (b) Expenses for consulting, marketing, or advertising services realised by non-resident entities (save for expenses made in favour of permanent establishments of non-residents entities which are taxed in Ukraine) when any of two conditions below has been met:
- The amount exceeding 4% of the income from the sale of goods, works, services of the previous year;
 - A non-resident entity has offshore status taking into account provisions of clause 161.3 of the Code;
- (c) Expenses for engineering services realised by non-residents entities shall not be included in expenses when any of three conditions below has been met:
- The amount exceeding 5% of the customs value of the equipment imported under the respective contract;
 - A non-resident entity has offshore status taking into account provisions of clause 161.3 of the Code;
 - A non-resident entity is not a beneficial recipient of such payment for services.
- (d) The amount of prepayment for the goods, works or services may not be included in expenses.



- (e) The amount of payment for the goods, works, services furnished by the simplified taxpayers, except for purchase of IT services.
- (f) The land is not subject to depreciation taking into account provisions of clause 147.3 of the Code.
- (g) It is very important to note that the amount of payment for the goods, works and services furnished by simplified taxpayers (except for the purchase of IT services) is not included in expenses (clause 139.1.12 of the Code).

**Gide Loyrette Nouel**

56 A, Bohdana Khmelnytskoho Street
Kyiv 01030 - Ukraine
Tel. +380 44 206 0980
Fax +380 44 206 0987
E-mail: gln.kyiv@gide.com

Contact

Karl Hepp de Sevelinges
hds@gide.com

For further information:
www.gide.com

**Gide Loyrette Nouel**

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