

# Doing business and investing in Ukraine

2010 Edition



# Partner Letter



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Managing Partner

I am pleased to present you with the 2010 edition of our guide, *Doing Business and Investing in Ukraine*. The guide is based on laws as at 1 January 2010 and information available in early January-February 2010.

Ukraine, like many other countries in the region and around the globe today, is facing exceptional economic challenges. So far the country has weathered the storm rather well. Clearly its geographic position and natural resources and also the "human factor" are all playing a key role in this achievement. Ukraine's proximity to both the European Union and Russia, the sheer quantity of its consumers (46mln), and the physical size of the country make it an excellent location for businesses to expand both locally and

regionally. The 2012 UEFA European Football Championship is now formally on track and will stimulate interest in Ukraine and help in the development of infrastructure and the tourism industry. Today's low asset prices provide investors with excellent opportunities. However, the country's main asset is its extensive human capital: Ukraine's well educated workforce provides the competitive advantage, making the country a preferred investment destination, despite a still complex regulatory framework. Further reforms are needed to raise Ukraine to international business standards. The country has already adopted many principles familiar to EU-investors. Its accession to the WTO accelerates trade and puts another layer of protection on investments. It also should not be forgotten that Ukraine's tax rates are competitive.

Since 1993, PricewaterhouseCoopers has been advising companies and individuals on how to establish themselves in Ukraine. We draw on our significant experience in the local market, as well as the strength of our international network to help to build value, manage risk, and improve the performance of your business in Ukraine. Apart from our vast experience in serving multinational and blue chip companies, we have a particular focus on middle market and private clients, with dedicated teams serving these segments.

A brief guide such as this cannot answer all your questions. However, it will provide you with a valuable insight into the Ukrainian market, and make you better prepared to meet the challenges ahead.

We look forward hearing from you and having the opportunity to work with you in the future.

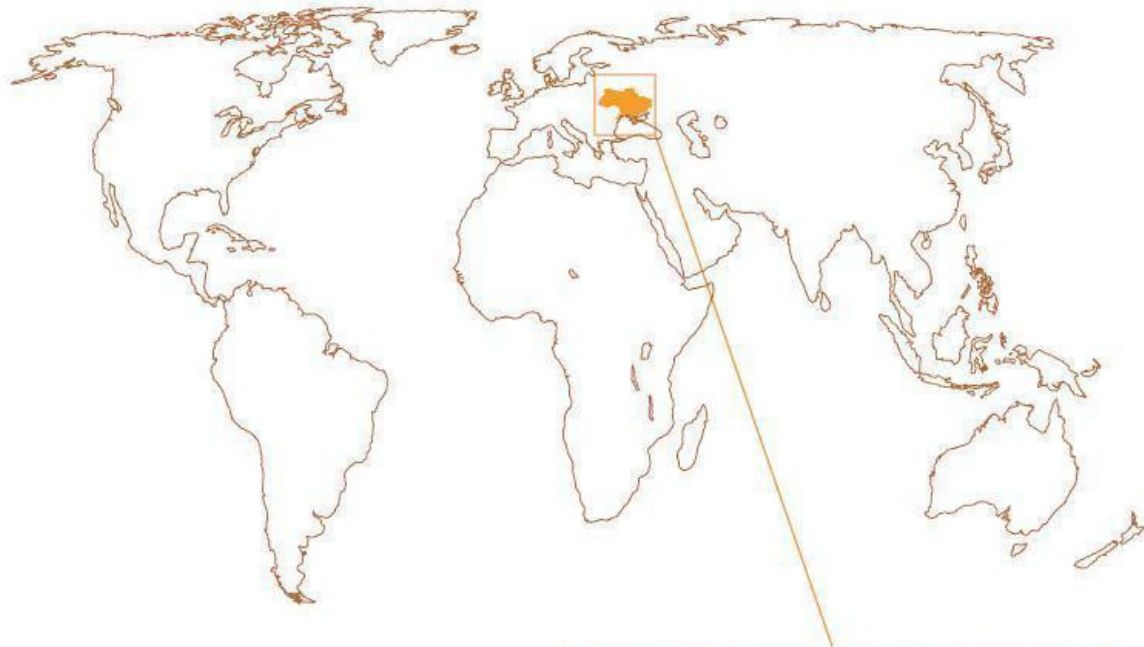
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# Office locations in Ukraine



The PricewaterhouseCoopers offices in Ukraine are located at the following addresses:

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Ukraine  
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Fax. [380] (62) 341 4690

## **3** Lviv office

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Lviv, 79015  
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For updated information, please check our website:  
[www.pwc.com/ua](http://www.pwc.com/ua)



# 1 Country profile and investment climate

## Investor considerations

- Ukraine's population is 45.7 million people, with a 5.7% reduction since 2001.
- The annualised real growth rate from 2000 to 2008 exceeded 7%.
- Severe recession in 2009 (15% GDP decline), but Ukraine's GDP is projected to grow by 2.5%-3% in 2010.
- In 2008, the IMF approved a USD 16.4 billion standby program to restore financial and economic stability in Ukraine.
- Hints for business visitors may be found in Appendix A.

## 1.1 Introduction

Ukraine, located in the heart of Eastern Europe, occupying a land area of 603,700 sq km, is the second largest country in Europe after Russia. It borders Poland, Slovakia, Hungary, Moldova and Romania to the west, Russia to the east, Belarus to the north and the Black Sea to the south.

Ukraine declared independence on 24 August 1991, following the dissolution of the Soviet Union. On 1 December 1991, 90.3% of those who voted approved a referendum formalizing independence from the Soviet

Union. The Union formally ceased to exist on 25 December 1991, at which time Ukraine's independence was recognized officially by the international community.

## 1.2 Government structure

The Head of State is the President. He is elected by popular vote for a five-year term. In February 2010 Victor Yanukovich was elected as the President.

Legislative power is exercised by a single-chamber Parliament, the Verkhovna Rada, which is comprised of

450 deputies and is elected every five years by party-list proportional representation. The last parliamentary elections were held in September 2007.

The highest Executive body is the Cabinet of Ministers. At the time of printing this report, the Prime Minister was Nikolay Azarov. The Prime Minister is appointed by the Parliament based on a submission from the President. The President nominates a candidate for the position of the Prime Minister on the suggestion of the parliamentary majority coalition. The Parliament appoints the members of the Cabinet of Ministers based on the nomination of the Prime Minister, except for the ministers of foreign affairs and defence, who are nominated by the President. There is an expectation that the Government will be stable for the next 2-3 years.

As Ukraine is transitioning from a presidential into a parliamentary republic, the "balance of power" between the President, the Parliament and the Cabinet of Ministers may change.

Administratively, Ukraine is composed of 24 regions and the Autonomous Republic of Crimea. The cities of Kyiv and Sevastopol also have a special legal status.

## 1.3 Legal system

Ukraine is a civil law country.

The Constitution, adopted in June 1996, sets out the structure of the national government, as well as its powers and functions. The powers of government are divided into three branches - legislative, executive and judicial.

Laws adopted by Parliament are forwarded to the President for signature. If the President signs the law, or fails to act within a 15-day period, the law is considered officially promulgated. The President has the right to veto legislation within the 15-day period, but the veto can be overcome by Parliament by a two-thirds majority.

The Constitutional Court of Ukraine is the sole organ of constitutional jurisdiction of Ukraine. The 18 judges are appointed for a one-time, nine-year term. The President, the Parliament, and the Congress of Ukrainian judges each appoint six judges. The judges select the Chief Judge from among themselves.

The court system in Ukraine has three branches:

- The general court system decides civil disputes and criminal cases, including cases filed by individuals that are not private entrepreneurs. The structure consists of local district courts, regional courts of appeal and

the Civil and Criminal Chambers of the Supreme Court of Ukraine.

- The commercial court system generally resolves business disputes between legal entities. It consists of local commercial courts (one in each region, plus Kyiv and Sevastopol), interregional courts of appeal, and the High Commercial Court.
- The administrative court system decides disputes involving state authorities. It consists of regional administrative courts (one in each region, plus Kyiv and Sevastopol), interregional courts of appeal, and the High Administrative Court.

The Supreme Court of Ukraine is the highest court, and has the power to review decisions of all three branches of the court system.

As an alternative to litigation, Ukraine allows for third party arbitration. Ukrainian law also allows foreign companies to include an arbitration clause in their contracts, including those with Ukrainian entities, which allow for arbitration by international arbitration institutions.

## 1.4 People

### Population

Ukraine's population was estimated at 45.7 million people at the end of 2009, which is 5.7% lower than the population disclosed in the 2001 census. Five cities have a population close to or exceeding one million people, including Kyiv with 2.7 million people.

Ukraine does not support dual citizenship. It is estimated that Ukrainian nationals make up 78% of the population, while Russian nationals account for 17%. More than two-thirds of the population live in urban areas. Females constitute 54% of the population.

### Religion

The majority of the population are members of one of the branches of the Orthodox Church. National holidays include Christmas (January 7), Easter and Holy Trinity Day. Around 8% of the population are Catholic, while 4% are Muslim, concentrated mainly in the Autonomous Republic of Crimea.

### Language

The official language is Ukrainian, although a majority of the population is bilingual, speaking both Ukrainian and Russian fluently. English is also used in business, although

not extensively. Many government websites have an English version (see Appendix B).

## Living standards

Per capita income has been rising, but average wages remain comparatively low. The official average monthly salary for employees in Ukraine was UAH 1,861 (USD 241) in 2009. Average salaries in Kyiv were 66% higher than average salaries in the rest of the country. It is worth underlining that some companies continue the practice of paying salaries 'in envelopes' and, therefore, official numbers may underestimate the actual level of personal income.

Despite these statistics, Ukraine has developed an affluent middle class. Minimum rents in Kyiv were in excess of USD 400 per month before the onset of the crisis in 2008. Ukraine has been one of the fastest-growing passenger car markets in Europe through the last half of 2000's, but the market collapsed in 2009. Restaurant prices in Kyiv are approaching, if not exceeding, those of major European cities.

Ukraine has a sizeable unofficial (hidden) economy. The Ministry of Economy in 2009 estimated the size to be at least 36% of GDP, while many analysts suggest that the true level is significantly higher.

## Unemployment

The official unemployment rate at the end of 2009 was 6.9%.

## 1.5 Economy

The Ukrainian economy grew at an annualised rate exceeding 7% from 2000 to 2008. However, in the fall of 2008, the global economic crisis exposed Ukraine's macroeconomic vulnerabilities, resulting in a contraction of industrial production, devaluation of national currency, and a severe credit crunch. GDP growth was 2.4% in 2008 and actual GDP was UAH 950 billion (USD 180 billion). In 2009

GDP contracted by approximately 15%, but it is forecasted to grow by 3% in 2010.

At the end of 2008, the International Monetary Fund approved a two-year stand-by program for SDR 11 billion (about USD 16.4 billion) to help the Ukrainian authorities restore financial and economic stability. By the end of 2009, Ukraine had received 3 tranches totalling USD 10.6 billion.

## Transport

Ukraine has a well-developed transport infrastructure, and is readily accessible by land or air. Ukraine has a railway network of 22,000 kilometres, and 169,400 kilometres of highways; 16 airports are open to commercial air traffic. Most international flights go to Boryspil International Airport, about 40km southeast of Kyiv, although limited international airports also operate in Dnipropetrovsk, Donetsk, Ivano-Frankivsk, Kharkiv, Lviv, Odesa and Simferopol.

## Communications

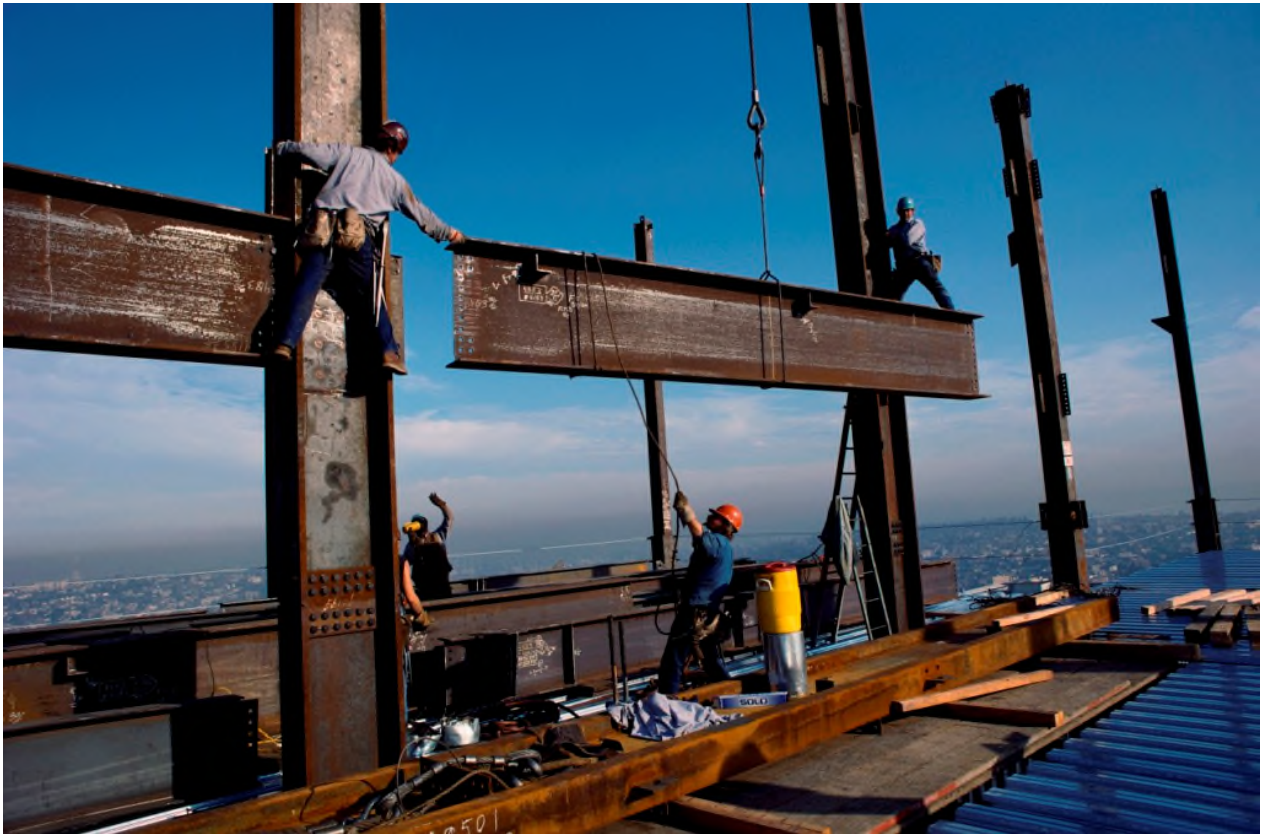
The mobile cellular telephone system has been expanding at a rapid rate in recent years. The three main mobile operators have a total of more than 50 million subscribers. The number of internet users is estimated at more than eleven million.

## 1.6 Foreign trade

Russia and the European Union together account for more than half of Ukraine's trade. The US is a relatively small trade partner, accounting for only 2.9% of exports and 3.3% of imports. In 2008, metals accounted for more than 41.2% of Ukraine's exports, however, due to decline in the global demand, the share of metals in the exports structure declined to 33.4% in 2009.

Ukraine imports 90% of its oil and most of its natural gas. The country is heavily dependent on Russia for the supply of natural gas, and this has a significant impact on Ukraine's economic and foreign policy.





## 2 Business environment

### Investor considerations

- Ukraine remains a challenging place to do business.
- Ukraine joined the WTO in 2008.
- Many investment opportunities exist, but Ukraine is still developing the legal and institutional frameworks required to fully support international business.
- Dramatic drop in the real estate market in 2008-2009 (up to 50%).
- The European football championship, to be hosted by Ukraine and Poland in 2012, is expected to provide a positive impact on the development of the economy and building infrastructure.

### 2.1 Business climate

Since becoming independent in 1991, Ukraine has struggled to shift from a centrally planned economy to a market environment.

Since 2000, Ukraine has implemented significant positive economic and legal reforms. The economy grew at an annual rate exceeding 7% over the period from 2000 to 2008. This growth was fueled by strong domestic demand,

and solid consumer and investor confidence. The economic and financial crisis that unfolded in 2008 shook investor confidence and stalled the inflow of capital. Ukraine remained in recession throughout 2009, with a recovery anticipated during 2010, as global conditions are expected to improve.

It appears that the short supply of credit is resulting in investments moving to low-yield, stable markets, and therefore, it is likely that Ukraine could become less

attractive for private-sector infrastructure investment. However, preparation of the 2012 UEFA European Football Championship may fuel the construction industry.

Ukraine allows foreigners to purchase businesses and property (but not agricultural land), repatriate revenue and profits, and receive compensation if property is nationalized. Reform is still needed, as complex laws and regulations, and weak enforcement of contracts by the courts still hinder foreign direct investment.

There was much interest in mergers & acquisitions (M&A) between 2004 and 2008. In 2007, the Ukrainian M&A market reached an estimated USD 9.8 billion, exhibiting explosive growth of 200% compared to 2006. In 2008, there were only 36 transactions with a total value of USD 3.7 billion, according to M&A Journal. Among the reasons for the decline in the volume of transactions were tight credit, decrease in the value of acquisition targets, delay of deals due to fair pricing difficulties, and economic uncertainties. Low activity on the M&A market remained an issue through and beyond the end of 2009.

At first glance, taxes appear quite low - 25% for companies, 15% for individuals, while value-added tax (VAT) is 20%. However, there are certain issues:

- Restriction on deductions means the effective corporate tax rate is closer to 30%.
- Social security contributions can be significant. In 2009, employer contributions to various funds exceed 36 % (up to 49.7%) of employees' earnings. The earnings base, which is subject to social contributions, is capped at USD 1,630 per month (see Chapter 7.3 for further information).
- VAT refund constraints, as well as restrictive rules for zero-rating sales of services to non-residents, mean that VAT can become a significant cost to business.

Despite its extensive human capital, natural resources, and industrial potential, it is clear that Ukraine still faces significant business challenges.

The World Bank Doing Business 2010 study put Ukraine in 142nd place out of 183 countries in terms of the ease of doing business. However, the study pointed out that reforms in 2008 improved protection of investors in Ukraine.

## 2.2 Economic development plans

Following the 2004 Presidential elections, the President's team focused on improving transparency. Tax privileges for

economic zones were removed entirely in early 2005 and privatisation sales become more transparent. Some headway has been made in bringing the large hidden economy into the open.

Unfortunately, the Government has not developed a clear strategy for reform. The removal of incentives and attempts to unwind questionable privatisations sent disconcerting signals to investors about the stability and predictability of the investment framework.

The transition into a parliamentary system is also likely to present certain challenges and uncertainty during the time of change, so it may be some time before a clear economic blueprint is developed.

## 2.3 Free trade zones

There are currently no free trade zones in Ukraine.

## 2.4 European Union, NATO, WTO

In 2005, President Viktor Yushchenko stated that membership in the EU was a strategic goal of his foreign policy. In practice, Ukraine maintains especially close ties with Russia (including energy dependence) and balancing this relationship affects the speed with which Ukraine can move toward integration. The EU is expected to deepen economic and political ties with Ukraine, but has yet to formally indicate Ukraine's prospects of future EU membership.

Ukraine also maintains a close relationship with the North Atlantic Treaty Organisation (NATO), particularly with respect to emergency situations, technical cooperation, scientific studies and military and defence reforms.

The General Council of the World Trade Organization approved Ukraine's accession on 5 February 2008. Ukraine became the WTO's 152nd member on 16 May 2008. Overall this has had a positive impact on Ukraine's investment climate.

## 2.5 International agreements

Ukraine has established diplomatic relations with over 170 countries.

Ukraine is a member of the United Nations, the Council of Europe, the International Monetary Fund (IMF), the World Bank, the European Bank for Reconstruction and Development (EBRD), the World Trade Organization (WTO), as well as a number of other international

organisations. Ukraine also cooperates with the Organisation for Economic Cooperation and Development (OECD), but is not a member.

In addition, Ukraine has concluded numerous bilateral agreements concerning trade, avoidance of double taxation, and mutual guarantees of investments. It has a free trade agreement with Russia, as well as with countries of the Commonwealth of Independent States (CIS).

## 2.6 Legal environment

The Ukrainian judicial system was significantly reformed in 2002. Judges are now appointed by presidential decree for five years, after which the Parliament confirms them for life.

Although the system has improved significantly, there are still many problems. The Supreme Court is regarded as being an independent and impartial body, but the same cannot yet be said for the lower courts. Courts also remain under-funded, meaning they are often understaffed, while some judges may not have sufficient experience to adequately resolve some modern issues in corporate law, taxation, bankruptcy, and intellectual property. Poor enforcement of court decisions is also a significant problem.

A legal framework does exist, and courts are one option for resolving disputes, but issues may be best resolved outside the judicial system. It is worth considering arbitration as an alternative dispute resolution mechanism when drafting contracts, although it needs to be recognised that this option is still developing and the system suffers from a shortage of skilled arbiters.

## 2.7 Property market

Foreign citizens and legal entities have the right to own apartments, houses, and other facilities. Ownership of non-agricultural land is also possible, although legal and regulatory restrictions can significantly complicate the process.

The global financial crisis continues to depress Ukraine's property markets. The commercial property market has been characterized by lowered rents and the growth of vacancy rates. The rents for Class A office buildings peaked in 2008 at over USD 70 per square metre and have since fallen to approximately USD 30 per square metre. Yields have increased in 2009 to 17-20% from 10-13% in 2007.

The retail premises and industrial premises segments have also slowed, mainly due to the downturn in the economy.

Residential property has yet to recover from the housing bubble, when prices increased by 550% between 2002 and 2007. Given the size of the housing bubble, it might take years before the market is corrected.

## 2.8 Foreign investor associations

There are a number of foreign business chambers in Ukraine, including the American Chamber ([www.amcham.kiev.ua](http://www.amcham.kiev.ua)) and the European Business Association ([www.eba.com.ua](http://www.eba.com.ua)). Both chambers have active committees on various issues affecting business and investors in Ukraine. Contact details are provided in Appendix B.



## 3 Foreign investment and privatisation

### Investor considerations

- There are very few restrictions on foreign investment.
- The Ukrainian legal system is still evolving.
- Ukraine has a number of foreign exchange restrictions, but these should not create unmanageable problems.
- Silent approval is now available for many permits and licenses.

### 3.1 Foreign investment

#### Investment climate

Ukrainian authorities regularly declare their keenness to encourage foreign investment and the broader public is well disposed towards foreign investment.

Generally, the regulatory framework for the establishment and operation of businesses in Ukraine by foreign investors is similar to that for domestic investors, apart from the ownership of agricultural land, publishing activities and the manufacture of carrier rockets. As a general rule, investment permits are not required, but all enterprises must be established according to the form and procedure prescribed by law and registered with the appropriate government agencies. Foreign investors are generally not required to seek special approval from authorities for

foreign direct investments, but shall register them with the state authorities.

Both domestic and foreign investors still encounter difficulties at a practical level. These do not relate specifically to the issue of foreign ownership or investment, but rather to arbitrarily enforced administrative hurdles, or random delays.

Stock of foreign direct investment amounted to more than USD 39 billion at the end of 2009. Foreign direct investment in 2009 was slightly less than USD 3 billion, compared to USD 6 billion in 2008.

## Regulatory legislation

Ukraine continues to struggle to build a legal system that facilitates easy interaction with the international community. Many issues are not dealt with by a single piece of legislation, so it may be necessary to piece several laws together to develop a full understanding of an issue. The various laws may also be ambiguous or contradictory, which may further complicate the issue. There is no consolidated tax code.

The following major pieces of legislation (in addition to taxation law) affect foreign investment into Ukraine:

- *The Foreign Investment Law* sets out in broad terms Ukraine's policy on inward investment and the rights and obligations of foreign investors.
- The *Civil Code* regulates civil relationships, the establishment of legal entities and personal property rights.
- The *Commercial Code* was enacted on the same day as the Civil Code, and governs business relationships. The Commercial Code is intended to regulate issues that are not dealt with in the Civil Code, although in practice there is some overlap.
- *On Securities and Stock Market* governs the public issuance and trading of securities.
- *The Competition Law* restricts business monopolies. The majority of mergers and acquisitions in Ukraine are likely to require pre-approval from the Anti-monopoly Commission.
- *The Law on Protection from Unfair Competition* aims to protect business entities and consumers from unfair competition.
- *The Environmental Protection Law* establishes a framework for pollution charges to be imposed on any

legal entity that discharges contaminants into the environment.

## Restrictions on foreign investment

Foreign companies are restricted from owning agricultural land, manufacturing of carrier rockets and some publishing activities.

## Investment incentives

Ukraine eliminated all investment incentives in March 2005.

## Foreign exchange issues

Foreign currency is regulated by the 1993 Cabinet of Ministers Decree, *On The System Of Currency Regulation And Currency Control*, as well as a number of implementation rules issued by the National Bank of Ukraine (NBU). A number of foreign currency transactions may be undertaken only if an individual licence has been obtained from the NBU. Although there has been an ongoing trend toward less restrictive rules, the most recent developments (late 2009) brought new restrictions. For example, foreign investments in monetary form on the territory of Ukraine must be made through investment accounts in Ukrainian banks (see below).

For further discussion on foreign exchange rules, see Chapter 4.2.

## Repatriation of capital and earnings

Foreign investors are entitled to repatriate profit, income or other funds relating to investments without any restrictions, provided the investment was made in accordance with applicable legislation and after the payment of applicable taxes. Foreign investors are guaranteed the right to the prompt and unimpeded repatriation of profits.

## Anticrisis Law

Until January 1, 2011, foreign investors are required to use Ukrainian "investment accounts" for making monetary investments in Ukraine and must register all types of investments with the authorities. Before enactment of the Anticrisis Law, state registration of foreign investments was not mandatory, although many foreign investors opted to register their investments. Registration of property investments involves the submission of a prescribed set of registration documents to the regional (oblast) state administration. Registration of monetary investment shall be performed by the NBU but guidance has yet to be issued.

## Guarantees and rights

Foreign investments duly registered with the state authorities are not to be subject to nationalisation, expropriation, requisition, or any other measure of similar effect, except when this is in the public interest. In such cases, compensation must be provided to the investor based on the market value of the property.

## 3.2 Simplification of licensing process

Starting from December 30, 2009 the procedure for obtaining licenses has been simplified.

A "silent consent" principle is established for obtaining most but not all permits (licenses). If an application for a permit (license) and the respective supporting documents have been properly submitted, and the authorities fail to respond within the term established by law (either to issue the permit (license) or reject the application), the applicant is allowed to pursue the activities as if the permit (license) had been issued.

Licenses are issued for an indefinite period, unless a limited term of validity for a particular type of license is established by the Cabinet of Ministers of Ukraine for a particular type of license. However, even in such a case, the term of validity will be not less than 5 years.

Certain types of business activity are excluded from the list of activities that are subject to licensing. A limited number of activities no longer require licenses.

## 3.3 Privatisation

### Background

Privatisation of medium and large-scale enterprises was started in 1995 under the "Mass Privatisation Program" (MPP) project sponsored by USAID. In parallel, the State Property Fund (SPF), the government's privatisation authority, privatised many small-scale enterprises, primarily for cash. The MPP was initially planned for one year (1995-96), but was in effect through 1999. Since approval of the *Privatisation program for 2000-2002*, privatisation programs have not been approved. Instead, the Cabinet of Ministers of Ukraine issues a list of enterprises to be privatised in the respective year.

### Failed OPP sale (2007-2009)

The Kryvorizhstal sale in 2005 demonstrated that transparent privatisation sales in Ukraine are possible. But

growing political and economic crises during the following years intensified disagreements between branches of government about the privatisation of strategic enterprises.

The most current example is Odesa Port Plant. Analysts anticipated that the sale of a 99.5% stake in the Odesa Port Plant would bring the Government USD 500 million in 2007. The 99.5 % share in Odesa Port Plant was auctioned, but the results of the auction were declared illegal by Presidential Decree and court resolutions. In 2009 another auction for Odesa Port Plant was conducted, but the result of the auction was again nullified by the Government.

### Legacy of privatisation

The impact of Ukraine's privatisation can be assessed in terms of the following strategic changes in Ukraine's economy:

- The State has given up majority ownership in 90% of the industrial enterprises it owned in 1991. Millions of Ukrainian citizens have become shareholders and more than 60% of Ukraine's labour force work for private enterprises.
- Although many directors and managers of privatised enterprises are from the Soviet era, they are gradually being replaced by a new post-Soviet generation of directors and managers.
- In many cases, the new generation of investment fund managers, who have become major shareholders via the privatisation program, are putting in place new enterprise directors and managers and introducing new management techniques.
- State budget support for unprofitable enterprises has been greatly reduced.

### Privatisation calendar

It is difficult to talk of a privatisation calendar in Ukraine. Political considerations mean that the list of potential privatisations is a moving target. For example, one of the more attractive entities still to be privatised is Ukrtelecom (a monopolist in the fixed-line communications market). Originally it was planned to sell a 92.8% interest by 2000. This year, SPF aimed to sell a 67.8% share estimated to have a value of USD 974 million. But despite significant publicity, the tender was not conducted.

Therefore, considering the political situation, it is necessary to monitor ongoing developments to identify opportunities that may arise. At the time of publishing (early February 2010) the privatisation list for 2010 had not been adopted.



## 4 Banking, finance and insurance

### Investor considerations

- There has been a significant level of international investment in the banking and insurance sectors.
- Consumer credit facilities are at minimal levels due to the economic slowdown.
- There is a tendency for reducing the quantity of banks and insurance companies in Ukraine.
- A full range of traditional banking services are available in Ukraine, although intermediation costs remain high.
- Since Ukraine joined the WTO in 2008, branches of foreign banks should be permitted to enter the market in Ukraine. However, a relevant legislative framework has yet to be adopted.
- Non-resident insurance companies will be entitled to open branches and provide a full scope of insurance activity in Ukraine starting from 2013.
- Early repayment of loans from non-residents is not allowed.
- There are no requirements to convert foreign currency export proceeds into Hryvnia.

### 4.1 Banking system

Ukraine has a two-tier banking system. The National Bank of Ukraine (NBU) is Ukraine's central bank. Commercial

banks, including the state-owned State Export-Import Bank of Ukraine (Ukreximbank) and the State Savings Bank of Ukraine (Oschadbank), operate under the authorisation and supervision of the NBU.

## National Bank of Ukraine

According to the National Bank Law (1999), the primary function of the NBU is to ensure the stability of the Hryvnia (UAH), the national currency of Ukraine. The NBU's objectives are also to maintain stability in the banking system, as well as price stability, to the extent this is possible.

The highest governing body of the NBU is the Council, consisting of 15 members. Seven members are appointed by Parliament, seven by the President, whilst the Governor (who acts *ex officio* as the fifteenth member) is nominated by the President and appointed by Parliament. The Council is responsible for developing the principles of Ukraine's monetary policy.

## Banking sector

The Ukrainian banking sector appeared to be the most affected by the credit crunch. The crisis continues to pose significant risks for the banking sector as it has triggered a significant slowdown in the credit market. Historically characterized by a number of significant weaknesses, Ukrainian banks are suffering from a lack of liquidity as many borrowers begin to default on their debts because of the devaluation of Hryvnia and the plunge in real estate prices.

Banks are required to prepare accounts that are based on International Financial Reporting Standards (IFRS).

As of 1 January 2010, 199 commercial banks were registered in Ukraine, out of which 185 banks have been granted licences by the NBU to perform banking transactions. There are about 30 representative offices of foreign banks.

The Ukrainian banking sector has a high level of concentration. According to data published by the NBU, over 50% of the banking sector's total assets were held by the ten largest Ukrainian banks. According to the NBU, at year end, the total loans granted by banks amounted to UAH 751 billion (USD 93.9 billion), and their total statutory capital amounted to UAH 122 billion (USD 15.2 billion). At least 49 banks in Ukraine had some foreign capital, of which 17 were fully owned by foreign owners; approximately 35% of the total statutory capital of all Ukrainian banks was represented by banks with foreign capital (including four of the ten largest).

Commercial banks require a license from the NBU. The NBU has established requirements for capital adequacy, minimum statutory capital, and minimum regulatory capital. Since 2006 the minimum statutory capital requirement for a bank is UAH 75 million (approximately USD 9.4 million).

## 4.2 Foreign currency rules

Foreign currency operations are regulated by the 1993 Cabinet of Ministers Decree, *On the System of Currency Regulation and Currency Control*, as well as a number of implementing rules issued by the NBU.

The key issues regarding Ukraine's current exchange control regulations are:

- Payments under foreign trade contracts between a resident and a non-resident entity should be in foreign currency only.
- Payments in foreign currencies between residents in the territory of Ukraine are generally prohibited.
- Salaries to Ukrainian staff must be paid in Ukrainian currency (but expatriate employees can be paid in hard currency).
- Foreign loans must be registered with the NBU before funds are remitted to Ukraine. NBU has reinstated a maximum interest rate and other charges that may be applied to foreign currency loans obtained from non-residents. Early repayment is prohibited (see below).
- The maximum allowable interest rates for foreign fixed rate loans in hard currency (inclusive of any fees and charges due under the loan agreement) are 9.8% p.a. for loans up to 1 year; 10% p.a. for loans for 1-3 years; 11% p.a. for loans over 3 years. For loans with floating interest rates the maximum allowable interest rate is three month's USD LIBOR plus 7.5%.
- Proceeds from export must be credited to the exporter's Ukrainian bank account within 180 days from the date of customs clearance (for goods) or date of services delivery. Similarly, prepaid goods must be imported and cleared through customs within 180 days of payment. Failure to do so results in a fine of 0.3% of the amount due or paid for each day of delay.
- The purchase of foreign currency in 2010 is subject to a 0.5% Pension Fund charge, which is withheld by the bank.
- Payments by Ukrainian business entities for services rendered by non-residents for amounts exceeding EUR 100,000 (annually) require confirmation from the Foreign Markets Monitoring Centre (FMMC) that the fee for the services does not exceed market prices. Provided relevant documentation is in place, this should not delay payments. However, the process cannot be taken lightly. If



the FMMC rejects an application, no payment will be permitted.

Ukrainian companies (and individuals) are required to obtain a license from the NBU for a number of transactions, including the following:

- Cash investments abroad for the acquisition of fixed assets, intangible assets, corporate rights, securities and derivatives.
- Purchase of Ukrainian securities from non-residents.
- Opening bank accounts abroad.

## Foreign borrowings

In 2009 the President of Ukraine signed a Law on Overcoming the Effects of the Financial Crisis. The Law introduces specific legislation in respect of banks and financial institutions. Until 1 January 2011 the Law prohibits:

- Early repayment of foreign loans under existing loan agreements.
- Amending existing or concluding new loan agreements allowing early repayment of a loan.

## 4.3 Specialised financial institutions

The Ukraine leasing market is growing.

According to the Ukrainian Leasing Development Project run by the International Finance Corporation ([www.leasing.org.ua](http://www.leasing.org.ua)), the number of leasing operations increases each year. Despite the fact that the number of leasing operations showed an increase in 2008, the price value of such operations fell in comparison with previous years because of increasing financial and political issues resulting from the crisis. This further reduced in 2009.

Transport, farm machinery and construction equipment constitutes the largest part of the leasing market.

## 4.4 Investment institutions

The law *On Joint Investment Institutions (Unit and Corporate Investment Funds)* was enacted in 2001 and provides a framework for the establishment of mutual investment funds. The investment funds boast an attractive tax regime for investments and re-investments (corporate profit tax exemption). They flourished in 2006-2007 but the

75% drop in the Ukrainian stock market in 2008 led to a drastic decrease in their popularity with investors.

Asset management companies, licensed by the State Securities and Stock Market Commission of Ukraine, are permitted to manage the assets of corporate and unit investment funds, as well as non-government pension funds. An investment fund, when created and registered with the State Securities and Stock Market Commission of Ukraine, issues securities (investment certificates or shares) to investors. Investors' money is invested in the securities of other issuers, in participatory interest, real estate, bank metals and other assets permitted by legislation.

## 4.5 Capital markets

Capital market transactions in securities are regulated primarily by the Laws on Securities and the Stock Market and the Law on State Regulation of the Stock Market in Ukraine. In addition, a new law regulating joint stock companies' activity has come into force.

All transactions on the stock market are under the control of the State Securities Commission of Ukraine.

The economic crisis resulted in a decrease of market capitalization. Thus, in 2009 the volume of trading through the PFTS Stock Trading System ([www.pfts.com/eng](http://www.pfts.com/eng)), the largest stock exchange in Ukraine, dropped dramatically due to the unfavourable business environment.

Current currency control regulations and cross-border investments rules, coupled with the current economic situation, discourage foreign investors from making investments in Ukraine through the stock exchange.

## 4.6 Insurance

There are more than 50 Ukrainian insurers with foreign capital, and a broad range of insurance services are available. Currently more than 150 insurance companies operate in Ukraine, 23 of them in the field of life insurance. The market is regulated by the State Financial Markets Commission, and initiatives to strengthen industry practices are ongoing. The activity of foreign insurance companies in Ukraine is limited to re-insurance and some types of insurance activity specifically envisaged in the law.

The insurance sector most affected by the economic crisis was that providing insurance to individuals. Nonetheless, a number of new insurance companies (both in life and non-life insurance) were registered during 2009. There are significant restrictions on Ukrainian residents' ability to make insurance payments abroad.



## 5 Importing and exporting

### Investor considerations

- Ukraine joined the World Trade Organization (WTO) in 2008.
- Goods imported into Ukraine are subject to customs duties, excise tax (if applicable) and value-added tax (VAT).
- Ukrainian customs valuation rules comply with WTO rules.
- Ukraine has a free trade agreement with Russia and other CIS countries.
- The customs authorities scrutinise customs values and the classification of imported goods, and post-entry customs audits have been implemented.

### 5.1 Trends in customs policy

In recent years, Ukrainian customs regulations have gradually evolved towards greater compliance with international practice. In 2004 Ukraine implemented a Customs Code which incorporated the main provisions found in international customs conventions and WTO principles, and customs classifications follow WTO guidelines.

In 2008 Ukraine joined the WTO. This resulted in a further reduction of import customs duties, and post-entry audits are expected to become more frequent.

Ukraine is a signatory to major international customs conventions, including the Kyoto Convention on Simplifications and Harmonisation of Customs Procedures, the International Convention on the Harmonised Commodity Description and Coding System, the Istanbul Convention on Temporary Admission.

Although the legal framework has developed in line with international norms, many administrative practices

remain unchanged. Thus, although Ukrainian law allows customs authorities to conduct post-entry audits to verify compliance with customs and tax legislation, in practice the authorities still exercise almost all customs control during the initial clearance of goods. Qualifying entities may benefit from simplified customs procedures; however, strict criteria prevent these benefits from being available to a wider range of entities.

Since 2008 Ukraine has introduced the option of electronic filing of customs declarations. But, at the moment, electronic filing is only used to make preliminary notifications.

## 5.2 Import restrictions

There is a compulsory certification procedure to ensure that imported goods comply with national standards. The certification is provided by the Ukrainian certification authorities (UkrSEPRO) in respect of a wide range of imported goods by issuing a Ukrainian Compliance Certificate. In the absence of such a document, goods cannot be imported into Ukraine.

In addition, certain imports to Ukraine require licenses, including plant protection chemicals, equipment and optical polycarbonate for manufacturing disks used in laser reading systems, ozone damaging substances, printer's ink, paper with water marks, certain food products.

## 5.3 Customs duties

### Classification of goods

The Ukrainian Classification of Foreign Economic Activities (UC FEA), which is based on the Harmonised Commodity Description and Coding System (2002), is the effective customs classification document in use in Ukraine. UC FEA serves as the basis for Ukraine's Customs Tariff. Ukraine is a member of the International Convention on Harmonised Commodity Description and Coding System, so this system is consistent with international standards.

### Valuation rules

Ukrainian customs valuation rules generally comply with the Agreement on Implementation of Article VII of the GATT 1994. This means that the transaction value is generally used as the basis for determining dutiable value. The customs value should be determined in accordance with one of the six WTO valuation methods, which apply in sequential order. The customs authorities are entitled to assess duties at a higher value in certain circumstances.

Recently the customs authorities have announced their official position in respect of customs treatment of

royalties. According to such position, royalties relating to patents, industrial patterns, certain types of plants, animal breeds, trademarks and copyrights are dutiable in most cases. Their interpretation is not necessarily in line with international standards.

### Tariff rates

There are two rates of import duty under the Customs Tariff.

- Reduced duty rates apply to goods originating from all WTO countries and countries that have granted Ukraine "Most Favoured Nation" trade status.
- Full rates of duty apply to goods originating from other countries, or where the country of origin cannot be determined.

In many cases, the reduced rates and full rates of duty are the same. Rates of duty may be ad valorem, specific (in monetary units per unit of goods), or a combined. There are seasonal, special, anti-dumping and countervailing duties. A selection of customs duty rates is provided in Appendix D.

### Free trade agreements

In addition to the reduced rates mentioned above, Ukraine has concluded free trade agreements with Russia and other CIS countries, as well as with Macedonia. These agreements allow many goods to be imported into Ukraine duty-free, subject to compliance with preferential rules of origin. The 2000 CIS Rules for Determining Country of Origin are used to determine whether goods originate from a particular country to qualify for these duty exemptions.

### Excise tax

Excise tax is payable on cars, car bodies, alcoholic beverages, tobacco products, beer, petrol and diesel fuel. Rates of excise duty are specific. A list of selected rates can be found in Appendix D.

### Import VAT

VAT is imposed on imported goods at a rate of 20%, unless expressly exempted under the VAT law (see Chapter 12). The taxable base is either the contractual or customs value of the goods, whichever is higher, plus the amount of any import duties and excise duties (if any).

### Customs processing fees

A customs processing fee is applied for overtime and off-location customs clearance of goods at an hourly rate ranging from USD 20 to USD 50 for the work of one customs inspector.

## Payments

Import duties and taxes are payable by the importer in local currency before or upon customs clearance. In certain cases, customs payments must be deposited with customs before the goods cross the Ukrainian border. Excise duty on imported cigarettes is payable prior to customs clearance during purchase of excise stamps.

## 5.4 Temporary import relief

Permission for temporary import/export with full conditional exemption from import taxes may be issued in a number of specific cases; including:

- Goods intended for display or use during exhibitions, fairs, conferences and similar events.
- Professional equipment used by mass media or required for making films.
- Containers, pallets, packaging or any other goods imported in connection with commercial transactions.
- Transport vehicles used for moving passengers and goods across the Ukrainian border.
- Sea vessels and aircraft imported for repair.

Ukraine is a member of the Convention on Temporary Admission (Istanbul, 26 June 1990) allowing tax-free temporary import of a limited number of goods into Ukraine. Temporary importation is allowed to a maximum of one year and can be extended further by the customs authorities.

## 5.5 Customs duties incentives

### Charter capital contributions

Property (except for re-saleable goods) contributed by a foreign investor to the charter capital of a Ukrainian entity may be imported free of customs duty, but will still be subject to VAT. Customs duty must be repaid if the property is disposed of within three years from the date of import.

### Toll manufacturing

Raw materials imported into Ukraine for processing under toll manufacturing arrangements enjoy exemption from import taxes and duties, provided the finished products are re-exported from Ukraine within 90 days. The processing should meet the following criteria:

- Raw materials and finished goods must belong to the foreign customer.

- The tariff code must change as a result of processing.
- The cost of the raw materials must be at least 20% of the value of the finished goods.
- The imported raw materials must be the main component at each stage of production.

Cross-border tolling is not allowable for agricultural products.

Finished goods (other than agricultural products) can be sold in Ukraine after tolling only through a permanent establishment of the foreign entity (an owner of the goods) in Ukraine, after import duties have been paid. However, the procedure of sales are not regulated and therefore, this may be problematic in practice.

### Repairs, assembly

Import of goods after repair abroad may be exempt from customs duty. A duty exemption applies to import of goods for repair, installation, assembly, mounting and adjustment on the condition that the repaired goods or finished products are exported from Ukraine within 90 days of import.

### WTO valuation decisions

With its entry into the WTO, Ukraine committed to comply with the WTO customs valuation guidelines on the following:

- Carrier media with recorded computer programs should be valued for customs based on the value of carrier media, i.e., the cost or value of the computer program should not be taken into account.
- Generally, charges for interest under a financing agreement entered into by the buyer and related to the purchase of imported goods shall not be regarded as part of the customs value.

### Representative offices

Representative offices of foreign companies may import goods for official use and which are not intended for resale under the temporary import procedures. Exemption from customs duty and taxes is not available, so the exemption has no practical advantage.

## 5.6 Documentation and procedures

All goods crossing the border are subject to customs control, which includes specific procedures aimed at ensuring compliance with customs rules. The customs authorities may conduct post-entry audits to verify compliance with customs and tax legislation. In addition to customs control, other types of border control including sanitary, veterinary, phytosanitary, radiological, ecological controls and control over cross-border movement of art may be conducted.

### Registration of importers

Any business entity (including representative offices of non-residents) that is engaged in import operations is required to register with the customs office that serves the area in which the company is located. Customs clearance of goods in another customs office requires permission from the customs office where the entity is registered.

### Documentation

Goods crossing Ukraine's border should be declared to the customs authorities, either by the importer or a licensed customs broker on behalf of the importer. The importation of goods must be supported by complete documentation. The following import documents are required for all shipments to Ukraine:

- Import customs declaration.
- Declaration of customs value.
- Cross-border contract.
- Invoice and waybill.
- Compliance certificate (if any).
- Certificate of origin.
- Evidence of payment of customs duties and taxes.
- Any other documents that may be requested by Customs.

Missing or deficient documents are likely to cause delays during customs clearance.

### Declaration of customs value

Customs value is declared by filing a declaration of customs value, including reference to the valuation method used. The importer must also provide relevant documents to demonstrate the customs value. If these documents are not available, or if the customs office has

well-grounded doubts about the data provided by the importer, the customs office may determine the customs value based on the information available. This may include information available to the authorities on prices for identical or similar goods.

When the customs value requires review, or when the importer does not agree with the customs value determined by the customs office, the importer may request that the customs office release the goods for free circulation against payment of import taxes. The importer may then appeal the determination of the customs value by the customs authorities to a higher customs office, or to the courts.

## 5.7 Warehousing and storage

To defer payment of import taxes and duties, goods may be stored in a warehouse of temporary storage (WTS) under customs control for up to three months before they are released under a specific customs regime. The WTS operator must obtain permission of the customs authorities. There are two types of WTS:

- Open WTS, which is available to any users on a contractual basis with the WTS owner.
- Closed WTS, which can be used only by its owner.

Alternatively, imported goods may be stored in an opened or closed customs bonded warehouse (CBW) under customs control without payment of import duty and taxes, for up to three years, depending on the nature of the goods. Not all goods, however, may be stored in a CBW. A CBW operator must obtain the license of the State Customs Service of Ukraine.

## 5.8 Exports

### Restrictions

A limited number of exports are subject to licensing and/or quotas. Examples include silver and gold, certain metal products exported to the EU and Russia, and oil or gas of Ukrainian origin.

### Registration of exporters

Any business entity that is engaged in export operations is required to register with the customs office that serves the area in which the company is located. Customs clearance of goods through another customs office requires specific permission from the customs office where the entity is registered.

## Export duties

Ukraine has limited export duties on natural gas, scrap metal, livestock, raw hides and certain oil seeds. Exported goods and ancillary services are zero-rated for VAT purposes.

## 5.9 Protection of intellectual property rights

Owners of intellectual property rights may request that Ukrainian customs authorities register goods containing intellectual property in order to prevent the illegal import or export of pirated or counterfeited goods. In this case, customs authorities may delay customs clearance of such goods until it can be proven that no breach of intellectual property rights has taken place. If the importer

or exporter does not submit sufficient evidence, the customs office may seize the goods and impose penalties.

## 5.10 Customs audits

The customs authorities are entitled to conduct post-entry audits and these have become more common in practice since 2008. These include field and desk audits. During field audits the customs authorities may analyse customs, financial, accounting and warehousing documentation.

As a rule, audits cover a 3-year period and focus on customs valuation, classification issues and eligibility for exemptions. During recent audits the customs authorities have focused on the customs treatment of royalties.



## 6 Business entities

### Investor considerations

- For representation, information gathering and liaison activities, a non-commercial representative office is likely to be an efficient vehicle.
- Establishing a legal entity is recommended for commercial activities, although a commercial representative office may be effective for a limited range of service activities.
- For a 100% investment, a limited liability company (LLC) is usually recommended. It is cheaper and quicker to establish than a joint stock company (JSC), and is less regulated. The minimal capital for an LLC is less than USD 200 (previously USD 10,000).
- Unincorporated joint ventures and partnerships exist as investment vehicles, but have uncertain legal status and are not widely used.
- Branches of foreign entities are not explicitly recognised by law, and would prove difficult to establish

### 6.1 Legal framework

#### Legal framework for business entities

The primary framework for establishing and operating legal entities in Ukraine is found in the 2004 Civil Code. Legal entities may be established in the form of joint stock companies, limited liability companies, additional liability companies, general partnerships or limited partnerships.

The Civil Code, the 1991 law *On Business Associations* as well as the 2009 law *On Joint Stock Companies* (the

JSC Law) deal with such issues as shareholder rights and obligations, corporate governance, and minimum capital requirements.

#### Commercial law

The 2004 Commercial Code governs business relationships, and was intended to regulate issues that are not dealt with in the Civil Code. In reality, parts of the two Codes overlap, including a number of provisions dealing with the establishment and operation of legal entities.

## 6.2 Forms of business organisation

### Choice of business entity

Establishing a legal entity in Ukraine involves registering with the local state registrar, the tax authorities, the statistics office, and various pension and social funds, as well as opening a bank account, and other formalities.

From a foreign investor's perspective, the choice will tend to be either an LLC, a JSC, or in certain circumstances a representative office engaged in either commercial or non-commercial activities.

For a 100% investment, using an LLC tends to be more convenient. It is easier and quicker to establish (less than 4 weeks), has lower minimum capitalisation requirements (less than USD 200), and is less regulated.

If an investor intends to carry out only preparatory or auxiliary activities in Ukraine, such as representation, information gathering and liaison activities, establishing a non-commercial representative office is a viable and convenient option, provided there is double tax treaty protection.

It is not possible for foreign entities to conduct full commercial activities (executing contracts, trading goods and providing services, etc.) through a commercial representative office. Nonetheless, a number of law firms and other service providers have established their presence in Ukraine in this manner.

### 6.3 Net asset requirement

According to the Commercial Code, if the value of a company's (LLC or JSC) net assets at the end of the second and each subsequent financial year is less than its registered share capital, the company must decrease its share capital and make relevant amendments to its Charter. In addition, the law states that if the value of net assets falls below the statutory minimum capital, the company "shall be liquidated".

Under the Law, the State Securities and Stock Market Commission has the right to initiate liquidation proceedings against JSCs which violate the net assets rule. As for the LLC, the procedure for initiating liquidation is not clear, and we are not aware of any company being liquidated due to its non-compliance with the net assets rule.

### 6.4 Limited liability companies

A limited liability company (LLC) does not have shares in a traditional sense. Instead, participants in an LLC own a

percentage in the company's capital (participatory interest), as specified in its Charter. Because investors' interests in an LLC are not "securities", as defined by law, they are not subject to registration with the State Securities and Stock Market Commission. This means that an LLC can be established more quickly than a JSC, and is easier to maintain.

Nonetheless, there are a number of key points that investors need to be aware of before establishing an LLC:

- Participants in an LLC may transfer their participatory interest in the company's capital to third parties (non-participants). However, other participants have a pre-emptive right to acquire the participatory interest in an LLC.
- A participant may withdraw from an LLC at any time by giving three month's notice. Upon withdrawal, a participant is entitled to his proportionate share of the assets of an LLC, although this will often involve cash settlement.
- A participant who systematically ignores or improperly fulfils his duties, or whose actions interfere with reaching the aims of the LLC, may be excluded from the LLC by a majority vote. The excluded participant is entitled to his proportionate share of the assets of the LLC at the time of exclusion.
- A participant's personal creditors may demand to withdraw the participant's share in LLC assets to settle his debts, provided the participant's other property is insufficient to satisfy the creditors' claims.
- Because a participant may withdraw from the LLC, it is unclear whether contributions to such LLCs should be reported as equity or as a liability from the LLC to the participant. This issue should not have any implications from a tax or legal perspective, but may impact the LLC's ability to obtain finance from external sources, and could also impact the IFRS accounting.
- An LLC does not generally require a financial audit unless one is demanded by its participants.

If an LLC is 100% owned by one foreign investor, these issues are likely to have little practical implication. However, if there are two or more participants, the abovementioned issues need to be considered. Some issues, such as the notice period required for withdrawal from the LLC and the method of compensation, could be addressed by including appropriate timeframes and constraints in the LLC's Charter, but cannot contradict the law.



## Formation procedures

An LLC may be established by a single participant, provided that the founding company is not itself owned by a single participant. Also, a person (legal entity or individual) may not establish more than one LLC with a single participant. The governing document of an LLC is its Charter. The Charter determines the company's objectives and scope of activities, the size of its Charter capital, the composition and competencies of the governing bodies and the rules for decision-making.

The distribution of the LLC's participatory interest is set out in its Charter. If the participatory interest is transferred, the Charter will need to be amended to record the change.

Generally, incorporation will take three to four weeks from the day documents are filed with the registration authority. An LLC is deemed to exist as a legal entity from the date of its state registration.

## Capital structure

In December 2009 the minimum charter capital of an LLC was reduced to one minimum monthly salary (previously it was 100 minimum salaries). The minimum salary increases on a regular basis and as at January 1, 2010 it was UAH 869 (approximately USD 110).

At least 50% of the LLC's Charter capital must be paid before the company may register, and the remaining contributions must be paid within the first twelve months of the LLC's activity. It is possible for participants to contribute assets in kind to an LLC.

An LLC must create reserve capital from net profits in the amount of at least 25% of its Charter capital. At least 5% of annual after-tax profit must be transferred to this reserve until the entire 25% fund is fully paid (this is not tax deductible).

The conversion of debt into equity is not feasible for the LLC.

## Relationship of participants, directors and officers

LLCs have two corporate bodies.

The Participants' Assembly consists of the participants of the LLC, who vote proportionally to their interest in the company capital. Quorum for a Participants' Assembly requires the presence of participants holding at least 60% of all votes. Most resolutions are approved by a simple majority of the voters present at the Participants' Assembly, although resolutions amending the Charter and a limited number of other decisions must be approved by a majority of all participants' votes.

The Board of Directors (or Director) is the executive body of an LLC, and is responsible for managing the day-to-day activities of the LLC and representing the LLC against third persons. There is no formal requirement to appoint a company president, corporate secretary or any other office holder. The structure of the Board, its authority, and its working procedures are specified in the Charter.

## Liquidation, receivership

An LLC is liquidated if its participants agree to liquidate the LLC, its corporate term expires (if one is specified in the Charter), or it is ordered to be liquidated by the court. In a voluntary liquidation, preference in distribution is given, in order, to:

1. Indemnification of losses caused by disability, other health injuries or death, as well as creditors' demands secured by pledge or otherwise.
2. Employees' claims connected with labour relations.
3. Taxes and duties.
4. All other claims.

The preferences are slightly different for liquidation through compulsory liquidation (bankruptcy).

## 6.5 Joint stock companies

A joint stock company (JSC) is a legal entity whose Charter capital is divided into a specified number of shares with equal nominal value. The liability of shareholders in a JSC is limited to the value of their capital contribution.

Any JSC established before 30 April 2009 (the effective date of JSC Law), must bring its activities into compliance with the JSC Law no later than 30 April 2011. If the General Shareholders' Meeting of a JSC decides to change the amount of its Charter capital, to redenominate its shares, or to issue securities after 30 April 2009, such company is required to bring its activities into full compliance with the JSC Law.

The law On Business Associations still regulates the activity of closed and open JSCs until their mandatory "transformation" into private and public JSCs by 30 April 2011. According to the JSC Law, all JSCs shall be established as "public" or "private" JSCs.

The legal framework for JSCs is for the most part similar to that for LLCs. However, the JSC Law regulates many peculiarities of JSCs' activities. A brief comparative of the two vehicles is provided in Table 2 on the page 29.

## Shares

- By 30 October 2010, all shares of the JSCs shall be dematerialised (transferred from documentary into non-documentary form).
- Shares in a public JSC may be sold through public offer or private placement, and may be further traded on a stock exchange. By contrast, shares in a private JSC may only be allowed to its founding shareholders.
- Existing shareholders in a private JSC have pre-emptive rights to purchase shares offered for sale by the other shareholders, as long as such rights are provided by the Charter.
- Public JSCs must be listed with at least one stock exchange in Ukraine. Share purchase agreements must be concluded only on the stock exchange where the public JSC is listed.

## Corporate

- The number of shareholders in a private JSC may not be more than 100.
- All shareholders must be notified in writing of the General Shareholder's Meeting 30 days before such meeting.
- Cumulative voting will be either mandatory or voluntary (depending on the type of the JSC and the number of shareholders) for the appointment of the members of the Supervisory Board and/or the Audit Committee. Cumulative voting means voting during election of JSC's bodies, where the total votes of a shareholder are multiplied by the number of members of the JSC's body that are being elected; the shareholder is entitled to give all the votes so counted for one candidate, or distribute the votes among several candidates.
- JSCs (both public and private) having 25 shareholders or less may approve their decisions by correspondence, as opposed to voting in person at the General Shareholders' Meeting.
- A sole shareholder is exempt from the requirement to convene and hold General Shareholders' Meetings. Instead, the powers vested in the General Shareholders' Meetings will be performed by the sole shareholder.
- Members of the Supervisory Board and the Audit Committee can only be individuals.
- JSC allows for conversion of debt into equity, but the State Securities and Stock Market Commission of Ukraine has yet to develop appropriate regulations.

## Formation procedures

The issued shares of JSCs (private and public) must be registered with the State Securities and Stock Market Commission of Ukraine, which involves filing a set of documents prescribed by law. Processing of the application by the Commission may take up to two months.

## Capital structure

The minimum capital requirement for a JSC is the equivalent of 1,250 Ukrainian monthly minimum salaries at the time when the JSC is formed. The following minimum capital requirements apply for JSCs established in 2010 are in Table 1 below:

Established on or after	Minimum salary	Minimum capital (UAH)	Est. minimum capital (USD)
1 January 2010	UAH 869	UAH 1,090,000	USD 136,000
1 April 2010	UAH 884	UAH 1,105,000	USD 138,000
1 July 2010	UAH 888	UAH 1,110,000	USD 139,000
1 October 2010	UAH 907	UAH 1,134,000	USD 142,000
1 December 2010	UAH 922	UAH 1,153,000	USD 144,000

A JSC must create a reserve capital from net profits and retained earnings in an amount not less than 15% of its Charter capital. At least 5% of annual net profits must be transferred to this reserve until the entire 15% fund is fully paid (this is not tax deductible).

## Minority shareholders

The JSC Law provides specific protection for minority shareholders through:

- Determination of the right of the shareholder to receive detailed information on the JSC's activity.
- Abolition of the practice of paying dividends with products produced by the JSC.
- Introduction of the right of shareholders to conclude shareholders agreements.
- Possibility of requesting the mandatory buy-out of shares in cases provided for by the JSC Law.

- Introduction of new rules for share acquisition.
- Disclosing conflicts of interest during acquisitions.

## Reporting requirements

The JSCs are required to submit quarterly and annual reports to the State Commission on Securities and Stock Market. These reports include the annual audited financial reports, quarterly financial reports, reports on securities circulation, and details of any shareholders owning more than 10% of the total shares. JSCs should also publish their annual report in the official media not later than 30 April of the following year.

## 6.6 Foreign directors

If a foreign national is appointed as a Director, the local authorities expect to see a written employment agreement (contract) concluded between the Ukrainian company and the individual.

A foreign national that is to be appointed as a director of a Ukrainian company needs to obtain a Ukrainian Tax Individual Number (Tax ID). To obtain a Ukrainian Tax ID, the foreign national or his/her representative should file with the tax authorities a set of documents established by legislation. Obtaining the Tax ID Code can take up to three weeks, and this can slow down the employment process.

After the Ukrainian company has been registered with all required state authorities, it will be required to obtain a work permit for foreign nationals. Ukrainian legislation prohibits employing a foreign individual without obtaining a work permit. Refer to Chapter 11 for a discussion of taxation of foreigners in Ukraine.

## 6.7 Partnerships and joint activities

The Civil Code of Ukraine provides for the establishment of general partnerships and limited partnerships as legal entities, but such types are not widely used. Because partnerships are legal entities, there are no regulatory or legal advantages to conducting business through a partnership. Taxation is also imposed at two levels - at the partnership level and in the hands of the partners.

Joint ventures typically involve the establishment of a separate legal entity (JSC or LLC) in Ukraine. However, the Civil Code does recognise the concept of a joint venture without the need to establish a separate legal entity. In such cases, the relationship between the parties will be governed by the agreement. Such agreements are commonly referred to as "joint activity agreements".

The use of joint activity agreements is still relatively unexplored. There are no minimum capital requirements or capital impairment rules to contend with. A partner may still withdraw by giving a three-month notice, but legislation considers that this could be treated as a breach of contract and necessitates the payment of damages.

## 6.8 Branches

In Ukraine, it is not currently possible to register a branch of a foreign legal entity.

## 6.9 Representative offices

A representative office is not a separate legal entity, and operates in Ukraine on behalf of the foreign company it represents.

From a tax perspective, local rules for representative offices are broadly in line with those of other countries. The problem is that the broader legal framework has not been updated, which can create uncertainty when dealing with state authorities.

Nonetheless, if the foreign company intends to carry out only non-commercial activities, such as representation, market monitoring, gathering of information, and liaising, it should be sufficient to establish a representative office, provided there is a double tax treaty in place.

If contemplated activities are limited to the provision of services, establishing a commercial/taxable representative office may be a suitable option. A number of professional firms operate under this structure.

A representative office should be registered with the Ministry of Economy of Ukraine (currently subject to a registration fee of USD 2,500), the Statistics authorities, the tax authorities, and the pension and social security funds. A representative office must also obtain a permit from the respective department of the Ministry of Internal Affairs of Ukraine to use its official stamp. Once the representative office has been registered with the tax authorities and has obtained a permit for the official stamp, it may open accounts in hryvnia and foreign currency in a Ukrainian bank.

Representative offices are subject to normal corporate income tax. However, an exemption may be available if the activities of the representative office are not sufficient to establish a taxable permanent establishment as defined by the relevant tax treaty.

Non-commercial representative offices are generally not subject to VAT. A commercial representative office must register for VAT once its taxable sales for the previous 12 calendar months exceed UAH 300,000, although it may also register voluntarily.

## Lost in translation

Ukrainian legislation is written in Ukrainian. Professional services firms typically provide advice to foreign investors in English or other foreign languages.

There is no agreed standard regarding how the titles of laws should be translated. For example, the Commercial Code is often referred to as the Economic Code, while the Law of Ukraine on Company Income Tax, is also referred to as On Enterprise Tax or as On Business Tax.

Individual words within the text of the laws may also be rendered in different ways. For example, the Ukrainian word *товариство* in the Civil Code is equally well rendered as company, association, society or partnership.

As with investment in any other country, one cannot assume that labels used in Ukraine will mean the same as they do in the investor's home country.

**Table 2: Brief comparison of joint stock companies and limited liability companies**

	<b>Joint stock company (JSC)</b>	<b>Limited liability company (LLC)</b>
<b>Registration</b>	Primary registration is made with the State Registration Department.  A JSC shares must be registered with the State Securities and Stock Market Commission.	Registration is made with the State Registration Department.
<b>Minimum capital</b>	1,250 Ukrainian monthly minimum salaries (approximately USD 136,000).	One Ukrainian monthly minimum salary (approximately USD 110).
<b>Transfer of shares</b>	There are generally no restrictions on the transfer of shares in a public JSC. There are specific regulations regarding significant shareholdings and mandatory by-outs.  In a private JSC, the existing shareholders may have a pre-emptive right to purchase shares.	Unless the Charter says otherwise, the existing participants have a pre-emptive right to purchase the participant's share in LLC.
<b>Supervision</b>	Regular reporting to the State Securities and Stock Market Commission, to the tax and other local authorities, filing of annual accounts.	Regular reporting to the tax and other local authorities, filing of annual accounts.
<b>Management requirements</b>	<ul style="list-style-type: none"> <li>▫ The General Shareholders' Meeting and the Supervisory Board (not required if there are less than 10 shareholders).</li> <li>▫ Single Director or a Board of directors headed by the General Director, or another body stipulated in the Charter.</li> <li>▫ Audit Committee or Internal Auditor (if there are fewer than 100 shareholders).</li> </ul>	<ul style="list-style-type: none"> <li>▫ The Participants' Assembly.</li> <li>▫ Single Director or the Board of Directors headed by the General Director.</li> </ul>
<b>Statutory audits</b>	There is a requirement to submit an annual audit report to the State Securities and Stock Market Commission.	Required by the law, but no penalties for failure to conduct the audit. In practice, most LLCs do not conduct audits
<b>Risks</b>	Liquidation if the net assets are less than the minimum requirements of the law.	<ul style="list-style-type: none"> <li>▫ Liquidation if the net assets are less than the minimum requirements of the law.</li> <li>▫ Participants may withdraw from the LLC at any stage with a three month notice.</li> </ul>
<b>IFRS</b>	Shares are treated as equity investment.	Because contributors may withdraw contributions at any time, financial reporting standards may require investment to be reported as loans.



## 7 Labour relations and social security

### Investor considerations

- Ukrainian labour law still contains many socialist concepts, including a strong sense of the employee's right to work and restrictive conditions on employment.
- Labour records must be kept for up to 75 years.
- Employer contributions to various social security funds exceed 36% of an employee's gross income (cap of approximately USD 1,600 per employee per month applies to the income subject to contributions).

### 7.1 Labour relations and the Labour Code

#### Employer / employee relations

In Ukraine, employment relations are generally governed by a Labour Code adopted in 1971, when Ukraine was still part of the Soviet Union. The Labour Code is historically employee-friendly and contains many socialist concepts, including a strong sense of the employee's right to work, and many instruments for protection of employees.

Potential employers should familiarise themselves with the general provisions of the Labour Code and other pieces of labour legislation. As is the case with many other countries, complying with local labour legislation tends to be one of the bigger challenges facing investors.

Although employers can enter into individual labour contracts with employees, the conditions of such agreements may not be worse than those guaranteed by the labour legislation. Contracting out of the provisions of labour legislation is not possible.

When disputable issues arise, they tend to be pursued directly with the courts. In practice, if employers are aware

of and respect the rights of employees, no significant issues for employers should arise in Ukraine.

## Unions

In Ukraine, Unions have a visible place in the labour market and there is a specific law for Trade Unions. They are easy to establish and are granted certain benefits by legislation. The largest Trade Union organization in Ukraine is named the Federation of Trade Unions of Ukraine (FPU). This Union claims to unite more than ten million trade union members and provides for a variety of approaches to the protection and status of Trade Unions. For instance, approval of the Trade Union is required in some cases before termination of employment relations with the employee, or before overtime hours can be implemented.

The Labour Code recognises Labour Agreements, and employers must establish such agreements if demanded by employees.

If a Labour Agreement is established, it will be binding for all employees, even non-union members. The trade union will also monitor the employer's compliance with the agreement.

## 7.2 Working conditions

### Salaries and wages

Minimum salary levels are prescribed in the annual budget law. According to the 2009 Budget Law of Ukraine, the minimum salary as of January 1, 2010, is set at UAH 869 (approximately USD 110) per month. The minimum salary level is increased on a regular basis.

Wages and other payments to Ukrainian employees should be paid in local currency (hryvnia). Salaries should be paid at least twice each month. Wages and other payments to foreign employees may be paid in foreign currency on a monthly basis.

### Working hours

In general, working time is restricted to 40 hours per week, with a five-day working week. An employer may introduce a six-day working week. In such a case, employees should not work more than seven hours per day.

Under labour legislation, employers may introduce overtime in exceptional cases. The amount of overtime may not exceed four hours in any two-day period or 120 hours per year. The legislation also requires overtime to be paid at double rates.

The Labour Code also contains provisions that entitle some employees to work shorter weeks. The working week is limited

to 36 hours for employees performing work under harmful working conditions while the night shift is one hour shorter (as is the day before a national holiday). Employers must also, if requested, grant a shortened working day or working week at proportional pay to pregnant women or women with a disabled child or a child under 14. The law also grants a shortened working day or working week also to those taking care of a sick family member based on a doctor's recommendation.

### Paid holidays

There are ten official public holidays in Ukraine per year. An employee's minimum annual holiday entitlement is 24 calendar days. This increases to 31 calendar days for employees under the age of 18. When determining the length of vacation for purposes of complying with the Labour Code, weekends during the vacation period are counted as vacation days, but public holidays are excluded.

The legislation also requires additional leave to be granted to:

- women having two or more children under the age of 15;
- women having a disabled or an adopted child;
- single parents.

Employees engaged in part-time studies may also be entitled to additional vacation leave.

Paid maternity leave is required for up to 70 calendar days before and up to 56 calendar days after childbirth. Payment is funded by the Social Security Fund, and is based on levels of income used for social security contribution purposes (i.e., it is capped).

### Equal opportunity and disabled employees

The Constitution of Ukraine and the Labour Code both preclude discrimination based on race, colour of skin, political, religious and other beliefs, sex, ethnic and social origin, property status, place of residence, linguistic or other characteristics.

In addition, Ukrainian law requires enterprises employing 8 or more individuals to employ a minimum number of disabled people - 4% of their total headcount but no less than one individual. If an employer does not meet this quota, it is required to make a payment to the Fund for the Social Protection of Disabled People equivalent to the company's annual average salary (50% for companies with 8 to 15 employees) for each working place that is not occupied by a disabled person. Calculation of the quota should be made every month.

## Termination of employment

Employment agreements are generally concluded for indefinite periods. Employment contracts, since they are a special form of employment agreement, may be concluded for fixed periods with certain types of employees (e.g., the CEO of the company). Employees on indefinite term employment agreements may terminate the employment relationship at any time by giving at least two weeks' notice whereas for fixed term employment contracts, an employee may terminate employment only on grounds of sickness or disability preventing him/her from performing his work under the contract. The employment contract may also be terminated according to the conditions specifically stipulated in it, or other conditions stipulated by legislation.

The Labour Code permits employers to terminate employment relationships at their initiative on the grounds of reorganisation of the company; failure of the employee to perform his/her duties or loss of trust in employees involved in financial matters (theft, etc). It is important, however, to ensure that all termination formalities are complied with in full accordance with legislation. Among these, the employer must follow the requirement for two months' termination notice prior to actual termination of employment relations.

In practice, employment is quite often terminated by mutual agreement and it is rare for disputes to arise.

Under employment legislation, the retirement age is 55 years for women and 60 years for men.

## 7.3 Social security system

### Coverage

The social security system in Ukraine covers pensioners, workers and their dependents for work-related accidents, illness, retirement, death and disability benefits, sickness and maternity benefits, medical care, severance benefit, and for child and family allowances.

### Contributions

Mandatory contributions to the Ukrainian social security and pension funds apply to all salaries paid through the payroll of a Ukrainian entity or a Ukrainian representative office of a foreign entity. In addition, it is possible for individuals to contribute voluntarily to the State Pension Fund, the Employment Insurance Fund and the Social Security Fund (up to the cap established by the law).

The taxable base for contributions (both employee and employer) is capped. For 2010, the cap is set at 15 times the subsistence minimum set for able-bodied individuals (approximately USD 1,700 per month).

Contributions (both employee and employer) are not due on income that is not subject to personal income tax.

### Employees' contributions

For employees of Ukrainian entities (including those employed by a representative office), social security contributions are withheld by the employer at source from salary payments, and remitted directly to the appropriate authorities.

For 2010 Ukrainian and foreign national employee's contributions (based on gross remuneration) are as follows:

- 2% to the State Pension Fund;
- 1% to the Social Security Fund;
- 0.6% to the Employment Insurance Fund.

Foreign nationals remaining on a foreign payroll are not liable to pay social contributions in Ukraine.

### Employers' contributions

Ukrainian employers are liable to pay social security contributions in respect of all Ukrainian and foreign national employees.

For 2010, the following rates apply to gross remuneration:

- 33.2% to the State Pension Fund;
- 1.4% to the Social Security Fund;
- 1.6% to the Employment Insurance Fund;
- 0.56% - 13.5% to the Fund for Social Insurance regarding Accidents at Work.

The rate for the Fund for Social Insurance regarding Accidents at Work is determined by the Fund's authorities specifically for each entity, and depends on the level of risk of accidents in the entity's industry sector. In most cases, the rates will be in the region of 1% to 2%.

### Penalties for non-compliance

There are severe penalties for non-compliance with social security obligations, particularly for contributions to the Pension Fund:

- If the Pension Fund identifies that income subject to contributions has been underreported, the penalty for the first offence is 100% of the taxable base for contributions (i.e., the employee's income, not the amount of contribution). For subsequent underreporting identified within one year of the first offence, the penalty is 300% of the underreported income.

- Contributions additionally calculated either by the Pension Fund or employer should be paid together with a penalty of 5% of that additional contribution for each month of delay.
- Late reporting attracts a 10% per month penalty for the first offence, and 20% per month for subsequent offences within one year of the first offence, based on the contributions made or to be made.
- Late payment is subject to a penalty of 50% (for advance payments) and 10% (for a final payment).

In addition, interest on late payments is charged at the rate of 0.1% per day, based on the amount of underpaid contributions starting from the day after the deadline for payment till the date of payment (inclusive).

Penalties are imposed separately by the Social Security Fund, Employment Insurance Fund, and the Fund for Social Insurance regarding Accidents at Work. As the penalties for these funds are based on salary (rather than contribution levels), the potential penalty exposures may be significant. There is no statute of limitation period in respect of contributions to social funds.

## 7.4 Foreign personnel

### Tax ID number

All taxpayers, including foreign nationals, must register with the State Registry for Individuals. Every individual is assigned a personal tax ID number, which is necessary for various transactions such as renting apartments, opening bank accounts, and paying personal income tax. Receiving the ID number is one of the conditions for obtaining the right to claim a tax credit (deduction) in respect of certain expenses incurred by a taxpayer during the reporting year.

### Residence permit / registration with the immigration authorities

Foreign nationals arriving legally in Ukraine may temporarily stay in the country on the basis of their passport and relevant entry visa (if required). The stamp affixed to the foreign national's passport by Frontier Service officer at the first entry to Ukraine is considered an automatic registration for the period of 90 days (cumulatively) in Ukraine.

If a foreign national stays in Ukraine for more than 90 days (cumulatively) during a 180-day period, his/her passport must be registered with the local immigration authority (Ukrainian abbreviation VGIRFO, formerly OVIR). A written application of the foreign national and the inviting party must be submitted

not later than three working days before the 3-month period expires. The extended registration will be evidenced by a registration stamp affixed to the foreign national's passport.

Foreign nationals that obtained Ukrainian work permits (see below) should obtain a temporary residence permit instead of a registration.

### Work permit

Ukrainian employers must obtain work permits for foreign nationals who are either directly employed by local companies, seconded to work in Ukraine by foreign companies, intra-company cessionaries (i.e., the foreign nationals assigned to work in Ukraine on temporary basis at their WTO residing employer's commercial presence in Ukraine), or providing services to affiliates.

A work permit is generally issued for up to one year with subsequent renewal. Intra-company cessionaries may apply for a work permit valid for up to three years and eligible for renewal lasting two more years. The overall time of employment in Ukraine is not limited.

The labour authorities must consider an application for a work permit within 30 days of its date of submission.

To obtain a work permit, foreign nationals are required to provide a range of documents, including an apostilled original copy of their certificates/diplomas and a criminal clearance certificate.

Non-compliance with the work permit requirements is subject to penalties (see below), as well as potential deportation of the foreign national from Ukraine (at the employer's expense).

Work permits are not required for the personnel of representative offices of foreign companies who are employed abroad. They should be accredited with the Ministry of Economy of Ukraine which is valid for up to 3 years.

### Penalties for non-compliance with immigration legislation

According to current Ukrainian legislation, various types of non-compliance with immigration legislation may be subject to the following penalties for individuals and/or their employer:

- Fines in the range of UAH 170 – 15,000, depending on the violation.
- Summary deportation of the foreign national.
- Administrative imprisonment and property confiscation (may apply in exceptional cases).





## 8 Accounting and audit requirements

### Investor considerations

- In principle, local accounting standards should not contradict international accounting standards. In practice, there are gaps between the two, so separate books may be required.
- JSCs are subject to an annual audit requirement and must publish their annual financial statements. These requirements do not apply to LLC's.
- Tax accounting is separate from financial accounting and may require duplication of recording. Tax accounting rules are prescriptive, and operate independently of accepted accounting principles.
- The short form Chart of Accounts may be found in Appendix E.

### 8.1 Accounting

#### International Financial Reporting Standards

The Law on Accounting and Financial Reporting, effective from 1 January 2000, introduced National Accounting Regulations (Standards) (NR(S)AU). The law states that local standards should not contradict International Financial Reporting Standards (IFRS), but in practice there are gaps

between the two. As at 1 January 2010, 34 NR(S)AU standards have been adopted.

#### Ukraine accounting regulations

Ukrainian entities, as well as representative offices of foreign entities, must maintain accounting records and financial statements in accordance with NR(S)AU. Financial statements are prepared for a calendar year and relevant interim periods, and must be prepared in Ukrainian UAH as the reporting currency. The financial statements include the balance sheet,

income statement, cash flow statement, statement of changes in equity, and notes to financial statements. Financial statements should be submitted to the founders or shareholders of a legal entity, labour collectives (if required), and the state statistics authorities and registrar. Other government agencies (e.g., State Commission on Securities and Stock Exchange, NBU, State Commission on Regulation of Financial Services Markets in Ukraine) prescribe additional requirements for entities under their jurisdiction.

JSCs, bond issuers, banks, trusts, stock exchanges, investment funds and investment companies, credit unions, non-state pension funds, insurance companies and other financial institutions are required to publish their annual financial statements and consolidated financial statement in the periodical press or by distributing them in the form of individual printed editions.

The enterprise's owners or the managing director are responsible for organizing the accounting function and ensuring that all economic transactions are recorded in supporting documents, ledgers and financial statements.

### Differences between NR(S)AU and IFRS

Although NR(S)AU are generally based on IFRS, they are not identical. There are still areas for which no local standards have been introduced (e.g., accounting for government grants and disclosure of government assistance, interim financial reporting, investments in associates and joint ventures, insurance contracts, investment property, share-based payments etc.). In addition, when local standards do exist, they often lack the detail and some of the disclosure requirements found in IFRS.

NR(S)AU have less interpretative guidance, explanations and illustrations than IFRS, which inevitably leads to some confusion in the application of local standards. This undermines the comparability and quality of financial statements in Ukraine. Tax considerations also play a role in local standards. Parliament has enacted numerous tax accounting rules that operate quite independently of accepted accounting principles. For example, new buildings acquired after 1 January 2004 may be depreciated for tax purposes at a rate of 2% per quarter on a reducing value basis, and NR(S)AU 7 "Property, plant and equipment" provides for several depreciation methods, including methods stipulated by Ukrainian tax law. This is not fully consistent with IAS 16, which requires the depreciation method to reflect the pattern in which the asset's economic benefits are consumed by the enterprise.

## 8.2 Chart of accounts

According to Decree № 291 of the Ministry of Finance, all Ukrainian legal entities should use the specified chart of accounts.

The chart of accounts represents the whole system of accounts, within which each account has a title and numerical symbol, and is assigned to a specific class or group.

Small businesses, non-profit non-government organizations and foreign business entities' representative offices are permitted to use a simplified set of accounting rules. In addition to the statutory accounts, Ukrainian taxpayers need to maintain a separate set of tax accounting records.

A short form Chart of Accounts may be found in Appendix E.

## 8.3 Audit requirements

Auditing is regulated primarily by the Law on Auditing, which outlines requirements for auditing firms and auditors in individual practice, regulates auditing methodology, and sets out the legal framework of operations for the Chamber of Auditors of Ukraine (UCA) and the Professional Public Union of Auditors of Ukraine.

The UCA is responsible for approving audit regulations and standards, carrying out the certification of auditors, approving programs of professional training for auditors, and maintaining the register of auditing firms and auditors in individual practice that are eligible to provide audit services in Ukraine.

In 2004, the UCA adopted the International Standards on Auditing (ISA) as the Ukrainian standards.

Several other laws (e.g., Law on Financial Services and State Regulation of Financial Services Markets, Law on Banks and Banking Activities, Law on Securities and Stock Market, Law on Insurance) establish additional requirements for audits and auditors for selected industries.

### Audits required by law

Under Ukrainian law, audits are mandatory for a range of enterprises, in particular:

- banks;
- insurance companies;
- JSCs;
- bond issuers;
- investment funds, trusts and other financial enterprises;
- brokers and traders;
- other companies that are required to publish their financial statements.



## 9 Tax system and administration

### Investor considerations

- The Ukrainian tax system continues to develop.
- A recent World Bank study concluded that Ukraine was one of the most difficult countries out of the 183 countries surveyed to pay taxes in. This is due more to the administrative burden than the underlying tax rate.
- Individual tax residents are taxed on worldwide income (at 15%). Non-residents are taxed only on income from Ukrainian sources (up to 30%).
- Prior to late 2009 it was relatively easy to become a Ukrainian tax resident.
- Corporate profits are subject to 25% tax. Dividends are separately taxed at the shareholder level in the hands of individuals and foreign shareholders.
- There is a simplified tax system for small businesses and private entrepreneurs.
- The VAT rate is 20% and is not fully consistent with EU legislation.
- With the exception of agricultural enterprises, the fiscal year is the calendar year.
- There is a 200% penalty for failing to deduct and remit withholding tax.
- The courts and the tax authorities are beginning to look at the substance of transactions but form over substance continues to prevail.

## 9.1 Tax system

The Ukrainian tax system has developed substantially over the past 20 years, but it suffers from a lack of systematic reforms. Tax law is often poorly worded, which results in ambiguous interpretation and increases the risk of disagreements between taxpayers and tax authorities.

Ukraine is not an easy country to pay taxes in. In the recent "Paying Taxes" study released by the World Bank, Ukraine was identified as one of the most difficult countries in which to pay taxes out of the 183 countries surveyed. The study estimated that a medium-size domestic business would need to make 147 tax payments each year, and would require 736 hours per year to comply with its tax compliance requirements.

For years, there have been discussions about consolidating the various revenue laws into a single Tax Code, which should ease compliance and administration, but progress is slow.

An interesting feature of the Ukrainian tax system is a simplified or unitary tax available for many small businesses. Qualifying sole proprietors opting to use the system pay a fixed amount of tax, while eligible entities pay a fixed rate of tax based on their revenues. In both cases, the businesses are exempted from income tax, a number of other small taxes, and potentially value-added tax (VAT). The corporate tax regime is discussed in Chapter 10.1, while the regime for private entrepreneurs is discussed in Chapter 11.2.

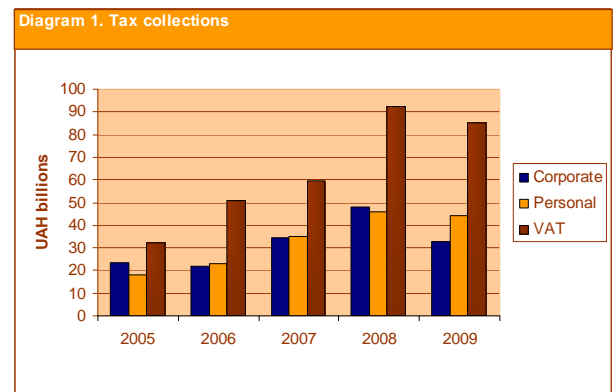
The tax authorities and courts have recently started to pay greater attention to the economic substance of taxpayers' transactions and consider the "overall picture". In a recent decision, the Supreme Court of Ukraine stated that commercial transactions need to be driven primarily by business purposes. However, the substance over form concept is still an undeveloped area in Ukraine.

In response to the economic crisis, a number of measures have been taken to support local businesses. In particular, several significant changes to the tax legislation impacting financial institutions were introduced (discussed further in Chapter 10).

## 9.2 Direct and indirect tax burden

Taxation accounts for around 72% of government revenues. More than 3/4 of this is collected through corporate income (profits) tax (CPT), personal income tax (PIT), and VAT. Tax collections have increased rapidly over the past five

years. The trend in income tax and VAT collections for the period 2005 to 2009 is illustrated in diagram 1.



Source: Ministry of Finance

As for 2009, tax revenues of Ukraine's state budget were approximately 8% behind the budgeted amount for the year.

## 9.3 Principal taxes

*On Taxation System*, the law that provides the general framework for taxation in Ukraine, provides for 28 state taxes that may be imposed. The principal taxes and compulsory payments are:

- Corporate income (profits) tax (CPT) (see Chapter 10).
- Personal income tax (PIT) (see Chapter 11).
- Value-added tax (VAT) (see Chapter 12).
- Pension Fund charge (see Chapter 10.6).
- Excise tax and import duties (see Chapter 5).
- Land tax (see Chapter 10.6).
- Stamp duty (see Chapter 10.6).

The taxation system also provides for 2 additional taxes and 12 additional duties that may be levied at the discretion of local authorities. The main local taxes affecting business are the advertising tax, municipal tax and the charge for using local symbols (these are generally immaterial).

Employers and employees must also make mandatory contributions to the state pension and social security funds. The rates and maximum contributions are set in the annual budget law and may result in a significant cost burden for employers (see Chapter 7.3 for further information). There has been widespread discussion on reducing the burden, as it is considered to have a negative impact on economic

growth. In particular, for the several years there have been numerous calls to unify all social contributions into a single social tax with the aim of simplifying tax administration, but this has not yet happened.

## 9.4 Legislative framework

### Statute law

According to the Constitution, taxes and levies, as well as penalties for non-compliance, may only be established by laws enacted by Parliament. Nevertheless, in the last few years the Ukrainian government has attempted to amend certain tax rules at its own discretion by adopting various resolutions.

Strictly speaking, the State Tax Authority (STA) does not have power to amend the law, but in practice, the STA often issues tax clarifications that are not always consistent with the law, although this can be a function of ambiguities in the law as much as anything else. Nevertheless, it is prudent to consider STA interpretations and the risk of conflict with the STA.

## 9.5 Tax treaties

As of February 2010, Ukraine has 68 effective double tax treaties. The most recent double tax treaty signed by Ukraine (but still not in force) is with Pakistan.

Withholding taxes on interest, dividends and royalties are typically reduced by the treaties. A summary of withholding rates under the various treaties is provided in Appendix C.

Taxpayers do not require confirmation from the tax authorities before claiming relief under a treaty. However, the withholding agent must hold a certificate of residence from the treaty country for the person to whom income is paid. The certificate is only valid for the calendar year of its issuance.

Currently, one of the most favourable treaties is the Ukraine - Cyprus treaty, which provides for 0% withholding tax on dividends, interest and royalties. This treaty is being renegotiated but given the reluctance of Cyprus to sign the new treaty and the unstable political situation in Ukraine, the exact date of implementation of a new treaty is uncertain.

## 9.6 Administration of the tax system

National taxes are administered by the STA. Local taxes are administered by the various local authorities.

The allocation of revenues between the state and local budgets is set out in the annual budget law. Revenues are allocated based on source, rather than by amount. For example, revenues from personal income tax, although administered by the STA, are normally allocated to local budgets. One consequence is that payments for some state taxes may need to be made to local budget accounts.

## 9.7. Registration requirements

All taxpayers are required to register with the STA and to obtain a tax ID number. Registration is undertaken through the local tax office where the individual or business is located. Representative offices of foreign entities (both commercial and non-commercial) are also required to follow the registration procedure. Registration with the tax authorities usually takes up to 10 calendar days.

Without a tax ID number, it is not possible to open a bank account in Ukraine.

## 9.8 Tax returns and payments

Personal income tax returns are filed for each calendar year, but individual taxpayers whose entire income is subject to withholding tax at source (e.g., salaries) are not required to file income tax returns. Personal income tax returns must be filed by 31 March of the following year.

Corporate income tax returns are filed on a quarterly basis, and returns must be filed within 40 calendar days of the end of each quarter. Resident companies and non-resident entities with a permanent establishment in Ukraine must keep records that comply with tax rules.

Withholding taxes must be paid to the state not later than the date the income is paid.

Value-added tax returns are generally filed on a monthly basis. The return must be filed within 20 calendar days of the last day of each month. If the filing date for any return falls on a weekend or a public holiday, the return should be filed on the following working day.

Tax returns may be filled either in paper or electronic form at the taxpayer's discretion.

Payment of taxes due must be made within ten calendar days from the day on which the return is required to be filed or the assessment is issued. Payments are normally made through the taxpayers' bank accounts.

## 9.9 Assessments

Taxpayers file returns and execute payments on a self-assessment basis. If the tax authorities determine that the tax shown on the return is incorrect, they may assess taxes within 1,095 days (three years) from the deadline for filing a return or the date on which the return is actually filed, whichever comes later.

There is no limit on the period in which an assessment may be made if a taxpayer has deliberately evaded tax (if proven in court) or when a taxpayer fails to file a return. The tax authorities will also charge significant penalties for late filing or understatement of tax liabilities (see Chapter 9.13).

## 9.10 Appeals

Assessments may be appealed administratively or through the court system. The initial appeal is made to the local tax office that issued the assessment. If an appeal is rejected, a taxpayer may appeal in turn to the regional and national office.

An administrative appeal must be filed to the relevant level of the tax authorities within ten calendar days of receiving an assessment or official advice that an administrative appeal has been rejected at a lower level.

The tax authorities must respond to the appeal within 20 calendar days. If they fail to do so, the appeal is deemed to be decided in favour of the taxpayer. The 20-day period may be extended by up to 60 days, but only if the authorities advise the taxpayer in writing within the initial 20-day period.

At any stage of the process, or if the national office rejects the appeal, a taxpayer is entitled to pursue action through the general court system (there is no separate tax court system). Submitting an appeal suspends the requirement to pay the assessed tax, as well as the accrual of interest and

penalties. Interest and late payment penalties will apply only if the taxpayer fails to pay the taxes by a revised due date after the appeal is finally resolved.

## 9.11 Withholding taxes

It is very important to ensure that withholding taxes are properly deducted and accounted for. Businesses generally have an obligation to withhold tax on payments to individuals (including sole proprietors) and payments to non-residents. 200% penalties apply for failure to withhold tax. Withholding tax must be remitted to the authorities no later than the date when the payment is made to the income recipient.

- Passive income (dividends, interest, royalties) from Ukrainian sources that is paid to non-resident entities is generally subject to 15% withholding tax.
- Other payments, including "engineering services," lease payments, agency and brokerage fees, are also subject to 15% withholding tax, but payments for most other services are not subject to withholding.
- 15% withholding tax applies to income on sale of real estate and on profits from sale of securities.
- Payments for freight services (including sea freight) are subject to 6% withholding tax.

Withholding tax rates may be reduced under a relevant tax treaty.

Payments to non-resident persons for advertising services performed in Ukraine are not subject to withholding. However, the resident payer is required to pay a 20% tax based on the value of such services.

A resident payer is also required to pay 12% tax if a payment is made to a foreign insurer or reinsurer whose rating of financial reliability does not meet requirements set by the authorised state agency. As the taxes on advertising and insurance are levied on the resident party, they cannot be relieved using a tax treaty.

## 9.12 Tax audits

The tax authorities may carry out scheduled audits once each year. Business entities must be notified of the audit in writing at least ten days before the scheduled audit. For normal business entities, the scheduled audit should be carried out within twenty business days, although the period may be extended by up to ten days.

In addition, the tax authorities may perform out-of-schedule audits in any of the following circumstances:

- A taxpayer does not respond within ten days to a request for information from the tax authorities when the tax authorities are cross-checking information, or when the cross-audit of another business entity has revealed a violation by the taxpayer.
- A business entity does not file tax returns on a timely basis.
- A taxpayer initiates an appeal process against an assessment.
- A business entity is reorganized or liquidated.
- A tax police investigation requires that a taxpayer's accounts be audited.
- A taxpayer claims a VAT refund for an amount exceeding UAH 100,000.

The duration of an out-of-schedule audit cannot exceed ten business days. Before starting an audit, the tax inspector must present a written order to the taxpayer, outlining the scope and period of the tax audit. The legislation prescribes that out-of-schedule tax audit should be authorized by a court; however, in practice tax authorities usually disregard this requirement.

## 9.13 Penalties

Administrative penalties (charged to officials or individuals) are normally specified in terms of a multiple of the monthly "non-taxable allowances" (currently UAH 17).

Multiple tax penalties may be imposed, and total tax penalties may be up to 100% of the tax underpaid (or 200% in respect of withholding tax).

### Late filing

In addition to a nominal penalty for late filing, if the tax authorities assess tax when a taxpayer fails to file a return, penalties could reach up to 50% of the tax assessed, depending on the period of delay.

### Late payment of tax

If a taxpayer does not pay the amount of tax shown in its tax return on time, or fails to pay an assessment within the time shown on the assessment notice (or if the taxpayer appeals the assessment, within ten days of the final resolution of the appeal), penalties are imposed as follows:

- 10% of the underpaid tax for delays of up to 30 calendar days;
- 20% of the underpaid tax for delays of 31 to 90 calendar days;
- 50% of the underpaid tax for delays exceeding 90 calendar days.

### Understated tax liabilities

If during an audit the tax authorities determine that the tax liability shown in the taxpayer's return is understated, they will impose penalties of up to 50% of the tax assessed, depending on the timeframe involved.

### Tax evasion

In addition to the above, if a taxpayer (or officials of the company) is convicted of tax evasion, a penalty of 50% of the tax due will be imposed. This penalty is assessed if a taxpayer understates its tax liabilities by a "large" amount. For 2010, the Criminal Code defines "large" as any amount over UAH 907,500. Taking into account penalties imposed due to the understated tax liability, a total penalty of 100% may apply.

The individual taxpayer (or officials) may also be subject to criminal penalties. For criminal tax evasion, fines of up to UAH 605,000 for 2010 may be imposed in combination with prohibition from occupying certain positions or engaging in certain activities for up to three years, or imprisonment for up to 10 years.

### Failure to withhold and pay tax

If a taxpayer does not pay tax when it is a mandatory condition for the sale of goods, or a taxpayer fails to withhold tax when required, a penalty of 200% of the deficient tax is imposed.

### Arithmetic or methodological errors in tax return

If the tax authorities determine during a "desk review" that arithmetic or methodological errors in a tax return resulted in an understatement of tax liabilities, a penalty will be applied of 5% of the additional tax assessed.

### Interest for late payments

When tax is not paid on time, interest for late payment is charged on a daily basis in addition to the above penalties. The rate is 120% of the NBU prime rate that is effective at the date the payment was due or the date that payment was made, whichever is higher.

For amounts calculated on the tax return, interest accrues from the date the tax was due. When the tax authorities assess tax, interest accrues from the due date for payment shown on the notice. Interest is charged on the entire outstanding tax, including penalties.

### Voluntary disclosures

If a taxpayer voluntarily discloses and pays the underpaid tax before the tax authorities commence an audit there will be a 5% penalty applied to the amount of under-declared tax. No further late payment penalty will be charged.

To apply this rule, a taxpayer must have filed an amended tax return or adjust tax liability in a tax return for the next tax period.

### Penalties during appeal

Penalties and interest do not accrue during the appeal process (see Chapter 9.10).

## 9.14 Tax clarifications

Tax clarifications may be sought from the tax authorities, and the tax authorities are required to issue such clarifications. Tax clarifications are not legally binding and do not provide solid protection against tax assessments and penalties. However, in practice tax clarifications are useful in resolving disputes with local tax authorities regarding uncertainty in the tax legislation.





## 10 Taxation of corporations

### Investor considerations

- The standard corporate tax rate is 25%.
- Qualifying small companies may opt to use a simplified tax system (with very favourable tax rules).
- There is no group consolidation.
- Depreciation is based on the reducing balance method; relatively generous rates are available.
- Losses may be carried forward indefinitely.
- When companies pay dividends, they are generally required to pay advance corporate tax (ACT) at the 25% CPT rate. This is in addition to potential withholding taxes of up to 15%.
- Taxable income expenses are based on the "first event rule".

### 10.1 Corporate tax system

#### Companies

Ukrainian entities and foreign entities doing business in Ukraine through a permanent establishment are liable for corporate income tax. The standard rate is 25%.

Special rules apply to Ukraine insurance companies. Net insurance premiums (gross premiums less amounts paid to reinsurance companies) are taxed at 0% for long-term life insurance premiums and pension insurance premiums, and 3% otherwise. Profits earned by insurance companies from non- insurance activities are taxed at the standard rate.

## Territoriality

Resident entities are legal and business entities whose personality or existence is established under the laws of Ukraine (i.e., incorporated in Ukraine). Non-resident entities are those whose existence is established under foreign law.

Resident entities are liable to Ukrainian tax on their worldwide income. Foreign taxes should be available for credit against Ukrainian tax liabilities, but may be difficult to obtain in practice.

Foreign entities are liable to Ukrainian tax only on income from sources in Ukraine. In broad terms, income will have a source in Ukraine if:

- The income arises from activities performed or property located in Ukraine; or
- In the case of dividends, interest, royalties and other passive income, the income is paid by a resident of Ukraine.

Professional services, except specific engineering services, are not treated as having a Ukrainian source and thus are not subject to withholding.

## Accounting period (compliance)

The reporting year for companies generally follows the calendar year. The exception is for agricultural manufacturers, which report based on a 30 June year-end.

Returns are submitted and payments of tax are made on a quarterly basis, generally reflecting accumulated taxable profit for the year to date.

## Permanent establishments

The domestic definition for a permanent representation essentially adopts the definition for permanent establishment found in the OECD Model Tax Convention, but with the addition of stronger agency tests.

When a foreign company conducts business in Ukraine through a permanent establishment, taxable income should be determined on the same basis as for domestic entities. If it is not possible to determine taxable profit in Ukraine based on the "direct" method (taxable income less deductible expenses), the allocation method or notional method may apply.

The allocation method requires the taxpayer to allocate a portion of its worldwide income and expenses to Ukraine. This method is difficult to apply in practice and is rarely used. The tax authorities have a preference for the notional

method, which involves applying a notional margin of 30% to gross revenues earned in respect of activities in Ukraine (generally funds received by the local permanent establishments and representative offices).

Ukraine has no special tax rules for non-commercial representative offices established to engage in liaison type activities. Such offices are subject to the normal corporate income tax, but an exemption from income tax may be available under a relevant tax treaty if the activities of the representative office are not sufficient to constitute a permanent establishment for the foreign entity.

## Special tax regimes

Qualifying small legal entities may opt to use the simplified taxation, accounting and reporting system. VAT-registered entities pay 6% of their sales proceeds under the simplified tax system, while non-VAT-registered entities pay 10%.

Agricultural producers are entitled to use a very favourable tax regime provided certain requirements are met. The main criterion requires that income from the sale of its own agricultural products constitutes not less than 75% of its total gross revenue.

## Holding companies and group taxation

There is no system of group taxation in Ukraine. All members of a group must file separate tax returns.

Dividend income received from another Ukrainian company is not subject to tax. Companies deriving more than 90% of their income from domestic dividends are exempt from paying advance corporate tax (see below).

Cost-sharing and similar intra-group payments other than remuneration for the services actually rendered may not be deductible.

## 10.2 Incentive regimes

Apart from small businesses and agricultural producers, Ukraine currently has very few incentives, although some are available. The following businesses are entitled to benefit from them:

- The publishing industry.
- Investment funds.
- Enterprises selling domestically produced energy-saving goods in Ukraine, enterprises adopting energy-saving projects (up to 50 % of profits may be exempt).

Starting from January 2010, a tax exemption is available for producers of electric and heat energy generated from bio-energy fuel as well as for producers of bio-energy powered domestic equipment. Tax incentives are also available for producers of methane gas.

Certain tax incentives have also been granted to UEFA and its related companies during the preparation and hosting stage of the 2012 UEFA European Football Championship in Ukraine.

Ukraine does offer generous depreciation rates for most fixed assets, i.e., property plant and equipment (see Chapter 10.4).

## 10.3 Gross income

### Business profits

Taxable profits are defined to be "adjusted gross income" less "allowable gross expenses" and depreciation charges.

Adjusted gross income encompasses all revenues received by a taxpayer from all economic activities, unless the revenues are expressly exempted under the law. Allowable gross expenses encompass all expenses incurred in relation to "business activities," unless a specific provision in the law restricts the deduction. "Business activities" are defined in the law as "any type of activity carried out by a person, aimed at making profits in the pecuniary form and creating tangible and intangible assets, provided such activity is regular, stable, and substantial."

There are significant differences between tax and financial accounting rules. Consequently, it is common for companies to prepare separate financial and tax accounts, which is very time consuming. The recent World Bank "Paying Taxes" study estimated that a medium-sized domestic business would require 736 hours per year to comply with its corporate tax compliance requirements.

### Accounting for income

For all taxpayers income should be recognised on the date on which payment is received, or on which goods or services are supplied, whichever comes first (the "first event rule"). However, for 2010 (and 2009), as an anti-crisis measure Ukrainian banks should recognize taxable income from lending on a cash-basis (lending income of banks accrued during this period that remains outstanding as at 1 January 2011 should also be taxable on a cash basis).

For goods, the date of supply is generally the date of shipment. For services, the practice in Ukraine is for the parties to a services contract to sign an "acceptance act"

document once the services are delivered, and this is generally considered to be the date of supply.

## 10.4 Deductibility of expenses

### Business expenses

Expenses incurred in the furtherance of a taxpayer's business activities should be deductible, unless a specific provision in the law says otherwise (see below).

For VAT-registered persons, revenues and expenses are calculated without VAT. For non-VAT-registered persons, the VAT component of any expenses will be included in deductible expenses.

Research and development expenses other than those subject to amortization are deductible when incurred, provided they are business-related.

For the 2010 tax year, banks will be entitled to a tax deduction on all loss provisions (including interest, commissions and in respect of all securities). For the 2011 tax year, there will be a deduction limit of 80% on such provisions. Other financial institutions are entitled to a deduction of up to 80% of all loss provisions. Prior to 2004, there was a 10% limitation in place.

### Non-deductible expenses

The following are the main items that are not deductible for corporate income tax purposes:

- Expenses that are not supported by relevant documents (e.g., contract, voucher, receipt, etc.).
- Expenses incurred for receptions, presentations, entertainment, and the provision of free samples and services for advertising purposes in excess of 2% of the taxpayer's taxable profits for the previous year (unless the taxpayer is in the business of providing such services).
- Insurance premiums (other than for medical, pension and mandatory insurance) in excess of 5% of total deductible expenses from the beginning of the year up to the end of the reporting period.
- Expenses for professional education and training, etc., in excess of 3% of employee compensation for the period.

- Business trip expenses for individuals that are not employees. Expenses on business trips for employees are deductible within the limits set by the Cabinet of Ministers of Ukraine.
- Expenses related to the provision of employees with uniforms, safety clothes and shoes, as well as food, are non-deductible if the amount exceeds the norms established by the Cabinet of Ministers of Ukraine.
- Payments in respect of goodwill, and amortization of goodwill.
- Expenses for car parking and the maintenance of cars (in addition, only 50% of payments under an operating lease for cars and expenses relating to the purchase of fuel and lubricants for cars may be deducted).
- Expenses for provision of warranty services in excess of 10% of the value of goods sold.
- Expenses related to repairs to fixed assets are subject to depreciation in excess of 10% of the aggregate book value of all groups of fixed assets as of the beginning of the reporting period (the excess is capitalised and is subject to depreciation).
- Charitable donations and contributions to non-profit organization are only deductible within certain limits.
- In addition to the above, payments for goods or services to foreign entities in listed jurisdictions operating offshore tax regimes (37 tax haven jurisdictions are listed) have limited deductibility. 85% of the amount of such payments are deductible, unless evidence is shown that the entity is subject to the ordinary tax rules of that jurisdiction (i.e., it does not benefit from the offshore tax regime).

## Accounting for expenses

The general rule is that expenses should be recognised on the date when goods or services were received, or the date when payment was made, whichever is earlier. When payment is made to a non-resident, a tax-exempt entity or an entity paying tax at reduced rates (e.g., a small business that has opted to pay the unitary tax), expenses are recognised on the date on which goods or services were received.

## Depreciation

Assets costing more than UAH 1,000 and with a useful life exceeding one year are subject to depreciation. Depreciation is determined on a quarterly basis, and is computed using the reducing-balance method for specific "

assets" (groups) of assets. Since 2004 taxpayers have been permitted to adopt any depreciation rate up to the following maximum quarterly rate:

Description of fixed assets	Depreciation rate
Group 1: Buildings, constructions, premises	2%
Group 2: Motor transport, spare parts, furniture, household electronic, optical and engineering devices and tools	10%
Group 3: All other assets, except Group 1, 2 and 4 assets	6%
Group 4: Computers, telephones, etc.	15%

Intangible assets may be amortized using the straight-line method over the period of the asset's lifetime, or ten years (whatever is less).

If the inflation index exceeds 10% in a calendar year, taxpayers may adjust the book value of their assets for depreciation purposes by the amount of the excess. For 2010 excess is expected to be up to 3%.

Effective January 2010, generous depreciation rates (up to 50%) may be applied to environmentally friendly new fixed assets (not used before).

## Interest

As a rule, interest will be deductible if the related debt is used to fund business activities of the taxpayer.

Ukraine does not have thin capitalization rules as such. Instead, there are restrictions on interest deductibility if a Ukrainian company is 50% or more owned or controlled by non-resident or tax-exempt persons, and interest is paid to those persons or their related parties. The interest so paid cannot exceed the amount of interest income plus 50% of the company's taxable profit (excluding interest income and before the deduction of interest and depreciation). Any interest paid to affiliates in excess of this limit is carried forward to future tax periods.

## Royalties and service fees

Royalties and service fees of a business nature are normally deductible payments. When service fees are made to related parties, however, the payer is required to

hold documentary evidence that the payments are for services actually rendered. The amount of the payment also may not exceed the "usual" (market) price.

## Operating Leases

Lease payments on operating leases are tax deductible for the lessee. The lessor is enabled to claim a deduction for depreciation of the leased assets.

## Financial Leases

Financial leasing is treated for tax purposes as if a sale had been made. The lessee would include the value of the property in the relevant group of fixed assets and claim depreciation charges. The lessee would also deduct the interest and commission elements of the lease payments in the period in which they are payable. The lessor would recognize taxable income for the total principal amount of the lease when the asset is transferred, and would recognise the interest and commission element of the payments over the term of the lease.

A lease is treated as a financial lease if it meets any of the following conditions:

- The leased property is transferred for a period during which at least 75% of its acquisition cost would be depreciated under tax depreciation rules, and the lessee is obliged to acquire title to the property during or at the end of the lease period.
- The sum of the lease payments equals or exceeds the acquisition cost of the property.
- The leased property has already been more than 50% depreciated by the lessor, and the lease payments (excluding the financing component using the discount rate of the NBU) equal or exceed 90% of the normal price for the property.
- The property has been manufactured to the order of the lessee and cannot be used by other entities when the lease expires because of the property's process and quality features.

Even if a lease meets one (or all) of these conditions, the parties may still agree to treat the lease as an operating lease for income tax purposes. If they do so, they must continue to treat it as an operating lease throughout the term of the lease.

## Employee remuneration

Employee remuneration is generally tax deductible. This rule applies to costs set out in a labour agreement (employment contract, collective agreement).

When an individual and members of his family own 20% or more of the shares in a company, compensation paid to those individuals cannot be deducted in excess of usual (market) compensation.

## Losses

Tax losses may be carried forward indefinitely. In practice, the Parliament and/or STA attempt to limit the availability of unrealized losses.

## 10.5 Special tax rules

### Dividends – Advance Corporate Tax (ACT)

Companies paying dividends are generally required to pay ACT at the standard rate (i.e., 25 %). ACT is available for the company to offset future corporate income tax liabilities. If the ACT is not able to be used in the year the dividend is paid, it is carried over to future income years, but cannot be refunded.

ACT is not paid by companies deriving more than 90% of their income from dividends.

Dividends derived by a Ukrainian entity from another Ukrainian entity are exempt from corporate tax, whereas dividends received from non-residents are taxable.

Companies must also deduct withholding tax from dividends paid to individuals and foreign entities. For dividends paid to resident or non-resident individuals, or to foreign entities (including those with a permanent establishment in Ukraine), the standard rate is 15%. A lower rate may apply under a relevant double tax treaty.

## Securities

Income from securities is calculated separately from other income, and is based on the so called "pooling method". Taxable income is determined by deducting the aggregate cost of acquiring each class of securities from the aggregate proceeds from selling such securities. If aggregate acquisition costs for the year exceed aggregate sales proceeds, the excess is carried forward and applied against sales of securities in subsequent years.

## Foreign exchange

Realised and non-realised foreign exchange gains and losses related to foreign currency loans are taxable/deductible.

Conversely, the tax authorities tend to disallow deductions of foreign exchange losses realized as a result of the acquisition of goods, although there are a number of arguments to support the deductibility of such costs.

## Inventories

Revenues received from the sale of inventories will be included in taxable income based on the "first event rule", i.e., the date of receipt of payment or shipment of goods, whichever occurs first.

Expenses incurred by a taxpayer on the purchase of goods from a non-resident are recognized for tax purposes upon actual receipt of such goods, regardless of the settlement date.

Notwithstanding the "first event rule", the taxpayers should calculate an increase/decrease of the book value of goods purchased at the end of each reporting period (i.e., quarterly). If the book value of stocks at the end of the reporting period is less than their book value at the beginning of the reporting period, the difference is included in the deductible expenses of the taxpayer in this reporting period. The excess book value of goods at the end of the reporting period over their value at the beginning is included in taxable income.

Inventories received or distributed free of charge are not taken into account for the above purposes.

Inventories may be valued for tax purposes using any of the following methods:

- Identified value of the appropriate inventory unit.
- Weighted average value of uniform inventories.
- First-in-first-out (FIFO) value of inventories.
- Target expenses.
- For inventories sold on a retail basis, the inventory sales price.

The selected method must be applied consistently for inventories having the same designated purpose and utilisation conditions. The method must also be applied consistently throughout each income year.

## Bad and doubtful debts

To claim a deduction for bad or doubtful debts, a taxpayer must initiate an action for collection. A deduction for bad or doubtful debts is allowed if:

- The creditor applies to the court with a claim for debt collection or for initiating bankruptcy proceedings.
- The debtor still has not paid 90 days after the sale, the creditor attempts to collect the debt through the pre-court dispute settlement process, and either: (a) the debtor sends a notice accepting the claim; or (b) the debtor does not receive an acceptance notice within one month.
- The creditor has a note of execution for collection executed by a notary.

In practice, the tax authorities allow the deduction of a bad or doubtful debt only if all the above measures are executed.

If the taxpayer subsequently recovers an amount that has been deducted as a bad or doubtful debt, the amount recovered is included in taxable income.

When a creditor pursues action to recover a debt, and the debtor fails to pay, the debtor is required to recognise income either 90 days after the deadline for payment under the contract or accepted claim, or 30 days after the court resolution or the execution of a note of execution by the notary. If the debt is subsequently repaid, the debtor may claim a deduction at the time of repayment.

## Other special tax rules

Special rules are available to deal with the recognition of income/expenses from long-term construction contracts and shipbuilding contracts.

Those agricultural enterprises which are subject to the special tax regime under the VAT Law can deduct the negative difference between output and input VAT. The positive difference is subject to the standard corporate tax rate.

## 10.6 Related party transactions

Special rules apply to transactions between related entities. Related entities are:

- a legal person that exercises control over a taxpayer, is controlled by a taxpayer, or is under common control with a taxpayer. Control is defined to include an interest of 20% or more in an entity;
- an individual (or family member of that individual) who exercises control over a taxpayer; or
- a company official (or family member of that official) who is authorized to execute binding legal agreements in the name of a taxpayer.

Transfer pricing rules also apply to non-residents and those paying taxes at reduced rates in Ukraine (e.g., payers qualifying as small companies under the simplified tax system etc).

Ukraine's transfer pricing rules are based on the arm's length principle. The law places strong emphasis on the comparable uncontrolled price (CUP) method, meaning that alternative approaches to pricing are unlikely to be easily accepted by the tax authorities. If it is not possible to determine the usual price because information on comparable transactions is absent or not publicly available, the law deems the contractual price to be the usual price.

If questioned by the tax authorities, taxpayers are required to justify their prices. Nonetheless, the onus is on the tax authorities to demonstrate that the contractual price does not satisfy the usual price requirement.

## 10.7 Transactions with land

### Corporate tax

Special rules apply to expenses/losses arising from the purchase/sale of land. Expenses related to the acquisition of land are neither depreciated nor deducted. If the land plot is sold in the future, the purchase cost is offset against the proceeds.

Losses incurred in the disposition of land are non-deductible.

### Land tax

Land tax is assessed annually for the following year and is paid monthly in equal instalments by the owners or users of

land. The rate of land tax depends on the category, location and existence of state valuation of each particular land plot.

## 10.8 Other taxes

### Special Pension Fund charges

The following special charges are payable to the State Pension Fund:

- Charge on the purchase of foreign currency in the foreign exchange market (withheld by the bank). As of January 2010, this charge amounts to 0.5 %.
- 3% charge based on the transfer value of a car.
- 1% charge on the acquisition of real estate payable by individuals and legal entities that purchase real estate.
- 7.5% charge on mobile communication services.

There are also a number of other business activities that require contributions to be made to the Special Pension Fund.

### Stamp duty

Stamp duty is imposed on certain actions, including notarisation of contracts and the filing of documents with courts. In most cases, the amounts involved are nominal, although there are exceptions. Operations carried out at commodity exchanges and sales of real property attract a stamp duty of 1%.

### Excise tax

Excise tax is payable on cars, alcoholic beverages, tobacco products, beer, petrol and diesel fuel, whether imported or produced domestically. Rates of excise duty are specific. A list of selected rates can be found in Appendix D.

### Charge on environmental pollution

Environmental pollution charges are imposed on any legal entity that discharges contaminants into the environment (air or water) or disposes of wastes. The actual rate depends on the type and toxicity of each contaminant.

The law also establishes maximum concentrations for contaminants. If the maximum concentration is exceeded, the charge rate is multiplied by five.

### Local taxes and duties

The principal local taxes and duties affecting business are:

- *Advertising tax.* This tax is payable by legal entities placing advertisement in mass media, on outdoor advertising or through other means. The maximum rate of advertisement tax is limited to 0.5% of the advertisement placement services cost. Advertising agencies or other entities that place advertisements should collect the tax.
- *Municipal tax.* This tax is payable by legal entities monthly and is calculated as a maximum of 10% of the individual non-taxable allowance, multiplied by the number of employees. Currently, the monthly tax is UAH 1.7 per employee.
- *Charge for use of local symbols.* The charge is payable by legal entities that, for commercial purposes, use local symbols (e.g., city emblem, name or image of architectural or historical monuments). The maximum rate of the charge is limited to 0.1% of the value of the goods/services using the local symbols that are sold.

There are 11 other local duties that may be levied at the discretion of the local authorities. Few of them apply to business entities. It is unlikely that these duties will place a significant burden on companies.





# 11 Taxation of individuals

## Investor considerations

- The tax year is the calendar year.
- Ukrainian tax residents are taxed on their worldwide income. Non-residents are subject to Ukrainian tax only on their Ukrainian source income.
- The standard tax rate for tax residents is 15%. The standard rate is applicable to most types of income, including salary income, dividends, royalties and investment income.
- Income received by non-residents as interest, royalties, dividends and (arguably) salary paid by a Ukrainian employer is taxed at 15%. Other income may be taxed at double this rate (i.e., 30%).
- Social security issues are a major cut factor in Ukraine and discussed in Chapter 7.3.

## 11.1 Territoriality and residence

Individuals are classified into two categories for income tax purposes:

- Residents are liable for tax on their worldwide income. The standard rate (i.e., 15%) is applicable to most types of income, including salary, dividends, royalties
- Non-residents are liable for tax only on their Ukrainian source income. A double tax rate (i.e., 30%) applies, except for interest, royalty, dividends and (arguably)

and investment income. Special tax rates apply in some cases specifically established by the law (e.g., inheritance, gifts, winnings and prizes, interest from deposits). Taxable income of foreign nationals who are considered to be tax residents in Ukraine are taxed in the same month.

for salary received from a Ukrainian employer. The Ukrainian tax authorities are currently challenging previously adopted interpretation of the law and try to apply the 30% tax rate in respect of employment income paid by Ukrainian employers to foreign nationals up until he/she obtains a tax residency certificate.

## Tax residence

A person is a tax resident in Ukraine if he or she has a place of abode in Ukraine. If the person also has a place of abode in another country, he is deemed to be resident of Ukraine if he has a permanent place of abode (domicile) in Ukraine but not in another country.

If the individual has a permanent place of abode (domicile) in Ukraine and another country, the person is deemed to be resident in Ukraine if his centre of vital interests is in Ukraine.

If an individual's centre of vital interests cannot be determined, the individual will be deemed to be a resident of Ukraine if he stays in Ukraine at least 183 days during the tax year (calendar year).

If residence status cannot be determined based on the previous rules, an individual will be deemed to be resident of Ukraine if he is a citizen of Ukraine.

According to the recent opinion of the Ukrainian Tax Authorities, all Ukrainian citizens are tax residents of Ukraine and subject to personal income tax, even if they reside abroad. PwC does not agree with this opinion, however, all Ukrainian individuals should be aware that failure to comply may be challenged.

An individual may also voluntarily choose that his/her main place of abode (and therefore tax residence) is in Ukraine. The law does not define the procedure for how this choice should be made, but up until January 2010 a foreign national could apply in writing to the local tax office where he/she has a place of abode asking to be considered as tax resident for a given calendar year.

## Tax registration

All taxpayers, including foreign nationals, must register with the State Registry for Individual Taxpayers, and be assigned a personal tax ID number. This number is required for various transactions such as registering Ukrainian companies, renting apartments, opening bank accounts, and paying personal income tax. Receiving the ID number is also one of the conditions for obtaining the right to claim a tax credit (deduction) in respect of certain expenses incurred by a taxpayer during the reporting year.

In practice, non-resident individuals whose income from Ukraine is exempt under a relevant tax treaty will not need to obtain a tax ID number unless it is required for the purposes other than taxation.

## 11.2 Private entrepreneurs

Individuals who are registered as private entrepreneurs (including foreign nationals having residence permits) may elect to be covered by the "single (unified) tax" regime if they meet the qualification criteria. The unified tax regime may be utilized for certain activities by private entrepreneurs employing up to ten employees and with annual proceeds from the sale of goods and/or rendering services of up to UAH 500,000 (approximately USD 62,500).

The monthly single (unified) tax is fixed by local authorities, and ranges from UAH 20 to UAH 200 (approximately USD 3 to USD 25), depending on the type of activity. Payment of the single (unified) tax relieves a private entrepreneur from other taxes such as personal income tax, VAT, social security taxes, and land tax in respect of their income earned from the entrepreneurial activities. However, the private entrepreneurs who act as the payers of the single (unified) tax may register voluntarily for VAT.

A private entrepreneur is obliged to file reports on the amount of income received and tax paid during the reporting period within five calendar days after the end of each reporting quarter. A report to the Pension Fund is filed once a year.

## 11.3 Gross income

Resident taxpayers are liable to pay tax in respect of any income received or credited/accrued in Ukraine or abroad during the reporting period, except for items specifically exempted from tax under the law.

### Employment income

All income received or credited from employment, in monetary form or in kind during a calendar year is subject to personal income tax. This includes all basic pay, overtime pay, supplemental pay, awards and bonuses, compensation for unused vacation, honoraria, taxable pensions, tax reimbursements, allowances (e.g., living, education, transportation, entertainment, and the like), fees (including directors' fees), and other income of a similar nature, whether monetary, in kind, or made by way of payment to third parties on behalf of the employee.

Additional benefits granted by employers also constitute taxable income, and include the following items:

- Accommodation or other tangible or intangible assets provided for an employee's use free of charge.
- The value of goods and food provided to employees free of charge.
- The reimbursement of an employee's personal, except for items specifically exempted from tax.
- Financial aid.
- The value of goods and services provided free of charge and the value of discounts when goods and services are sold to employees at less than the market price.

There are a number of important exceptions:

- The provision of accommodation or tangible assets for use free-of-charge is not taxable when it is a condition for performing labour functions by an employee.
- Benefits in the form of free use of vehicles do not constitute taxable income if granted by a resident employer which qualifies as a corporate profits taxpayer.
- Amounts paid by an employer in favour of an employee under any voluntary insurance constitute taxable income for the employee.
- Amounts paid by employers to educational institutions for training/re-training of employees are not taxable within specific limits.
- Expenses reimbursed by employers in respect of certain types of medical treatment and services.

## Income from independent activities

Income from independent activities is subject to the standard rate of taxation. However, individuals registered as private entrepreneurs may (as an alternative) elect to be covered by the single (unified) tax regime (see Chapter 11.2).

## Rental income

Rental income is subject to tax at the standard 15% tax rate. Such income is determined based on the contractual fee, but cannot be lower than the minimum rental fee determined according to the methodology established by the Cabinet of Ministers of Ukraine.

If the lessee is a business entity, it is obliged to act as a tax agent, and to withhold tax from rent payments to an

individual, unless that individual is registered as a private entrepreneur.

## Income from prizes and winnings

Income in the form of prizes (other than cash prizes from the state lottery) and similar winnings is taxed at double the standard rate (30%). If the prize or winnings are received in non-monetary form, the income is grossed up to determine the tax base. The tax is withheld by the entity paying the prize or winnings.

## Investment income

Income from the sale of investment assets is determined independently of other income. The gain or loss is determined for each investment asset sold (sales proceeds less acquisition cost), and then aggregated for the year. If the aggregate amount is positive, it is subject to tax at the standard 15% rate. If the aggregate amount is negative, it is carried forward and applied against investment income in subsequent years.

There are no requirements in the law for individuals to report sales income based on market values.

The following transactions are also treated as the sale of an investment asset:

- The exchange of one investment asset for another investment asset. The sales proceeds are deemed to be the market value of the shares that the individual transfers.
- The redemption of corporate rights by an issuer.

## Disposal of real estate

Revenues from the sale of real estate (including incomplete constructions) is subject to tax at either 0%, 1% or 5%, depending on the nature of the real estate and the number of real estate sales performed by the same taxpayer during a calendar year. The tax authorities endeavour to apply the 30% tax rate to income received by non-resident individuals from the disposal of property. The tax is based on the higher of the price indicated in the sale agreement and the property's value calculated by the authorised state authority.

## Disposal of movable property

Gross revenue from the sale of movable property is subject to tax at the standard rate (15%).

As an exception, one sale per calendar year of a car will be subject to a lower 1% rate.

## Inheritance and gifts

Income received as an inheritance or gift is not subject to tax if received from a resident spouse, son or daughter, parent, parent-in-law, or a spouse's children. A 5% rate applies if received from other resident testators than those stated above. A 15% rate applies if received from a non-resident.

## Proceeds from insurance

Receipts from insurance companies under the following form of insurance contracts are exempt from tax:

- Proceeds from health/accident insurance, provided the insured event is confirmed by appropriate documents.
- Proceeds from property insurance, provided the amount of reimbursement does not exceed the market value of the insured property (increased by insurance payments) and is used for repair and/or replacement of the damaged or lost property.

Proceeds from life insurance when an insured person dies are taxed on the same basis as an inheritance.

## 11.4 Tax-exempt income

Apart from the exceptions already noted, the following are the main items of income that are exempt from taxation:

- Income from investments in securities issued by the Ukrainian Ministry of Finance and prizes from state lotteries.
- Alimony received from residents.
- Shares received from capitalization of undistributed profits, if prorated.
- Interest income from deposits placed with banks and non-banking financial institutions and from saving certificates. This exemption is available until 31 December 2012.

## 11.5 Deductions

### Business

Private entrepreneurs (other than those subject to the unified tax regime) are entitled to deductions from their gross income on the same basis as corporations (see Chapter 10).

If the actual expenses cannot be documented, a standard deduction of between 5% and 60% may be applied. The actual rate of deduction depends on the type of activity (in practice, a 25% rate is most common).

### Non-business

There are no major deductions available to individuals in Ukraine. A registered taxpayer may claim a deduction (so-called "tax credit") from annual taxable income for a limited amount of documented expenses incurred in the reporting year for:

- A limited amount of interest on mortgage provided it is used to finance acquiring taxpayer's "main place of residence".
- Secondary professional or higher education of a taxpayer and his/her family members (spouse, parents, parents-in-law, children). For 2010 the credited amount is limited to UAH 1,220 (approximately USD 150) per month of education.
- Limited premiums for voluntary long-term life insurance or non-state pension insurance for the benefit of a taxpayer and his/her family members (spouse, parents, parents-in-law, children).
- Donations to Ukrainian charity and not-for-profit organizations in an amount from 2% to 5% of the taxpayer's taxable income.

The total deductions may not exceed the amount of taxable income received in the form of salary. Amounts not deducted from the income of the reporting year cannot be carried forward.

### Social security contributions

Taxable income is reduced by the amount of mandatory employee contributions to the State Pension Fund and to other social security funds.

The employer's mandatory pension and social security contributions are not included in the taxable income of the employee.

For details on Social Security contributions, see Chapter 7.

## 11.6 Foreign tax credits

Tax residents are allowed a credit for foreign taxes paid on income received abroad, provided there is a double tax treaty between Ukraine and the relevant foreign state. The amount of foreign tax credit is limited to the amount of

Ukrainian tax that would arise from the equivalent income in Ukraine (i.e., maximum 15%). To claim a tax credit, the taxpayer requires an official confirmation of payment issued by the relevant foreign tax authority.

## 11.7 Taxation of non-residents

Non-resident individuals are subject to Ukrainian tax only on income that has a source in Ukraine. The source rules for individuals are broader than those for corporations. For individuals, any income received from activities performed, capital employed or property used in Ukraine will have a Ukrainian source.

Income earned by non-residents from sources in Ukraine in the form of interest, dividends or royalties is taxed at the same rates as for residents, unless subject to a lower rate under a relevant tax treaty.

Salary and director's fees paid by a Ukrainian resident employer (including a representative office) should also be taxed at the standard rate (i.e., 15%), although legislation is unclear in this respect. According to a 2004 clarification issued by the tax authorities, salary received by a non-resident from a Ukrainian resident employer should be taxed at the standard rate (i.e., 15%), but this order was cancelled in December 2009. This order was replaced by an instruction that stated that the 30% rate should be applied to the salary income of foreigners until the individual is able to provide evidence of Ukrainian tax residency. This is an ongoing issue at time of publication, and enterprises should consult advisers prior to making salary payments to foreigners. Any other income earned from sources in Ukraine, including salary and director's fees paid by a non-resident employer, is taxed at the 30% rate. Consideration should also be given to the provisions in Ukraine tax treaties, which often exempt income earned by individuals from short-term visits to Ukraine from Ukrainian tax.

## 11.8 Tax compliance

### Obligations of withholding agents

Employers and other business entities that pay income to individuals are defined as tax agents, and are responsible for withholding the tax and state pension and social insurance contributions, and remitting them to the state and appropriate authorities.

Tax agents should remit the withheld tax to the state not later than the date of payment of income to individuals. Tax

in respect of income that is accrued but not paid to the individuals should be transferred to the state within 20 calendar days of the end of the reporting month.

If income is paid in kind, the tax agent should remit the tax to the state not later than the next banking day following the date of "payment". Tax agents who fail to withhold tax from income paid to individuals are responsible for payment of the tax liability (plus 200% fines and interest). Tax agents must also file quarterly reports on income paid to individuals and the amount of tax withheld from that income.

### Tax returns for individuals

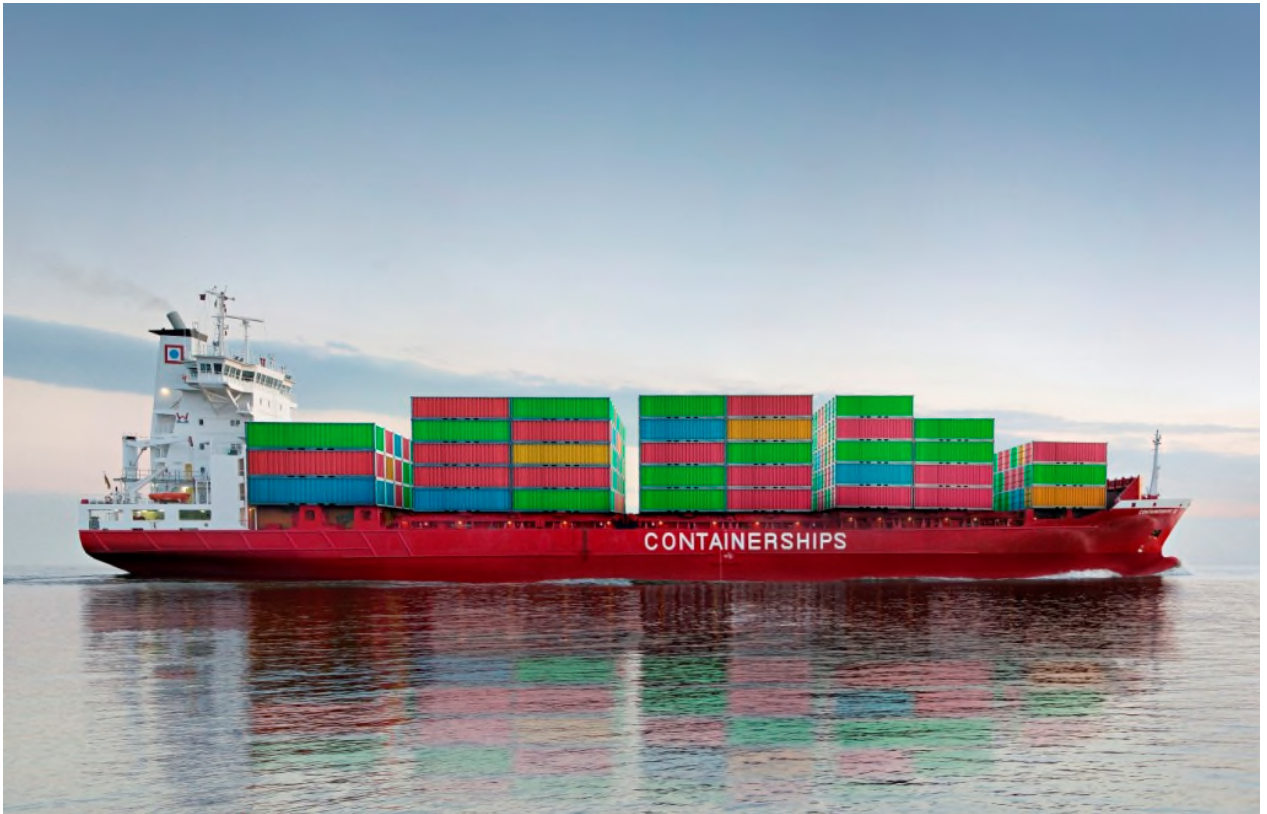
A taxpayer is not required to file an income tax return if his/her only source of income during a reporting year is received from tax agents. However, if the individual wishes to claim a tax credit (deduction) for expenses incurred during the year or to claim a foreign tax credit, he/she may file a return.

Overpaid personal income tax should be returned to the taxpayer within 60 calendar days from the date of filing the tax return. If there is a delay, the state treasury has to pay a fine to the taxpayer in an amount from 10% to 100% of the refund due, depending on the period of delay. Upon the taxpayer's request, the overpayment may be offset against the taxpayer's future tax liabilities.

A resident or non-resident individual who receives taxable income from entities or sources that are not tax agents is required to file a personal income tax return with the tax authorities. The return should be filed with the local office where the individual resides, by 31 March of the year following the reporting year. Tax due on the return must be paid by 10 April. Payment must be made in local currency (hryvnia).

According to the law, no extensions are available, but an individual who was not able to file the tax return by the deadline because of reasonable circumstances may apply for an extension of time to file. Adequate documentation must be provided to support the application. The return would then be due within 30 calendar days, and any payment would be required within ten days of that new filing date.

If a tax resident departs from Ukraine, the individual must submit a "departure tax return" no less than 60 days before his departure, and settle the tax due based on the assessment issued by the tax authorities. No such requirement exists for non-resident individuals.



## 12 Value added tax

### Investor considerations

- The standard rate of VAT is 20%. The export of goods and a very limited range of services are zero-rated.
- Many services to non-residents are effectively considered outside the scope of VAT (i.e., exempt services). This impacts the recoverability of input VAT.
- Refunds are available according to the law, but obtaining refunds is very difficult, and is a major issue for many investors. In addition, VAT-registered persons may not claim a refund during their first twelve months following registration.
- Buyers must ensure that invoices they obtain comply fully with VAT rules. The tax authorities look at invoices closely, and disallow input tax credits, even if the defects in the invoice are relatively minor.
- VAT returns and payments must generally be made monthly.

### 12.1 Introduction

Ukraine first introduced value-added tax (VAT), or *podatok na dodanu vartist* (PDV) as it is known in Ukrainian, in 1992. Ukraine operates the input-output model of VAT. VAT-registered persons deduct the VAT paid on their inputs from the VAT charged on their sales and account for the difference to the tax authorities.

The standard rate of VAT on domestic sales of goods and services and the importation of goods is 20%. Exported goods and related services are zero-rated. Other services provided to non-residents are considered to be outside of scope of VAT.

## 12.2 Taxable activities

Other than businesses that elect to be covered by the unitary tax (see Chapters 10.1 and 11.2), an entity engaged in business is required to register for VAT if sales for the past 12 months exceed UAH 300,000. Taxpayers engaged in business with sales below this threshold may register voluntarily for VAT.

## 12.3 Scope of VAT

Unless there is an express exemption in the law, VAT applies to:

- Supply of goods and services where the place of supply is in Ukraine, including when supply is made without consideration; and
- Importation of goods into Ukraine.

### Place of supply for goods

The place of supply for goods is determined under the following rules:

- If goods are to be transported, the supply takes place where the goods are located when they are dispatched.
- If the goods do not need to be transported, the supply takes place where the goods are located when they are sold.
- When goods that require assembly or installation are sold, the supply occurs where the goods are assembled or installed. If it is not possible for the goods to be shipped in assembled form, supply occurs where the goods are located when they are dispatched.
- The sale of real estate occurs in the place where the property is located.
- The supply of goods to sea, air or railroad vessels occurs at the place where the vessel will depart.
- For internet sales, goods are considered to be supplied in the place where the seller is located or is resident.

### Place of supply for services

The general rule is that services are supplied from the place where the supplier is registered for VAT. However, if services are provided by (or to) a non-resident:

- The place of supply will be the location of its representative office or person exercising agency functions for the non-resident.
- If the non-resident has no representative office or agent, the place of supply is the location of the buyer. (The buyer is then required to account for VAT under the reverse charge mechanism (see Chapter 12.8)).

Specific place of supply rules apply to the following services:

- The services of realtors and entities responsible for the preparation, co-ordination, supervision and performance of real-estate construction and finishing work (e.g., architects and designers) are supplied in the place where the relevant realty is, or will be, located.
- Valuation of immovable property and work on movable property, personnel services for servicing maritime, air and space facilities occur in the place where the services are provided.

Special place of supply rules also apply to the supply of intellectual property rights, advertising, accounting, legal, consulting and data processing services, and the leasing of movable property to non-residents:

- If the non-resident recipient of such services has a permanent representative office, address or residence in Ukraine, the services are considered supplied at the location of that representative office, address or residence, and so will be subject to VAT.
- If the non-resident does not have a permanent representative office, address or residence in Ukraine, the services will be treated as performed outside Ukraine, and accordingly will be outside the scope of VAT.

The legislation is not clear and the tax authorities tend to claim that many of the above services provided to non-residents should be subject to 20% VAT.

### VAT on importation

Unless expressly exempted under the law, imported goods are subject to 20% VAT during customs clearance. The taxable base is the higher of the contractual or customs value of the goods, plus the amount of any import duties and excise duties.

## 12.4 Zero-rating

The export of goods and the supply of services that are ancillary to the export of goods are zero-rated. Zero-rating also applies to the supply of international transport services and toll manufacturing services (if finished goods are then exported from Ukraine).

## 12.5 Exempt supplies

Ukrainian law distinguishes VAT-exempt transactions from transactions that are outside the scope of VAT, but from a practical perspective the distinction is not important. In either case, a person making such sales will not be entitled to claim an input tax credit against those sales.

A number of transactions are specifically "exempt" from VAT, including:

- Most financial services and the transfer of certain financial instruments. However, as exemptions are defined with respect to specific transactions, transactions must be reviewed individually to confirm whether an exemption applies.
- Depository, clearing and registrar activities in the securities market, as well as brokerage and dealer services for securities transactions.
- The issue, sale and exchange of securities and corporate rights and the payment of dividends and royalties in cash or securities.
- The sale/supply by banks and other financial institutions of collateral repossessed from individuals and private entrepreneurs.
- The interest or commission element of payments under a financial lease, up to a maximum of 200% of the NBU prime rate. However, the transfer of property under a financial lease is treated as a taxable sale.
- Insurance and reinsurance services supplied by licensed insurers, agents and brokers.
- The transit of cargo and passengers through Ukraine.

## 12.6 Taxable amount

In most cases, the amount of VAT will be determined based on the transaction price for the supply of goods or services. If the market price exceeds the transaction price by more than 20%, the seller must account for output VAT based on the market price.

For imported goods, VAT is based on the higher of the contract price or customs value stated in the bill of entry, increased by the costs of bringing those goods into Ukraine, excise taxes and duties payable at the time of importation, and any payments for the use of intellectual property incorporated into the goods.

Where the place of supply is in Ukraine, VAT must be incorporated into the stated sale price.

## 12.7 Input tax credits

The general rules for VAT input tax credits are as follows:

- VAT paid on goods and services that will be used to make taxable sales may be claimed as an input tax credit.
- VAT incurred to purchase or import goods and services that will be used to make sales that are VAT-exempt or outside of scope of VAT may not be claimed as a credit.
- When goods and services are used to make partly taxable and partly non-taxable sales, the input tax credit is apportioned between the taxable and non-taxable sales. Input tax credits are directly attributed to taxable and non-taxable sales. Any input tax credits that cannot be directly attributed would then be allocated based on the proportion of taxable sales to total sales for each month.
- No input tax is available for the purchase of a car (except taxes).

A claim for input tax must be supported by a valid VAT invoice issued by a VAT-registered person or a duly executed import customs declaration.

In most cases, input tax credits will be based on the transaction price. However, if the transaction price exceeds the market price by more than 20%, the input tax credit should be based on the market price.

## 12.8 VAT compliance

### Registration

A person qualifying as a taxable person is required to register with the tax authority at the place where its business is located and to obtain a VAT registration number.

The local tax authority should issue a VAT registration certificate to the applicant within ten calendar days. VAT



registration takes effect from the date specified on the registration certificate.

## Accounting requirements

VAT-registered persons are required to keep separate accounts for taxable and VAT-exempt sales and purchases and issue VAT invoices.

## Information on VAT invoice

A VAT-registered person is required to provide a VAT invoice for all transactions. The invoice must include the following information:

- The number of the tax invoice and the date the invoice is issued.
- The full name and registration number of both the buyer and the seller.
- The addresses of the taxpayer (seller).
- The type and quantity of the goods and services provided.
- The sales price (excluding VAT), the tax rate and amount of VAT, and the total amount payable.

Separate invoices are required for taxable and exempt transactions. Invoices for exempt transactions must include the words, "без ПДВ" (*bez PDV* - without VAT).

Buyers need to pay particular attention to the information contained in VAT invoices, particularly when significant amounts are involved. The tax authorities pay close attention to the details on invoices when they conduct audits, and will disallow input tax credits even if there are relatively minor defects in the invoice.

## VAT liability

VAT liability is calculated monthly using the input-output method. The VAT liability in a given month will be the total amount of output tax charged on sales, less the input VAT relating to taxable sales.

VAT is accounted for as follows:

- VAT on the sale of goods is generally accounted for on the date that goods are delivered to the customer or the date that payment is received from the customer, whichever is earlier.
- VAT on the sale of services is generally accounted for at the time a document is executed evidencing delivery

of the service or receipt of payment from the customer (an "act of acceptance"), whichever is earlier. It is usual commercial practice for both supplier and customer to sign a formal document evidencing the delivery of the service.

- Entitlement to an input tax credit for purchases arises on the date of payment to the supplier or the date on which the VAT invoice is received, whichever is earlier.
- Entitlement to an input tax credit for imported goods or services arises on the date the tax is paid.

## Reverse charge

Services acquired from non-residents are subject to the application of a VAT reverse charge. A person required to account for VAT on such transactions would report the VAT as output tax in a specific line in the VAT return for the month in which the transaction is required to be recognised. The corresponding input tax would then be claimed as a credit in the following month (if the buyer is entitled to a VAT credit).

## Returns and payments

VAT-registered persons are required to file VAT returns on a monthly basis (except for any small businesses). The return must be filed within 20 calendar days of the last day of the month (or the next working day if the 20th day falls on a weekend or a public holiday).

VAT payments must be made within ten calendar days of the date on which returns are required to be filed.

## Refunds

A VAT-registered person may apply for a refund if they have been in a VAT credit position for two consecutive months. The refund is limited to the amount of input tax actually paid for the previous months.

According to the law, if an application for refund is filed, the tax authorities are required to check and confirm the entitlement within 65 days. The State Treasury should then remit money to the applicant's bank account within five business days after receiving approval from the tax authorities. In practice, there is no liability for the government if it does not issue VAT refunds on a timely basis.

Obtaining VAT refunds has been a major problem area for investors.

VAT-registered persons are specifically not entitled to refunds if:

- They have been registered for VAT for less than 12 calendar months before the month for which a refund is sought, except where refund relates to input tax paid on purchase or construction of fixed assets based on a Government decision.
- The amount of the refund claimed exceeds taxable sales for the last 12 calendar months, except for refund of input tax on the purchase or construction of fixed assets.
- They have not carried on business activities during the last 12 calendar months.



## 13 Introduction to PricewaterhouseCoopers

PricewaterhouseCoopers ([www.pwc.com](http://www.pwc.com)), the world's largest professional services organisation, provides industry-focused assurance, tax and advisory services to build public trust and enhance value for its clients and their stakeholders.

Drawing on the talents of more than 163,000 people in 151 countries, PricewaterhouseCoopers provides a full range of business advisory services to leading global, national and local companies as well as to public institutions. These services include audit, accounting and tax advice; management, information technology and human resource consulting; financial advisory services including mergers and acquisitions, business recovery, project finance, and litigation support; business process outsourcing services; and legal services provided through a global network of affiliated law firms.

PricewaterhouseCoopers refers to the US firm of PricewaterhouseCoopers LLP and other members of the worldwide PricewaterhouseCoopers organization.

### PricewaterhouseCoopers in Ukraine

Coopers & Lybrand and Price Waterhouse established their Ukrainian operations in 1993 and 1995 respectively, before merging in 1998. Having continued to expand its services and knowledge of Ukraine's business environment, PricewaterhouseCoopers provides the highest level of professional services to international and Ukrainian enterprises. Overseen by 18 partners and directors and employing more than 350 specialists and support staff, PricewaterhouseCoopers operates in Ukraine from its offices in Kyiv, Donetsk and Lviv.

The combination of local experience and a one-firm culture enables PricewaterhouseCoopers to provide advice that is consistent. In addition, its global standards are responsive to local conditions and requirements.

Engagements are generally staffed by a combination of Ukrainian specialists, with knowledge of local conditions and regulations, and international consultants, who have expertise in tackling issues faced by international enterprises and who are practised in dealing in the Ukrainian environment. The key element of PricewaterhouseCoopers' success in Ukraine is the quality of its staff, to which partners are committed to providing the most up to date management training throughout their careers.

Our team is divided into three service lines: Assurance Services, Advisory Services, and Tax and Legal Services.

## Assurance services

Assurance Services provides assurance on the financial performance and operations of our clients' business, through external and internal audits, financial and accounting reviews and investigations, regulatory consulting and training courses.

The Ukrainian practice is comprised of Ukrainian and international specialists possessing a deep knowledge of both national and international financial reporting standards. As part of our long-term development strategy, we encourage local employees to obtain an internationally recognised professional qualification in accounting (UK ACCA). Our firm has the largest number of ACCA graduates of any professional service firm in Ukraine. In addition, we have a large number of certified Ukrainian auditors holding either banking audit or commercial audit qualifications.

PricewaterhouseCoopers' knowledge and experience gained over seventeen years of reform in Ukraine, enables our specialists to advise not only on assurance matters, but also to put them in context and to advise on the likely impact that the pace and direction of economic and financial change will have on a commercial activity in Ukraine.

As a result of its long-term presence, PricewaterhouseCoopers Ukraine has developed strong relationships with key contacts, including government ministries and leading professional organisations. These relationships enable the firm to be well placed to assist in resolving queries on accounting, reporting and related regulatory issues.

Available Assurance services include:

- **Audit** – statutory and regulatory audit and treasury services.

Our audit is aligned with business functions, not just financial processes. Businesses need auditors and advisors who understand their strategy and can reflect this in their audit approach. Using our approach and working alongside our clients, our lead partner provides strong control from the centre. We put great emphasis on understanding our clients' strategy and the need to address all risks. This approach represents, we believe, an important step forward in client service, audit quality and efficiency.

- **Accounting and regulatory advice** – corporate structures, technical accounting advice (supported by Global Corporate Reporting (GCR)), review of treasury operations, compliance with current and new regulations.
- **Attest and attest-related services** – independent assessment of financial and non-financial data.
- **Public services audit and advisory** – audit, internal audit and associated services for government, education and other non-profit organisations.
- **Corporate training** – business training and development services in the area of finance and accounting, IT systems, risk management, and management development.

## Advisory services

The Advisory Services practice provides two main types of services:

**Deals:** Deals Services refers to assistance with and execution of all types of financial transactions, providing advice on mergers and acquisitions, privatisations, financial and operational due diligence, value advisory and business valuation including real estate and asset valuation, feasibility studies and business plans, market analysis, project finance (including Public-Private Partnership schemes), finance raising and post-deal services.

PricewaterhouseCoopers provides a full range of services to guide clients through complex business transactions, and supports companies through every aspect of a transaction, from identifying the appropriate acquisition or divestiture candidates to assisting with deal structuring and capital sourcing. A wide range of privatisation services including lead advisory, target identification, company profiles, analysis of privatisation options, and transaction support are available, as well as assistance and support for companies seeking new capital, or companies involved in

an acquisition, divestiture, restructuring or shareholder buyout. Services in relation to transactions, such as identification and evaluation of a transaction through due diligence, structuring services, market analysis and post-deal services are provided.

**Consulting:** Our Consulting team is dedicated to helping clients improve their financial and operational performance. Our Group works closely with other advisory practices in the firm to assist clients in meeting their most pressing challenges.

The assistance we provide is targeted at strengthening management control, increasing operational effectiveness and thereby increasing shareholder value. We know from experience that improving performance requires companies to focus on four distinct aspects: business model, financial drivers, management system and value creation system.

In our experience, projects are judged a success when the expected business benefits are clearly defined up front and when the project is managed to demonstrate achievement of those business benefits. By employing this principle in our methodologies, the Performance Improvement team strives to provide superior value to our clients.

Crisis Management services involve corporate recovery and turnaround, optimised exits, insolvency/liquidation, as well as dispute analysis and investigations. It advises on and implements a complete range of solutions for business recovery situations, corporate bankruptcy and implementation of large-scale turnarounds for underperforming corporations.

Our dispute analysis and investigations practice involves corporate investigations, fraud risk management, background research of entities, computer forensics and cybercrime investigations, as well as investigations of insolvency and bankruptcy, together with intellectual property.

## Tax and legal services

Effective tax planning is vital for the growth and development of any organisation. Few major decisions can be taken without considering their tax and legal implications. In Ukraine, where the tax and legal system is complex and subject to constant revision, professional advice is even more of a necessity to achieve success.

Therefore, companies who seek the very best in tax and legal advice in Ukraine turn to PricewaterhouseCoopers for a complete solution to their complex business problems. Clients realise that by seeking our expert advice, considerable savings can be achieved.

Our team of local and expatriate professionals have expertise in all areas of taxation – corporate and personal, direct and indirect, corporate law – to help clients maximise their tax advantages and minimise their exposures. We advise both national and international companies based upon our knowledge of Ukrainian legislation and its interrelationship with international laws and treaties. This knowledge, together with our focus on specific markets and industries, helps us to add value to our clients' businesses and give them the edge they need in the marketplace.

Our Tax and Legal Services practice is divided into five main areas of expertise:

**Corporate tax:** Our team has extensive experience in advising clients based on Ukrainian laws and their interpretation by tax authorities, as well as their interrelation with international regulations and treaties. Our specialists are highly qualified to advise on all aspects of inward investments into Ukraine, and the structuring of those investments in terms of corporate profits tax, withholding tax, dividend taxation and local tax regulations. The team provides proactive advice on international tax planning and structuring, mergers and restructuring, and undertakes company health checks and due diligence projects, as well as assistance with tax authorities (during tax inspections and lodging of objections).

With corporate tax, we have a large team dedicated to transactions services, mergers and acquisitions and international tax structuring.

**VAT and other indirect tax:** Our indirect tax specialists have extensive experience in resolving complex issues related to indirect taxes, customs procedures and foreign trade. Services available include VAT consultancy and tax reviews, VAT planning and efficiency schemes for domestic and cross-border operations, assistance during tax inspections; support and advice during appeals. Customs consulting includes tax planning for minimising import duties, assistance in complying with customs procedures, use of bonded warehouses, intellectual property rights, obtaining import/export licences, assistance during customs clearance and audits, and support during customs litigation or complaints.

**Human Resources Services (HRS):** HRS brings together all of the professionals working in the human resource consulting arena – specialists in individual tax, payroll, benefits, assessment, education, equity, reward, staffing, regulatory, legal, and process management – offering clients an unmatched breadth and depth of local and global expertise. Available services include individual advice, ranging from assistance with obtaining work and residence permits, to advice and assistance with all matters regarding

Ukraine's personal income taxation legislation, salary surveys, outplacement, and human resources audit.

**Compliance solutions:** With the increasing focus on governance and regulation, tax compliance has never been so important. Compliance failure represents not only a financial risk – financial penalties and a possible increase in the tax charge – but also a serious business risk, as it can damage a group's reputation with the authorities and the public.

PricewaterhouseCoopers can help you manage your tax compliance issues, risks and opportunities, allowing you to have firm control. We can help you, both within Ukraine and

cross-border, with preparing and reviewing tax returns and computations, negotiating with tax authorities, corporate income tax compliance, indirect tax compliance, accounting services and payroll services.

**Legal services:** Our lawyers are qualified to give advice in a multitude of areas that include advising multinational companies and local businesses on how to structure their investments and activities in Ukraine, banking, securities and financing, privatisation, mergers and acquisitions, legal due diligence, corporate structures, competition, trade practices, intellectual property and employment, tax litigation.

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# Appendix A - Hints for business visitors

## Visas other entry formalities

Citizens of the USA, Canada, countries of the Commonwealth of Independent States (except Turkmenistan), European Union countries, Andorra, Iceland, Japan, Liechtenstein, Monaco, Mongolia, Montenegro, Norway, San Marino, Serbia and Switzerland do not need a visa to enter Ukraine if the duration of their stay does not exceed 90 days from the first entry within the last 12-month period. However, they do need to hold a passport that is valid for at least six months from the date of their entry into Ukraine. For citizens of other countries, a visa is obligatory.

Countries whose citizens require a visa to enter Ukraine, need an invitation for business and private visas, which should be duly issued by the immigration authority (Ukrainian abbreviation VGIRFO, former OVIR). The invitation is submitted with the appropriate application to the Ukrainian Embassy / Consulate abroad. An invitation is not required to obtain a work visa, as working visas are issued on the grounds that the original of the work permit is available.

The specific documents to be submitted together with the visa application are not consistent across all Embassies and Consulates. This list of documents is subject to frequent change. Generally, it is not required to come to the Embassy or Consulate in person in order to obtain a visa. Persons travelling to Ukraine should confirm the visa rules from a reliable source before departure.

Additionally, the citizens of some African, Asian and CIS countries, e.g., Moldova, Afghanistan, Tajikistan, Turkmenistan, the Republic of South Africa, India, etc. (excluding ethnic Ukrainians with confirming documents) should have proof of their financial security for the period of their stay in Ukraine. Citizens from "risk countries" must have available funds (or guarantees) in the amount of 20 subsistence salaries (approximately USD 2,200) for every full or incomplete month of their stay in Ukraine

## Currency

The currency of Ukraine, the Hryvnia, i.e., UAH, was introduced in 1996.

Currently, the National Bank of Ukraine (NBU) adopts a de facto peg against the US dollar. The official US dollar/UAH exchange rate was fixed to 5.05 from April 2005 until May

2008. The world finance crisis has hit the stability of the national currency and Hryvnia devalued by more than 70% against the US-dollar by the end of 2009. As of end of 2009 the US dollar/UAH exchange rate amounts to approximately 8 UAH.

It is common practice in Ukraine for some prices to be set in US dollars, and to a lesser extent Euros, particularly for high-value items. Property rentals, for example, will typically be expressed in dollars. In most cases, however, settlement will still be made in Hryvnia.

## Public holidays

In 2010, Ukraine will have the following public holidays:

- New Year's Day (January 1).
- Orthodox Christmas (January 7).
- International Women's Day (March 8).
- Orthodox Easter (April 4).
- Labour Days (May 1 & 2).
- Victory Day (May 9).
- Orthodox Pentecost (May 23)
- Constitution Day (June 28).
- Independence Day (August 24).

If a holiday falls on a Saturday or Sunday, the following Monday will be a non-working day. If a holiday falls on a Tuesday or a Thursday, it is common for Parliament to recommend that the Monday or Friday be declared as a holiday as well, and for a Saturday of another week to be made a working day to compensate.

For 2010, the Cabinet of Ministers has already recommended to move the following working days:

- Monday 4 January to Saturday 16 January.
- Tuesday 5 January to Saturday 30 January.
- Wednesday 6 January to Saturday 13 February.
- Friday 8 January to Saturday 27 February.
- Monday, 23 August to Saturday, 21 August.

However, the above recommendations are not applied to the post, treasury and banking institutions.

# Appendix B - Useful sources of information

## Government websites

Many government websites have pages written in English. These can be useful to get a flavour of government policies and initiatives in various areas of the economy. Caution should be exercised, however, before relying on information in English. Although the Ukrainian web pages are generally well maintained and up to date, the same cannot be said for the English version. To obtain current information, the only real solution is to have someone review the Ukrainian and provide a translation.

At the time of writing, the following agencies have English pages on their websites:

Cabinet of Ukraine	<a href="http://www.kmu.gov.ua/control/en">www.kmu.gov.ua/control/en</a>
Main Department of Civil Service	<a href="http://www.guds.gov.ua/control/en/index">www.guds.gov.ua/control/en/index</a>
Ministry of Agrarian Policy	<a href="http://www.minagro.kiev.ua/?lng=E">www.minagro.kiev.ua/?lng=E</a>
Ministry of Economy	<a href="http://www.me.gov.ua/control/en/index">www.me.gov.ua/control/en/index</a>
Ministry of Education and Science	<a href="http://education.gov.ua/pls/edu/educ.home.eng">education.gov.ua/pls/edu/educ.home.eng</a>
Ministry of Finance	<a href="http://www.minfin.gov.ua/control/en/index">www.minfin.gov.ua/control/en/index</a>
Ministry for Foreign Affairs	<a href="http://www.mfa.gov.ua/mfa/en/news/top.htm">www.mfa.gov.ua/mfa/en/news/top.htm</a>
Ministry of Labour and Social Policy	<a href="http://www.mlsp.gov.ua/control/en/index">www.mlsp.gov.ua/control/en/index</a>
National Academy of Sciences	<a href="http://www.nas.gov.ua/en/Pages/default.aspx">http://www.nas.gov.ua/en/Pages/default.aspx</a>
National Bank of Ukraine	<a href="http://www.bank.gov.ua/Eng/default.htm">www.bank.gov.ua/Eng/default.htm</a>
State Committee of Statistics	<a href="http://www.ukrstat.gov.ua">www.ukrstat.gov.ua</a>
State Committee for Regulatory Policy and Entrepreneurship	<a href="http://www.dkrp.gov.ua/control/en/index">www.dkrp.gov.ua/control/en/index</a>
State Property Fund	<a href="http://www.spfu.gov.ua/eng/index.php">www.spfu.gov.ua/eng/index.php</a>
State Tax Administration	<a href="http://www.sta.gov.ua/control/en/index">http://www.sta.gov.ua/control/en/index</a>
Verkhovna Rada (Parliament)	<a href="http://portal.rada.gov.ua/control/en/index">portal.rada.gov.ua/control/en/index</a>

## Business groups

**American Chamber of Commerce (Amcham)**  
Horizon Park Business Centre 12, Amosova Str.  
15 Floor  
Kyiv 03038  
Tel. (380-44) 490-5800  
Fax (380-44) 490-5801  
[www.chamber.ua/](http://www.chamber.ua/)

**British-Ukrainian Chamber of Commerce**  
Suite 42  
34A Grushevskogo Str.  
Kiev 01021  
Tel. (380-44) 410-5720  
Fax. (380-44) 230-2151  
[www.bucc.com.ua](http://www.bucc.com.ua)

**European Business Association (EBA)**  
1A Andriijivskyy Uzviz Str.  
1st floor  
Kyiv 04070  
Tel. (380-44) 496 0601  
Fax (380-44) 496 0602  
[www.eba.com.ua](http://www.eba.com.ua)



## Appendix C - Withholding taxes as at 1 February 2010

Country	Dividends (%)		Interest (2) (%)	Royalties (3) (%)
	Non-portfolio (1)	Portfolio		
Domestic rates:				
Non-resident individuals	15	15	5 / 15 (4)	15
Non-resident corporations	15	15	15	15
Treaty rates:				
Algeria	5	15	10	10
Armenia	5	15	10	0
Austria	5	10	2 / 5 (5)	0 / 5
Azerbaijan	10	10	10	10
Belarus	15	15	10	15
Belgium	5	15	2 / 10 (5)	0 / 10
Brazil	10	15	15	15
Bulgaria	5	15	10	10
Canada	5	15	10	0/10
China (PRC)	5	10	10	10
Croatia	5	10	10	10
Cyprus (6)	0	0	0	0
Czech Republic	5	15	5	10
Denmark	5	15	0 / 10 (7)	0 / 10
Egypt	12	12	12	12
Estonia	5	15	10	10
Finland	0 / 5 (8)	15	5 / 10 (7)	0 / 5 / 10
France	0 / 5 (9)	15	2 / 10 (5)	0 / 5 / 10
Georgia	5	10	10	10
Germany	5	10	2 / 5 (5)	0 / 5
Greece	5	10	10	10
Hungary	5	15	10	5
Iceland	5	15	10	10
India	10	15	10	10
Indonesia	10	15	10	10
Iran	10	10	10	10
Israel	5/10	15	5 / 10 (10)	10
Italy	5	15	10	7
Japan (6)	15	15	10	0 / 10
Jordan	10	15	10	10
Kazakhstan	5	15	10	10
Korea (ROK)	5	15	5	5
Kuwait	5	5	0	10
Kyrgyzstan	5	15	10	10
Latvia	5	15	10	10
Lebanon	5	15	10	10
Libya	5	15	10	10
Lithuania	5	15	10	10
Macedonia	5	15	10	10
Malaysia (6)	15	15	15	10 / 15
Moldova	5	15	10	10

Mongolia (6)	0	0	0	0
Morocco	10	10	10	10
Netherlands	0 / 5 (11)	15	2 / 10 (5)	0 / 10
Norway	5	15	10	5 / 10
Poland	5	15	10	10
Portugal	10 / 15 (12)	15	10	10
Romania	10	15	10	10 / 15
Russian Federation	5 (13)	15	10	10
Serbia and Montenegro	5	10	10	10
Singapore	5	15	10	7.5
Slovakia	10	10	10	10
Slovenia	5	15	5	5 / 10
South Africa	5	15	10	10
Spain (6)	15	15	0	0 / 5
Sweden	0 / 5 (14)	10	0 / 10 (5)	0 / 10
Switzerland	5	15	0 / 10 (5)	0 / 10
Syria	10	10	10	15
Tajikistan	10	10	10	10
Thailand	10	15	10 / 15 (10)	15
Turkey	10	15	10	10
Turkmenistan	10	10	10	10
United Arab Emirates	5	15	3	0 / 10
United Kingdom	5	10	0	0 (15)
U.S.A.	5	15	0	10
Uzbekistan	10	10	10	10
Vietnam	10	10	10	10

- (1) The ownership threshold for the non-portfolio rate is 10%, 20%, 25% or 50%, depending on the specific provisions in the treaty.
- (2) Several treaties contain a rate of 0% on interest paid to or guaranteed by a government or one of its agencies.
- (3) If more than one rate is shown, this means that the rate will depend on the type of royalties paid.
- (4) The lower rate applies to interest on current or deposit bank accounts, certificates of deposit, contributions to a credit union, and participatory and fixed-yield mortgage certificates.
- (5) The lower rate applies to interest paid on certain credit sales, and on loans granted by a financial institution.
- (6) The treaties with Cyprus, Japan, Malaysia, Mongolia and Spain were entered into by the USSR before it dissolved. Ukraine will continue to honour these treaties, unless they are superseded.
- (7) The lower rate applies to interest paid in connection with the sale on credit of any industrial, commercial or scientific equipment, unless the indebtedness is between associated enterprises.
- (8) The 0% rate applies if the investor holds at least 50% of the capital of the company paying the dividends and the capital invested is at least USD 1,000,000; the payer of dividend should not operate in the field of gambling, show business or intermediation business, or auctions).
- (9) The 0% rate will apply if a French company or companies hold directly or indirectly at least 50% of the capital of the Ukrainian company, and the aggregate investments exceeds 5 million French francs.
- (10) The lower rate applies to interest paid on any loan granted by a bank
- (11) The 0% rate applies if the investor holds directly at least 50% of the capital of the company paying the dividends, and the capital invested is at least USD 300,000.
- (12) The 10% rate applies if the company receiving the dividend has, for an uninterrupted period of two years before the dividend is paid, owned at least 25% of the capital stock of the company paying the dividends.
- (13) The 5% rate applies if the capital invested is at least USD 50,000.
- (14) The 0% rate applies if the Swedish company holds directly at least 25% of the voting power of the company paying the dividends, and at least 50% of the Swedish company is held by Swedish residents.
- (15) The 0% rate applies only if the royalties are taxable in the United Kingdom.

# Appendix D - Selected customs duties and excise tax rates

## Selected customs duties rates

Product or Group of Products	Rates of duty		
	Reduced rate, %	Full rate, %	Products originating in CIS, %
IT equipment	0 – 5	0 – 5	exempt
Cars	10	10	exempt
Office equipment, including paper	0 – 10	0 – 10	exempt
Coffee, tea	0 – 10	0 – 10	exempt
Beer	EUR 0.05 per litre	EUR 0.05 per litre	exempt
Chocolate products	10 – 15	10 – 15	exempt
Pharmaceuticals	0	0	exempt
Agricultural equipment	0 – 10	0 – 10	exempt

## Selected excise tax rates

Product	Excise duty rate
Beer	UAH 0.31 per 1 litre
Wine base of grapes	UAH 0.01 per 1 litre
Fortified wine	UAH 0.50 per 1 litre
Wine, sparkling wine, vermouth	UAH 2.50 – UAH 2.60 per litre
Fermented fruit beverages with added alcohol	UAH 34 per litre of 100% alcohol
Fermented fruit beverages without added alcohol	UAH 0.34 per litre
Ethyl alcohol and other spirits, liqueurs and other spirituous beverages	UAH 34 per litre of 100% alcohol
Spirit distillates and other spirit beverages from grape wine	UAH 14 per litre of 100% alcohol (starting from 1 January 2010 - UAH 20 per litre of 100% alcohol)
Tobacco raw materials	0
Cigars, cigarillos	UAH 60 per 100 sticks and 20% of sale turnover
Cigarettes	UAH 35 – UAH 60 per 1000 sticks and 20% of sale turnover (but not less than UAH 50 – UAH 100 totally)
Tobacco for smoking, chewing tobacco or snuff	UAH 10 per kilogram and 20% of sale turnover
New cars	EUR 0.03 – EUR 1 per cubic centimetre
Used cars	EUR 1 – EUR 3.50 per cubic centimetre
Motorcycles, motor bikes	EUR 0.20 per cubic centimetre
Petrol and diesel	EUR 12 – EUR 110 per 1000 kilograms

## Appendix E - Short form Chart of Accounts under Decree No. 291

Synthetic Accounts (1 <sup>st</sup> Tier Accounts)		Subaccounts
Code	Name	Code
1	2	3
Class 1. Non-current Assets		
10	Fixed Assets	100-109
11	Other Non-current Tangible Assets	111-117
12	Intangible Assets	121-127
13	Depreciation of Non-current Assets	131-135
14	Long Term Financial Investments	141-143
15	Capital Investments	151-155
16	Long Term Biological Assets	161-166
17	Deferred Tax Assets	
18	Long Term Account Receivables and other Non current Assets	181-184
19	Goodwill	191-193
Class 2. Stock (Inventories)		
20	Inventories	201-209
21	Current Biological Assets	211-213
22	Low Value Items	
23	Production (Manufacture)	
24	Production Wastage	
25	Semi-finished Goods	
26	Finished Goods	
27	Agricultural Produce	
28	Goods (Stock)	281-286
29		
Class 3. Cash, Settlements and Other Assets		
30	Cash in Hand	301-302
31	Bank's Accounts	311-314
32		
33	Other Funds	331-334
34	Short Term Promissory Notes Receivable	341 -342
35	Current Financial Investments	351-352
36	Settlements with Buyers and Customers	361-363
37	Settlements with Various Debtors	371-377
38	Provision for Doubtful Debts	
39	Deferred Expenses	
Class 4. Equity and Provision for Liabilities		
40	Statutory Capital	
41	Share Capital	
42	Additional Capital	421-425
43	Reserve Capital	
44	Retained Earnings (Loses)	441-443
45	Withdrawn Capital	451-453
46	Unpaid Capital	
47	Provision for Future Expenses and Payments	471-478
48	Targeted Finance	

Synthetic Accounts (1 <sup>st</sup> Tier Accounts)		Subaccounts
Code	Name	Code
1	2	3
49	Insurance Reserves	491-496
Class 5. Long Term Liabilities		
50	Long Term Borrowings	501-506
51	Long Term Promissory Notes payable	511-512
52	Long Term Liabilities in Respect of Bonds issued	521-523
53	Long Term Lease Liabilities	531-532
54	Deferred Tax Liabilities	
55	Other Long Term Liabilities	
56-		
59		
Class 6. Current Liabilities		
60	Short Term Loans	601-606
61	Current Debt on Long Term Liabilities	611-612
62	Short Term Promissory Notes payable	621-622
63	Settlements with Suppliers and Contractors	631-633
64	Settlements on Taxes and Payments	641-644
65	Settlements on Insurance	651-655
66	Settlements on Payments to Employees	661-663
67	Settlements with Participants (or shareholders)	671-672
68	Other settlements	680-685
69	Deferred Income	
Class 7. Revenue and Results of Operations		
70	Sale Revenue	701-705
71	Other Operating Income	710-719
72	Income from Interest in Equity	721-723
73	Other Financial Income	731-733
74	Other Income	741-746
75	Extraordinary Income	751-752
76	Insurance Payments	
77		
78		
79	Financial Results	791-794
Class 8. Expenses by nature		
80	Material Expenses	801-809
81	Labour Costs	811-816
82	Social Payments	821-824
83	Depreciation and amortisation	831-833
84	Other Operating Expenses	
85	Other Expenses	
86-89		
Class 9. Operating expenses		
90	Cost of Sales	901-904
91	Production Costs (Overheads)	
92	Administrative expenses	
93	Selling expenses	
94	Other Operating Expenses	940-949
95	Financial Expenses	951-952
96	Loss from Interest in Equity	961-963
97	Other Expenses	971-979
98	Income tax expense	981-982
99	Extraordinary Expenses	991-993
Class 0. Off balance sheet accounts		

<b>Synthetic Accounts (1<sup>st</sup> Tier Accounts)</b>		<b>Subaccounts</b>
<b>Code</b>	<b>Name</b>	<b>Code</b>
1	2	3
01	Leased Non-current Assets	
02	Third party Assets in Store	021-025
03	Contractual Liabilities	
04	Contingent Assets and Liabilities	041 042
05	Guarantees and Security Given	
06	Guarantees and Security Received	
07	Written-off Assets	071 072
08	Strict Accounting Forms	
09	Depreciation Charges	

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