23 September 2020
EY Tax and Legal Practice
Tax News

Major legislative initiatives on taxation: a brief overview

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Recently, legislative bills proposing significant tax changes have been registered in the Verkhovna Rada of Ukraine:

- Draft Law "On Amendments to the Tax Code of Ukraine and Other Laws of Ukraine to ensure the Collection of Data and Information Necessary for Reporting of Certain Taxable Items" (registration No. 4065; hereinafter "**Bill No. 4065**"), registered on 7 September 2020.
- Draft Law "On Amendments to the Tax Code of Ukraine and Other Laws of Ukraine on Securing Balanced Budget Revenues" (registration No. 4101; hereinafter "**Bill No. 4101**"), registered on 15 September 2020 at the initiative of the Cabinet of Ministers of Ukraine.

Both bills have not been considered by the Verkhovna Rada of Ukraine yet, so the final wording of changes is unknown. Below we outline a brief overview of the most significant initiatives.

Bill No. 4065

- Limitation of the scope of business purpose test for corporate profit tax purposes to the following transactions:
- Transactions recognized as controlled according to Article 39 of the Tax Code of Ukraine (hereinafter the "**Tax Code**").
- Purchase / sale of goods, including noncurrent assets, works and services from/to non-residents incorporated in low-tax jurisdictions or specific forms of business (starting from 01 January 2022).
- Accrual of royalty in favor of non-residents (starting from 1 January 2022).

In all the above cases, the burden to adjust pre-tax financial result in respect of controlled transaction or burden of proof of the respective circumstances (inter alia, lack of business purpose) regarding non-controlled transactions as stated above lies on the tax authority subject to relevant provisions of Article 39 of the Tax Code.

- Amendments to certain transfer pricing rules:
  - vesting the tax authorities with powers to (i) not consider (disregard) the controlled business transaction when assessing the taxpayer's financial result, if non-related parties would not enter into such controlled transaction or (ii) replace the controlled transaction with alternative variant which could have taken place between commercially rational non-related parties in comparable circumstances
  - introducing a rule on distribution of functions, risks and assets in case of insufficient substantiation of parties' actual behavior: they should be attributed to the Ukrainian party to the controlled transaction
  - addition to the requirement on the transfer pricing documentation's content: in case of purchase (sale) of goods, works (services), intangible assets, other items of business transactions, other than goods, the taxpayer is obliged to justify economic feasibility and business purpose of such transactions. It should be noted that this information shall be also disclosed in transfer pricing documentation prepared for non-controlled transactions, the price of which must be justified using the transfer pricing methodology.
- Clarification of thin capitalization rules, including:
  - limitation of interest expenses shall apply only to interest originating from debts to non-residents
  - interest accrued in favor of international financial organizations (subject to certain conditions) and foreign banks should not fall under the limitation.
- Postponement of rules regarding taxation of non-residents' income from direct / indirect disposal of shares / participatory interest in a Ukrainian entity, which derive their value principally from real estate in Ukraine until 2021.
- Postponement of new rules for permanent establishments until 2021. Among others, until the end of 2020 permanent establishments may use the "indirect" and other usual methods to determine their taxable profit.
- Update of rules on controlled foreign companies (hereinafter the "**CFC**"), namely:
  - transfer of the first reporting (tax) year for the CFC report to year 2022 (if the reporting year does not correspond to a calendar year – to the reporting period that begins in 2022)
  - prolongation of tax-free CFC liquidation until 2022
  - introduction of an exemption from military levy within tax-free CFC liquidation
  - possibility to file the first CFC report for year 2022 simultaneously with filing an annual tax return for 2023 without triggering fines / interest penalties
  - postponement of application of increased ownership ratios in foreign entities used for CFC recognition (25% instead of 10%) to years 2022 – 2023
  - non-application to the taxpayer of tax fines / interest penalties, inability to bring the taxpayer to administrative or criminal responsibility for breach of CFC rules (Article 39^2 of the Tax Code) as a result of 2022 – 2023.
  - removal of the controller's obligation to file CFC's primary documents along with transfer pricing documentation.
- Removal of extended tax statute of limitation (2,555 days) for audits of tax agents in respect of personal income tax and military levy on employment-related payments.
- Other changes (including those on tax audits, excise tax and application of electronic cash registers).

Bill No. 4101

- Changes in corporate profit taxation, including:
  - limitation of the right to carry forward tax losses to five years after the year of their origination, starting from tax losses that originated in 2016
  - deferral of tax expenses in respect of interest under transactions with non-residents until they are actually paid (i.e., interest cannot be deducted when accrued)
  - introduction of taxation of non-residents' profits from sale or other disposal of securities, derivatives or participatory interests which are not contributed to residents' charter capital
  - introduction of taxation of non-residents' fees for provision of brokerage, commission and agency services, if such services are provided outside of Ukraine
  - establishment of an obligation for asset management companies to prepare and file corporate profit tax returns and financial statements with respect to each collective investment scheme which is managed by it and is not a legal entity.
- Granting the tax authorities with powers to receive information on the status of the taxpayer's bank accounts, flow of funds and operations, remaining account balance, availability of safekeeping arrangements with the bank, if there is a decision on recovery of funds for tax debt settlement.
- Simplification of the procedure for recovery of tax debt which arose from non-payment of liabilities and/or interest penalties self-assessed by the taxpayer – without a court's sanction and regardless of the amount of tax debt / period of delay.
- A one-time write-off of tax fines and interest penalties if the respective tax debt (which arose as of 1 March 2020 and remained unsettled as of 1 September 2020) is paid in full.
- Changes in value added tax application, including:
  - exclusion from the list of taxable supplies of goods for cases when agricultural plants, plantings, animals are liquidated in case of loss, slaughter due to force majeure or other circumstances that are beyond the reasonable control of the taxpayer

- specification of the "first event" rule for cases when a document is prepared in an electronic form. Chargeable event arises at the date when the electronic document is prepared
- clarification of the chargeable event for supply of goods.
- Other changes (regarding personal income tax, single, excise, environmental taxes, extraction royalty and unified social contribution).

Please note that the reviewed bills will be subject to further harmonization since they contain duplicate provisions.

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