

Tax Newsletter

2011 Tax Code: Key changes related to personal income tax

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Tax Code

Following the adoption of the Tax Code by the Ukrainian Parliament in December 2010, this Newsletter summarizes key changes related to Personal Income Tax (PIT).

I General provisions

• Tax residence

The tax residence determination for individuals corresponds to the one previously established by the Personal Income Tax Law (PIT Law), providing a number of tie-breaker criteria. Residents are taxed on their worldwide income.

Registered freelancers and private entrepreneurs also qualify as Ukrainian tax residents and therefore, subject to Ukrainian tax on their worldwide income.

• Tax rates

The same tax rates generally apply to tax residents and non-residents.

The standard 15% - 17% rate applies to income received as salary and other benefits under employment and civil agreements, state and non-state lottery winnings or gambling, foreign income and other income not covered elsewhere.

Monthly income less than 10 minimum salaries established as of 1 January of the reporting year (for 2011 – UAH 9,410 per month) is subject to a 15% rate. The balance is taxed at 17%.

A double rate [30% - 34%] applies to income received as winnings or prizes (except for state or non-state money lottery or gambling).

Specific tax rates of 0 – 5% may apply to certain types of income received by tax residents (see Chapter II).

• Tax-exempt income

Generally, all income received or accrued for the taxpayer in any form is taxable, with some minor exceptions:

- Amounts paid by employers for employees' voluntary insurance or to specific educational institutions for employee training, within specific limits and conditions.
- Interest income from current bank accounts which is used solely for the receipt of salaries, scholarships, pensions, social aids and other social payments received by individuals.

Highlights

Personal income tax

- A progressive tax rate of 15-17% for both residents & non-residents.
- Ukrainian dividends are subject to 5% tax.
- A tax residence test is similar to the PIT Law.
- The deadline for filing an annual tax return – by 30 April of the year following the reporting one, although this may be postponed to 31 December in certain circumstances.
- Tax liability is payable on a self-assessment basis by 31 July of the following year.
- The penalty for late submission of a tax return remains the same at UAH 170. The penalty for non-submission is 25% of the tax due.
- Penalties for tax payment delay/non-withholding have decreased to 25%-75% of the tax due for tax agents (non-withholding) and 10-20% for tax payable on a self-assessment basis (payment delay).
- Ukrainian tax agents will be obliged to submit monthly reports in addition to quarterly ones.
- Relations under civil agreements can be considered employment relations if "recognized as such".
- Equity received as a gift or inheritance is considered as bought for a price equal to the state duty and tax paid at the time of receipt.

- Interest from securities issued by the Ministry of Finance of Ukraine.
- State lottery winnings or prizes up to 50 minimum salaries (i.e. currently UAH 47,050).

• Employment benefits

Generally, all employment-related income, including salary and benefits, is taxable. However, additional benefits provided or compensated by the employer are tax free if their provision or compensation is required **for the performance of an employee's labour functions in accordance with the labour agreement (contract) or is prescribed by the provisions of the collective agreement or under the law** and within the limits established by them. Based on this, provision of a housing is taxable if it is not an essential condition for a position (e.g. a driller working long shifts at a site).

• *Effective employment*

A company engaging individuals under civil agreements can be considered an employer of those individuals if "recognized as such". There is no indication which state authority is empowered to make such a decision. This may result in additional social security charges and penalties imposed on the deemed employer.

• *Tax payments by tax agents*

The relevant tax must be transferred to the budget simultaneously with the income payment. If income is provided in cash or in-kind, tax must be transferred to the budget no later than the next banking day.

Banks are allowed to accept documents for income/salary payments only if the calculation of personal income tax transfer to the budget is provided along with them (payment documents for transfer of the tax to the budget, for example).

• *Recalculation of tax*

Employers and/or tax agents are authorized to perform recalculation of incomes accrued and taxes withheld for any period and in any case in order to ensure correct taxation. If, as a result of the final recalculation, an individual taxpayer terminating employment (for example) with a tax agent still has outstanding tax liabilities, such liabilities must be settled by the individual on a self-assessment basis within his annual tax liability.

• *Penalties*

The penalties for late payment or underpayment of tax have been decreased:

- A penalty of 10/20% applies in respect of tax paid late on a self-assessment basis depending on the period of delay (30 days of delay inclusively or more).
- A penalty of 25/50/75% applies in respect of the tax not withheld in full by tax agents (depending on the number of violations over three calendar years).

If a taxpayer does not submit a tax return, or indicates incorrect data in a tax return that results in tax understatement, a penalty of 25% of the additional tax due calculated by the tax authorities applies.

• *Reporting and tax payment*

An individual is obliged to file a tax return if during the year he/she received income from non-tax agents (e.g. foreign income), or income from two or more tax agents, provided the total amount of such income for any month exceeds 10 minimum salaries established as of 1 January of the reporting year (for 2011 – UAH 9,410).

The standard annual filing deadline is 30 April of the year following the reporting one. It can be extended till 31 December based on the taxpayer's application, if the documents for a foreign tax credit need to be obtained from a foreign jurisdiction.

The obligation to file a tax return is deemed to be fulfilled if a taxpayer received only the following incomes throughout the year:

- From tax agents, except for the cases mentioned above;
- From the sale/exchange of property, gifts or inheritance where tax was paid before the notarization of the agreement.

Tax liability due on a submitted tax return must be paid by an individual on a self-assessment basis by 31 July of the year following the reporting one, irrespective of whether the filing extension was applied for or not.

Tax liability additionally calculated by the tax authorities should be paid by the deadline indicated in the tax assessment issued by the tax authorities.

II Special provisions for the taxation of some types of income

• *Interest and dividends*

Ukrainian interest and dividends are subject to tax at a 5% rate with some exceptions. Specifically, an interest income received from current or deposit bank accounts, deposits made with non-banking financial institutions in accordance with legislation or from a deposit certificate is taxable starting 1 January 2015.

• *Rental income*

- No tax deduction of expenses is available.
- Realtors are obliged to report to the tax authorities on rental agreements concluded with their assistance.
- Tax non-residents (individuals) are allowed to rent out their real estate located in Ukraine only through a Ukrainian private entrepreneur or a Ukrainian legal entity which should act as a tax agent. Failure to do so will be considered tax evasion.

• *Investment income*

For taxation purposes, investment assets (e.g. shares) received as a gift or inheritance are considered as bought for a price equal to the state duty and tax paid as a result of gift/inheritance receipt.

• *Foreign income*

Foreign income which is taxable under the Tax Code is subject to rates of 15-17%.

• *Income from disposal of real estate and movable property*

For tax residents, a 0% rate applies to proceeds received from disposal of a house, a flat or a share of such house/flat/cottage if it is the first disposal for the year and the asset was in the individual's possession for more than three years.

A 5% rate applies to subsequent sales of immovable property.

A 1% rate applies to the proceeds received from selling one car, or a motorcycle or a scooter per year. A 5% rate applies to additional sales.

15% and 17% rates apply to incomes from the disposal of movable and immovable property received by tax non-residents.

The tax must be paid before notarization of the sale-purchase agreement.

Income from the disposal of movable and immovable property cannot be lower than the "evaluation price" and for the sale of a car, motorcycle or scooter it cannot be lower than 25% of the price of the same new objects. The evaluation certificate must be provided to the Notary.

• *Income received by tax non-residents*

Income of tax non-residents sourced in Ukraine should be subject to tax under the same order and rates as for tax residents, unless otherwise specified by the Code.

There is also an unclear provision that was in the previous PIT Law, but was not enforced in practice. If "Ukrainian-sourced" income is paid to a non-resident by another non-resident, such income must be transferred to an account opened by a recipient at a Ukrainian bank. The bank should act as a tax agent for this income. In practice, this provision was not functioning and tax non-residents filed tax returns and paid tax due on a self-assessment basis.

There is also a provision that if a non-resident received Ukrainian-sourced income from a non-resident in cash or in-kind, the recipient of such income must pay the tax due within 20 days of the following month. It is unclear how it will work in practice.

For the year when a foreign citizen becomes a tax resident, he/she is obliged to file a tax return, declaring Ukrainian and foreign income.

III A personal income tax at a glance - 2011

Income type	Tax rate
Salary, other benefits under employment and civil agreements, state and non-state lottery winnings or gambling, foreign income and other income not covered elsewhere: <ul style="list-style-type: none"> • up to UAH 9,410 per month • exceeding UAH 9,410 per month 	15% 17%
Winnings or prizes (except for state or non-state money lottery or gambling)	30% - 34%
Interest: <ul style="list-style-type: none"> • from Ukrainian and foreign banks – till 31 December 2014 • from Ukrainian banks – after 1 January 2015 • from foreign banks – after 1 January 2015 	Exempt 5% 15-17%
Dividends: <ul style="list-style-type: none"> • from Ukrainian companies • from foreign companies 	5% 15-17%
Disposal of real estate by tax residents : <ul style="list-style-type: none"> • first sale • second and further sales • first and subsequent sales of property abroad 	0% 5% 15-17%
Disposal of real estate and movable property by non-residents	15-17%