

# Flash Report

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## *Beneficial ownership test*

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## *Tax office focusing on royalties*

As we explained in our recent tax newsletters, the Tax Code (and most Ukrainian double tax treaties – “DTTs”) provide for a beneficial ownership test to determine if withholding tax on income payable from Ukraine could be reduced under a DTT.

We are now aware that the central tax authorities have recently expressed their opinion in respect of beneficial ownership on royalties (through an internal letter to other tax offices). They opine that only an owner of an IP object (but not a licensee) may be considered as a beneficial owner of royalty income. This restrictive interpretation is likely to have a significant negative (retroactive?) impact on any businesses in Ukraine that have entered into sub-licensing agreements with non-residents.

We fully disagree with such an approach, as the Code and DTTs refer to the beneficial owner of income and not of intellectual property itself. If a non-resident is beneficially entitled to the income, then she/he should be entitled to the treaty relief.

Nevertheless, if taxpayers are using the reduced treaty rates when making royalty payments to non-residents in respect of sub-licensing agreements, they should be prepared to be challenged during the next audit process and through a subsequent uncertain court process.

Considering the undeveloped concept of beneficial ownership in Ukraine and the most recent tendencies in court practice (i.e. favoring the tax authorities), taxpayers should be prepared to defend their position through a lengthy court procedure.