

Doing business and investing in Ukraine

2011 Edition

Partner's letter



Boris Krasnyansky

Managing Partner

I am very pleased to present the 2011 edition of our guide: **Doing Business and Investing in Ukraine**. The guide is based on laws as at 1 March 2011 and information made available through February 2011. This has been prepared due to a number of significant changes that have been implemented since the publication of our 2010 edition, in particular the introduction the new Tax Code.

Ukraine, like many other countries in the region and around the globe today, continues to face exceptional economic challenges. So far the country has weathered the storm better than expected. Clearly, its geographic position and natural resources, as well as the "human factor", have all played key roles in this achievement. Ukraine's proximity to both the European Union and Russia, the sheer quantity of its consumers (46 million) and the physical size of the country make it an excellent location for businesses to expand both locally and regionally. Preparations for the 2012 UEFA European Football Championship are on track and will stimulate interest in Ukraine and help in the development of infrastructure and the tourism industry. Accession to the WTO has accelerated trade and placed another layer of protection on investments and the anticipated free trade agreement with the EU will further increase opportunities. Recent implementation of the comprehensive Tax Code and a number of other legislative improvements over the past twelve months are very positive steps. These and other measures should markedly improve Ukraine's ratings in the World Bank ease of doing business index in the medium term and should make Ukraine an attractive investment location.

Since 1993, PricewaterhouseCoopers has been advising companies and individuals on how to do business 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 Ukrainian 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 some valuable insight into the Ukrainian market and make you better prepared to meet the challenges ahead. More detailed advice should be sought.

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

March 2011

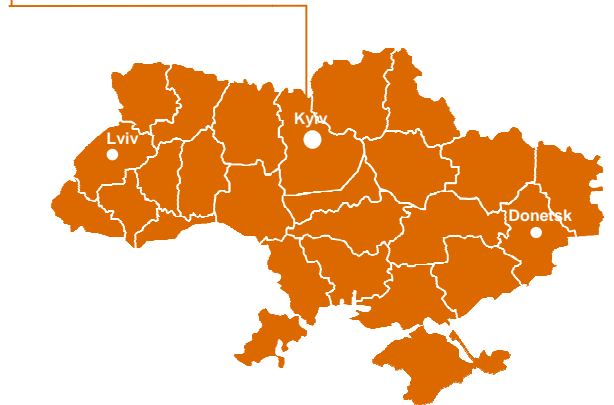
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Office locations in Ukraine



PwC offices in Ukraine are located at the following addresses:

Kyiv office

75 Zhylyanska Street
Kyiv, 01032
Tel.: +380 44 490 6777
Fax: +340 44 490 6738

Donetsk office

2-A Pushkina Boulevard
Donetsk, 83001
Tel.: +380 62 341 4700
Fax: +340 62 341 4690

Lviv office

72 Heroiv UPA Street
Lviv, 79015
Tel./Fax: +380 32 242 5305

***Laws and regulations change constantly.
For updated information, please check
our website: www.pwc.com/ua***

1



Country profile and investment climate

Investor considerations

- *Ukraine has a population of 45.8 million people. The population has decreased by 6% since 2001. The population is 54% female.*
- *Real growth rate per annum exceeded 7% from 2000 to 2008, but the global financial crisis caused a 15% decline in GDP in 2009.*
- *GDP for 2010 was USD 133.6 billion-and is forecast to grow by 4.5% in 2011.*
- *In 2010, the IMF approved a USD 15.3 billion stand-by arrangement program for Ukraine to support the government's economic adjustment and reform program.*
- *Hints for business visitors may be found in Appendix A.*

1.1 Introduction

Ukraine, located in the heart of Eastern Europe and occupying a land area of 603,700 sq km, is the second largest country in Europe after Russia. It is bordered by 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 August 24, 1991 following the dissolution of the Soviet Union. On December 1, 1991, 90.3% of voters approved a referendum formalising independence from the Soviet Union. The Union formally ceased to exist on December 25, 1991, at which time Ukraine's independence was officially recognised 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 Yanukovych was elected president of Ukraine.

Legislative power is exercised by a single-chamber parliament called the Verkhovna Rada, which is comprised of 450 deputies who are 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. The prime minister is appointed by the parliament based on a submission from the president. The prime minister is Nikolay Azarov and he heads a coalition government that

fully supports the president. 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. The current government is expected to be stable until the 2012 elections.

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, lays out the structure of the national government along with its powers and functions. The powers of government are divided into three branches - legislative, executive and judicial.

Laws adopted by the parliament are forwarded to the president for signing. If the president signs the law or fails to act within a 15-day period, the law should be officially signed and officially promulgated. The president has the right to veto legislation within the 15-day period, but the veto can be overridden by a 2/3 majority of the parliament.

The Constitutional Court of Ukraine is the sole organ of constitutional jurisdiction in 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. Those judges then 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 Highest Specialised 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 Highest Commercial Court of Ukraine.
- 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 Highest Administrative Court of Ukraine.

Under Constitution of Ukraine, the Supreme Court of Ukraine heads the judicial system of Ukraine, which has the power to review decisions of all three branches of the

court system. However, due to the 2010 judicial reform the powers of this Court were significantly decreased, while the highest courts of all three branches became the courts of last instances and obtained a right to admit the cases for reconsideration to the Supreme Court of Ukraine by their sole discretion.

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 allows for arbitration by international arbitration institutions.

1.4 People

Population

Ukraine's population was estimated at 45.8 million people at the end of 2010, which is 6% lower than the population recorded in the 2001 census. Five cities have a population close to or exceeding one million people, including the capital Kyiv with 2.7 million people.

Ukraine does not allow 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, the latter of which mostly reside 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 outside of Kyiv. Many government websites have an English language 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 2,239 (USD 282) in 2010. Average salaries in Kyiv were 50% higher than in the rest of the country. Many companies continue the practice of paying salaries “in envelopes” and therefore, official numbers may not accurately reflect the actual level of personal income.

Despite these statistics, Ukraine has developed an affluent middle class. Minimum rents in Kyiv are between USD 300-400 per month. Ukraine has been one of the fastest-growing passenger car markets in Europe through the last half of 2000's. Although the market collapsed in 2009, it has since started to rebound. Restaurant prices in Kyiv are approaching, if not exceeding, those of major European cities.

Ukraine has a sizeable unofficial and underground economy. The government in 2010 estimated the size to be about 40% of GDP, while many analysts suggest that the true level is even higher.

Unemployment

In January 2011 the official unemployment rate was about 8%, but the actual rate is likely to be higher.

1.5 Economy

The Ukrainian economy grew at an annual rate of over 7% from 2000 to 2008 and actual GDP reached UAH 950 billion (USD 180 billion). However, in the fall of 2008, the global economic crisis exposed Ukraine's macroeconomic vulnerabilities, resulting in a contraction of industrial production, a devaluation of the national currency, and a severe credit crunch. In 2009, GDP contracted by approximately 15%. It has since rebounded, having grown 4.2% in 2010 with growth and forecast to grow further 4-5% in 2011.

In July 2010, the IMF approved a 29-month standby arrangement (SBA) in the amount of SDR 10 billion (about EUR 11.7 billion, or USD 15.3 billion) in support of the authorities' economic adjustment and reform program. The SBA provides exceptional access to IMF resources, amounting to 728.9 percent of Ukraine's quota in the Fund. In December 2010, the Executive Board of

the IMF completed the first review of Ukraine's economic performance under the program supported by the SBA. The completion of the review enabled the immediate disbursement of SDR 1 billion (about EUR 1.2 billion, or USD 1.5 billion). Drawing the full amount would bring total disbursements under the program to SDR 2.25 billion (about EUR 2.6 billion, or USD 3.4 billion).

Transport

Ukraine has a well-developed transportation infrastructure and is readily accessible by land and air. It has 22,000 kilometres of railway, 169,400 kilometres of highways and 16 airports that are open to commercial air traffic. Most international flights go to Boryspil International Airport, about 29 km 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 rapidly expanding in recent years. The three main mobile operators have a total of more than 30 million subscribers. The number of internet users is estimated at more than 12 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 trading partner, accounting for only 2.2% of exports and 3.2% of imports. In 2010, metals accounted for more than 33% of Ukraine's exports. 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 its economic and foreign policy.

2



Business environment

Investor considerations

- *Ukraine remains a challenging place in which to do business.*
- *Ukraine joined the WTO in 2008.*
- *Ukraine has a comprehensive free-trade agreement with Russia and is negotiating another with the EU, which is expected to be signed in 2011.*
- *Many investment opportunities exist, but Ukraine is still developing the legal and institutional frameworks required to fully support international business.*
- *There was a dramatic drop in the real estate market during the 2008-2009 economic crisis (prices declined by about 50%). It has yet to pick up, although commercial rents are now increasing again.*
- *The European football championship, to be hosted by Ukraine and Poland in 2012, is expected to have a positive impact on the development of the economy and the building of 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 of over 7% over the period of 2000 to 2008. This growth was fuelled 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, but experienced a recovery in 2010 as global conditions continued to improve. The recovery is continuing in early 2011.

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 for the 2012 UEFA European Football Championship may energize the construction industry.

Ukraine allows foreigners to purchase businesses and property (with the exception of agricultural land), repatriate revenue and profits and receive compensation if property is nationalised. 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 an 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, decreases in the values of acquisition targets, delay of deals due to fair pricing difficulties and other economic uncertainties. Low activity in the M&A market remained an issue throughout 2009 and 2010, but there are signs of improvement in 2011.

At first glance, taxes appear quite low - 23% for corporations and 15-17% for individuals, while value-added tax (VAT) is 20%. However, there are certain issues:

- Restrictions on deductions mean the effective corporate tax rate is closer to 30%.
- Social security contributions can be significant. In 2011, 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 1,775 per month (see Chapter 7.3 for more information).
- VAT refund constraints combined with restrictive rules for zero-rating sales of services to non-residents means that VAT can become a significant cost to doing 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 2011 study put Ukraine in 145th place out of 183 countries when it comes to ease of doing business. However, the study pointed out that reforms have improved investor protection in Ukraine. The government has introduced more legislation that should substantially improve this rating in future years.

2.2 Economic development plans

President Victor Yanukovich and the government are currently developing a comprehensive development plan.

2.3 Free trade zones

There are currently no free trade zones in Ukraine.

2.4 European Union, NATO, WTO

In 2005, then President Victor Yushchenko stated that membership in the EU was a strategic goal of his foreign policy and current President Victor Yanukovich has confirmed this as well. 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 Organisation approved Ukraine's accession on 5 February 2008 and Ukraine became the WTO's 152nd member on 16 May 2008.

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 Organisation (WTO) as well as a number of other international organisations. It 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, the avoidance of double taxation and mutual guarantees of investments. It has a free-trade agreement with Russia and other countries of the Commonwealth of Independent States (CIS) and is now negotiating a free-trade agreement with the EU, which is expected to be signed in 2011.

2.6 Legal environment

The Ukrainian judicial system was significantly reformed in 2002. Judges are appointed by presidential decree for five-year terms, after which the parliament confirms them for life.

Although the system has improved significantly since 2002, 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 are underfunded which means they are often understaffed,

and 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 of 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 and 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 30-40 per square metre.

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 is likely to take years before the market again reaches 2008 levels.

2.8 Foreign investor associations

There are a number of foreign business chambers in Ukraine including the American Chamber of Commerce (www.chamber.ua) and the European Business Association (www.eba.com.ua). Both chambers have active committees on various issues affecting business and investors in Ukraine. There are also business associations for German, British and Japanese businesses, among others. 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 and are gradually being removed.*
- *Silent approval is (theoretically) available for many permits and licences.*

3.1 Foreign investment

Investment climate

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

In general, 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).

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 for foreign direct investments, but must register with the state authorities. Registration as a foreign investment may also ease the restrictions of remittance of dividends abroad.

Many 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 and/or random delays.

Stock of foreign direct investment amounted to more than USD 45 billion at the end of 2010. Foreign direct investment in 2010 was slightly less than USD 4.7 billion, compared to USD 4.4 billion in 2009.

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 matters. The following major pieces of legislation – in addition to taxation laws – 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* (enacted on the same day as the Civil Code) 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 carrier rockets and from some publishing activities.

Investment incentives

The Tax Code has introduced a number of tax initiatives for a range of investors (see Chapters 9-12 for further information).

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.

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 prompt and unimpeded repatriation of profits.

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

Since late 2009, the procedure for obtaining licences has been simplified, although in practice, difficulties remain.

A "silent consent" principle is established for obtaining most, but not all, permits (licences). If an application for a permit (licence) 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 [licence] or reject the application), the applicant is allowed to pursue the activities as if the permit (licence) had been issued. It is uncertain how this will work in practice.

Licences 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 licence. However, even in such a case, the term of validity will be not less than five years.

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

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. In 2002, the Cabinet of Ministers of Ukraine issued an annual list of enterprises to be privatised in the respective year, but this has not always been followed in practice.

The Kryvorizhstal sale to Mittal Steel in 2005 demonstrated that transparent privatisation sales in Ukraine are possible. However, growing political and economic crises in subsequent years intensified disagreements between the branches of government about the privatisation of strategic enterprises.

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 often 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). It was planned to sell a 92.8% stake by 2000, but it never materialised.

The privatisation list for 2010 included several attractive companies including the large industrial engineering and manufacturing enterprise Luhanskteplovoz.

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 move toward reducing the number of banks and insurance companies in Ukraine.*
- *A full range of traditional banking services is available in Ukraine, although intermediation costs remain high.*
- *According to the WTO accession document in 2008, branches of foreign banks should be permitted to enter Ukraine, but the 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 beginning in 2013.*
- *There are no requirements to convert foreign currency export proceeds into hryvnia (UAH).*

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 prices, 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 the parliament, seven by the president, whilst the governor (who acts ex-officio as the fifteenth member) is nominated by the president and appointed by the 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 substantial 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 the hryvnia and the plunge in real estate prices since 2008.

Banks are required to prepare accounts that are based on international financial reporting standards (IFRS).

As at 1 January 2011, 195 commercial banks were registered in Ukraine, out of which 176 have been granted licences by the NBU to perform banking transactions. There are about 30 representative offices of foreign banks.

The Ukrainian banking sector is highly concentrated. According to 2011 data published by the NBU, about 30% of the banking sector's total assets were held by the ten largest Ukrainian banks. According to the NBU as at February 1, 2011, the total loans granted by banks amounted to UAH 755 billion (USD 95 billion), and their total statutory capital amounted to UAH 146 billion (USD 18.4 billion). At least 55 banks in Ukraine had some foreign capital, of which 20 were fully owned by foreign owners. Approximately 40% of the total statutory capital of all Ukrainian banks belonged to those with foreign capital (including four of the ten largest).

Commercial banks require a licence 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 that:

- 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 (a specific licence is required);
- salaries to Ukrainian staff must be paid in UAH currency (but expatriate employees can be paid in hard currency);
- foreign loans must be registered with the NBU before funds are remitted to Ukraine. There is a maximum interest rate (including other charges) that may be applied to foreign currency loans obtained from non-residents;
- the maximum allowable interest rates for foreign fixed rate loans in hard currency is 9.8% p.a. for loans up to 1 year; 10% p.a. for loans for 1-3 years and 11% p.a. for loans over 3 years. For loans with floating interest rates, the maximum allowable interest rate is three months 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;
- 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. The process cannot be taken lightly as if the FMMC rejects an application, no payment will be permitted.

Both Ukrainian companies and individuals are required to obtain a licence 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.

Neither Ukrainian companies nor individuals can borrow funds to make investments abroad.

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), the number of leasing operations

had been increasing every year up to 2009, but has since slowed down.

Transport, farm machinery and construction equipment constitute 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 profits 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. This is gradually showing signs of improvement.

Asset management companies, licensed by the State Securities and Stock Market Commission of Ukraine, are permitted to manage assets of both corporate and unit and non-governmental 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 capitalisation. Thus, in 2009, the volume of trading through the PFTS Stock Trading System (www.pfts.com/eng), the largest stock exchange in Ukraine, dropped dramatically due to the unfavourable business environment. In 2010, Ukraine improved and was one of the best performing exchanges in the world.

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. More than 451 insurance companies are currently operating in Ukraine, 70 of which in the area 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 in 2010. 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.*
- *Ukrainian customs valuation rules generally comply with WTO rules.*
- *Goods imported into Ukraine are subject to customs duties, excise tax (if applicable) and value-added tax (VAT).*
- *Ukraine has a free-trade agreement with Georgia, the CIS countries and Macedonia and is negotiating another with the EU.*
- *The customs authorities scrutinise customs values and the classification of imported goods and post-entry customs audits have been implemented.*
- *A new customs code is expected to be implemented in June 2011.*

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. A modernized draft Customs Code is debated in parliament.

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 and 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 the 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. However, 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. Goods cannot be imported into Ukraine without this document.

Moreover, 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 and 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 (2007), 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 should be 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.

The customs authorities have recently announced their official position in respect of customs treatment of royalties and according to it, royalties relating to patents, industrial patterns, certain types of plants, animal breeds, trademarks and copyrights are dutiable in most cases. This

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

Free-trade agreements

In addition to the reduced rates mentioned above, Ukraine has concluded free-trade agreements with Georgia, the CIS countries and Macedonia. Ukraine has also signed a free-trade agreement with the EFTA countries, although it is not yet in force. 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.

The government is negotiating an FTA with the EU and the president has indicated that his goal is to have this signed in 2011.

Excise tax

Excise tax is payable on cars, car bodies, alcoholic beverages, tobacco products, beer and 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 Tax Code (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 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 EUR 20 to EUR 50 for the work of one customs inspector.

Payments

Import duties and taxes are payable by the importer in UAH 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;

Partial exemption from VAT is available for goods imported into Ukraine to be temporarily used for production or work projects. The amount of VAT paid should be 3% for every month or part of a month during which the goods have been temporarily imported of the amount which would have been charged if the goods concerned had been cleared for home use. Partial exemption from customs duty has not been implemented yet.

Temporary importation is allowed for a maximum of one year, but can be extended by the customs authorities.

5.5 Customs duties incentives

Charter capital contributions

Property (except for resale goods) contributed by a foreign investor to the charter capital of a Ukrainian entity or to joint investment activity 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 (including VAT), provided the finished products are re-exported from Ukraine within 90 days. To comply, 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 (owner of the goods) in Ukraine after import duties have been paid. However, the procedure of sales are not regulated and therefore, this is problematic in practice.

Repairs, assembly

A VAT exemption applies to the 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 the carrier media, which is to say that the cost or value of the computer program should not be taken into account.
- Generally, interest charges 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 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 Customs control

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, along with 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 support the declared 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 only be used 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 a licence from 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.

Starting from October 2010, the government introduced quotas on grain exports as well.

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 the 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. At the current stage the customs authorities view customs audit as a priority area of customs control.

As a rule, audits focus on customs valuation, classification issues and eligibility for exemptions. In recent audits, the customs authorities have focused on the customs treatment of royalties.

Areas of customs audits

In future customs audits, the customs authorities will also review:

- classification of imported goods, specifically in cases where revised tariff codes would attract higher amounts of customs duty and VAT;
- country of origin of imported goods, especially in cases where the goods were imported free of customs duty under free-trade agreements.
- inclusion into customs value of imported goods of artwork, design and engineering works.

- verifying prices of imported goods between related entities and revealing whether relations could impact the customs value of imported goods.

Customs audits include scheduled and unscheduled field and desk audits.

Scheduled customs audits

The customs authorities need to inform business entities about the scheduled audit 10 calendar days in advance. The duration of a scheduled audit is 30 days, which can be extended to up to 15 days more. The customs authorities may carry out a scheduled audit of an entity once a year.

Unscheduled customs audits

No advance notification is required for an unscheduled customs audit. Unscheduled customs audits may be carried out at random, for example, if the customs authorities were to have reasonable cause to believe a violation of customs law by the business entity had taken place. Unscheduled customs audits can last for an unlimited amount of time.

During field audits, the customs authorities may analyse customs, financial, accounting and warehousing documentation.

Assessments

The Tax Code establishes that customs audits cover a three-year period.

If the customs audit detects an underpayment of duty and VAT, penalties from 25% to 75% of the underpayment may apply. Late payment interest at the rate of 120% of the National Bank rate is applicable in the case of breaching of conditions of exemption from customs duty and VAT.

The appeals procedure is similar to that of the tax authorities. (see section 9.10 below).

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 130. The minimal share capital for JSC is USD 148,000.*
- *Since late 2010 the procedure of registering an LLC established by a non-resident entity has become more complex due to introduction of changes into anti-money laundering legislation.*
- *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 130) and is less regulated.

At the same time, recently amended (in late 2010) legislation covering this area requires the identification of an LLC's ultimate shareholders during its state registration in Ukraine. Namely, the founders (legal entities) have to disclose their ownership structure up to the level of individuals with a significant shareholding (10% of shares or more).

Due to lack of developed practice, additional data/documents may be required from the state authorities as to disclosure of the ownership structure.

This requirement does not apply to a case where an entity is first established by a physical individual and his corporate rights are further sold to a non-resident company (i.e. ultimate founder).

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, 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 have the right to initiate liquidation proceedings against JSCs which violate the net assets rule and they tend to scrutinise this issue (particularly for banks and insurance companies). As for the LLC, the procedure for initiating liquidation is not clear and we are not aware of any company being liquidated due to non-compliance with the net assets rule. However, this is likely to change from 2011 as the tax offices will have access to financial statements.

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 months notice. Upon withdrawal, a participant is entitled to his proportionate share of the assets of the LLC, which often involves a 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 financing 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 aforementioned 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, provided they do not 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, 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 1 March 2011, it was approximately USD 130.

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 an LLC.

Relationship of participants, directors and officers

LLCs have two corporate bodies.

The Participants' Meeting consists of the participants of the LLC, who vote proportionally to their interest in the LLC's charter capital. The Quorum for a Participants' Meeting 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' Meeting, 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 single 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 parties. There is no formal requirement to appoint a company president, corporate secretary or any other officeholder. 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 it, its corporate term expires (if one is specified in the Charter), or it is ordered to be liquidated by a court. In a voluntary liquidation, preference in distribution is given as follows:

1. Indemnification of losses caused by disability, other health injuries or death, as well as creditors' demands secured by pledge or otherwise;
2. Employee 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. 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 either "public" or "private".

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 1 on page 27.

Shares

- By 30 April 2011, all shares of the JSCs have been dematerialised (transferred from documentary into non-documentary form).
- Shares in a public JSC may be sold through a 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 included into the stock list of at least one stock exchange in Ukraine. Shares of public JSCs may be purchased or sold on the stock exchange.

Corporate

- The number of shareholders in a private JSC may not exceed 100.
- All shareholders must be notified in writing of the General Shareholder's Meeting 30 days before said meeting.
- Cumulative voting will be either mandatory or voluntary (depending on the type of 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 the 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 to 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.
- A 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 a month.

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 minimum capital requirements for JSCs at March, 2011 was 1,176,250 (USD 148,000). 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 shareholder agreements;

- possibility of requesting the mandatory buyout of shares in cases provided for by the JSC Law.
- introduction of new rules for share acquisition;
- disclosure of conflicts of interest during acquisitions.

Reporting requirements

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 a Tax ID 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 employees. 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 with which to contend. A partner may still withdraw by giving three months 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 in this manner.

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.

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 upon standard regarding how the titles of laws should be translated. For example, the Commercial Code is often referred to as the Economic Code.

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 English 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.

6.10 Brief comparison of joint stock companies and limited liability companies

Table 1

	Joint stock company (JSC)	Limited liability company (LLC)
Registration	Primary registration is made with the State Registration Department. JSC shares must be registered with the State Securities and Stock Market Commission.	Registration is made with the local State Administration.
Minimum capital	1,250 Ukrainian monthly minimum salaries (approximately USD 148,000).	One Ukrainian monthly minimum salary (approximately USD 130).
Transfer of shares	There are generally no restrictions on the transfer of shares in a public JSC. There are specific regulations regarding significant shareholdings and mandatory buyouts. In a private JSC, the existing shareholders may have a pre-emptive right to purchase shares.	Unless the Charter sets forth otherwise, the existing participants have a pre-emptive right to purchase the participant's share in LLC.
Supervision	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.
Management requirements	<ul style="list-style-type: none"> The General Shareholders' Meeting and the Supervisory Board (not required if there are less than 10 shareholders). Single Director or a Board of directors headed by the General Director, or another body stipulated in the Charter. Audit Committee or Internal Auditor (if there are fewer than 100 shareholders). 	<ul style="list-style-type: none"> The Participants' Meeting. Single Director or the Board of Directors headed by the General Director.
Statutory audits	There is a requirement to submit an annual audit report to the State Securities and Stock Market Commission.	Not directly required by the law. In practice, most LLCs do not conduct audits
Risks	Liquidation if the net assets are less than the minimum requirements of the law.	<ul style="list-style-type: none"> Liquidation if the net assets are less than the minimum requirements of the law. Participants may withdraw from the LLC at any stage with a three month notice.
IFRS	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.
Minimal dividend payment	Not required	Not required
Reserve capital	Not less than 15% of share capital	Not less than 25% of share capital



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 1,775 per employee per month applies to the income subject to contributions).*
- *The new Law "On Collection of and Accounting for the Unified Statutory State Social Insurance Contribution" entered into force on 1 January 2011. This Law has simplified the procedure.*
- *Companies with more than eight employees are required to employ disabled individuals for 4% of their headcount. Failure to do so attracts substantial penalties.*
- *The government has announced that the new Labour Code should be in place by 1 June 2012.*

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 the 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 called 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.

In late 2010, the government announced that they would be introducing a new Labour Code that shall be made in line with Western principals. At this stage we expect the Code to be implemented by June 2012.

7.2 Working conditions

Salaries and wages

Minimum salary levels are prescribed in the annual budget law. According to the 2011 Budget Law of Ukraine, the minimum salary as of 1 January 2011 is set at UAH 941 (approximately USD 118) 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.

Working hours

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

According to labour legislation, employers may introduce overtime in exceptional cases. The legislation 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, women with a disabled child or a child under the age of 14. The law also grants a shortened working day or working week 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 social leave to be granted to

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

Employees engaged in part-time studies may also be entitled to additional study 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 eight 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 reorganization 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 for women (planned to increase to 60 within the next five years) 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 provides for child and family allowances.

Contributions

Ukrainian mandatory state unified social contribution applies to all salaries paid through the payroll of a Ukrainian entity or a Ukrainian representative office of a foreign entity, as well as remuneration paid to individuals under civil agreements. In addition, it is possible for individuals to contribute voluntarily to the Ukrainian mandatory state unified social contribution (up to the cap established by law).

The taxable base for contributions (both employee and employer) is capped. For 2011, the cap is set at 15 times the subsistence minimum set for able-bodied individuals (based on the subsistence minimum valid as of 1 January 2011 the cap is approximately USD 1,775 per month). The cap will be gradually increased to approximately USD 1,900 by the end of the year.

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), unified social contribution is withheld by the employer at the source from salary payments and remitted directly to the appropriate authorities.

For 2011, Ukrainian and foreign national employees' contribution is 3.6% (based on gross remuneration/cap). For individuals providing entities with services based on civil agreements, the contribution is 2.6% (based on gross reward/cap).

Individuals remaining on a foreign payroll are not liable to pay mandatory unified social contribution in Ukraine.

Employers' contributions

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

For 2011, the following rates apply to gross remuneration: 36.76% - 49.7%, depending on the level of risk of accidents in the entity's industry sector (34.7% for remuneration of services based on civil agreements).

Administration

Employers are required to file a monthly personified report with the Pension Fund of Ukraine by the 20th of the month following the reporting month.

Penalties for non-compliance

There are severe penalties for non-compliance with social security obligations:

- Avoidance of registration or untimely registration is penalised in the amount of 10 times the minimal amount of income not subject to personal income tax (currently approximately USD 20).

- Non-payment or delay with payment of contributions is subject to a penalty in the amount of 10% of the outstanding amounts/amounts paid late.
- Contributions additionally calculated by the Pension Fund or employer should be paid together with a penalty of 5% of that additional contribution for each month of delay, but not more than 50% of that additional contribution.
- Late reporting or non-reporting attracts a penalty in the amount of 10 times the minimal amount of income not subject to personal income tax (currently approximately USD 20). Inappropriate bookkeeping attracts a penalty in the amount of 8-15 times the minimal amount of income not subject to personal income tax (currently approximately up to USD 30).

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).

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 resident 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- see Appendix A). The stamp affixed to the foreign national's passport by a Frontier Service officer upon the initial entry into Ukraine is considered an automatic registration for a period of 90 days (cumulatively) in Ukraine, unless a shorter period is specifically indicated in the visa.

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 no later than three working days before the three-month period expires. The extended registration

will be evidenced by a registration stamp affixed to the foreign national's passport.

Foreign nationals that have 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 a temporary basis at their WTO residing employer's subsidiaries 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 copies 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 three 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 employers:

- Fines in the range of UAH 170 – 20,000, 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 reality, there are gaps between the two.*
- *JSCs are subject to an annual audit requirement and must publish their annual financial statements. These requirements do not apply to LLCs.*
- *From 1 April 2011, tax accounting is directly connected to financial accounting. Tax officials are not familiar with accounting standards and this could lead to disputes.*
- *The short form Chart of Accounts can 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 them. As at January 1, 2011, 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 with 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 do IFRS, which inevitably leads to some confusion in the application of local standards. This undermines the comparability and quality of financial statements in Ukraine. From 1 June 2011, corporate tax profit will be based on the statutory financial statements. This is in contrast to the past, when there was separate tax accounting. The tax office and many chief accountants are not familiar with NR(S)AU / IFRS. This is likely to result in considerable confusion in the first few years.

The adoption of the 2011 Tax Code results in additional matters to consider. Deferred tax calculation, applying the new tax base for the fixed assets and new corporate income tax rates have the most significant impact in accounting. The new tax code seeks to reduce the number of differences between tax and accounting records, for example in implementing new rules on the timing of recording expense and revenue in tax records. However, certain temporary differences between tax and accounting balances will remain, affecting deferred tax calculation. The new tax code requires completing a count of a company's fixed assets as of 1 April 2011. The fixed assets are to be adjusted in the tax accounting records to match the values in the statutory accounting records except for the effect of valuations completed after 1 January 2010. The corporate profit tax rate will decrease gradually from the current 25% to 16% effective starting 1 January 2014 (23% from 1 April 2011). These new rates have to be applied in calculating the deferred tax balance.

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 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-governmental organisations 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 Ukrainian Chamber of Auditors (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. the Law on Financial Services and State Regulation of Financial Services Markets, the Law on Banks and Banking Activities, the Law on Securities and Stock Market, the 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 comprehensive Tax Code implementing significant changes to existing legislation entered into force on 1 January 2011.*
- *A 2011 World Bank study concluded that Ukraine was one of the most difficult countries in which to pay taxes out of 183 countries surveyed. This is due more to the administrative burden than the underlying tax rate (including social security administration).*
- *Individual tax residents are taxed on worldwide income. Non-residents are taxed only on income from Ukrainian sources. Both resident and non-resident individuals are taxed at progressive tax rates of 15-17%.*
- *Corporate profits are subject to 23% tax in the 2nd – 4th quarters of 2011. The tax rate will be gradually reduced to 16% by 2014.*
- *There is a simplified tax system for private entrepreneurs, which allows them to pay up to UAH 200 per month (USD 25).*
- *The VAT rate is 20% and is to be reduced to 17% by 2014. It is not fully consistent with EU legislation.*
- *With the exception of agricultural enterprises, the fiscal year is the calendar year.*
- *There are penalties of up to 75% 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

Ukraine is not an easy country in which to pay taxes. In *Doing Business 2011* 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-sized domestic business would need to make 135 tax payments each year (including social security), and would require 657 hours per year to be compliant with its tax requirements.

In 2010, the first significant tax reform aimed at improving the investment climate in Ukraine took place with the introduction of the Tax Code (entered into force on 1 January 2011). The Code implies significant amendments to tax rules and administration; but there are still many clauses with unclear wording, which may lead to ambiguous interpretations and disagreement between taxpayers and the tax authorities. There are likely to be amendments introduced throughout 2011.

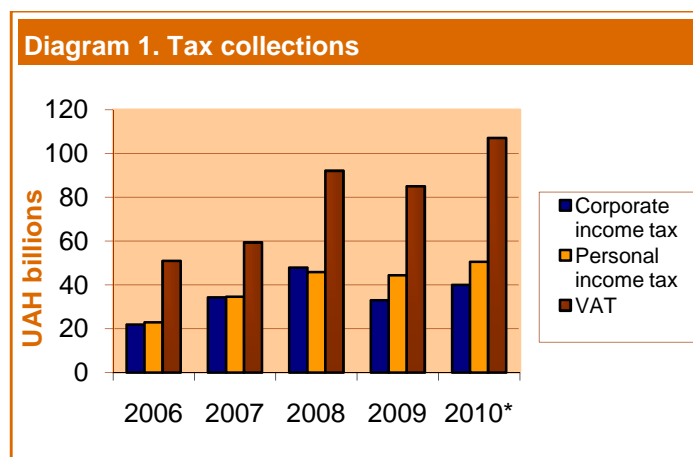
An interesting feature of the Ukrainian tax system is a simplified or unitary tax available for many small businesses. Qualifying sole proprietors opting to use the system pay a fixed amount of tax. The corporate tax regime is discussed in Chapter 10.1, while the regime for private entrepreneurs is discussed 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. Although, the form over substance concept continues to dominate in Ukraine, this is likely to change (for example, the Tax Code provides for a beneficial ownership test).

In order to improve the investment climate in Ukraine and stimulate the growth of small businesses, a number of measures including tax holidays have been introduced for some sectors of the economy (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 collection has increased rapidly over the past five years. The trend in income tax and VAT collections for the period 2006 to 2010 is illustrated in diagram 1.



Source: Ministry of Finance

* in forecast

9.3 Principal taxes

The Tax Code provides the general framework for taxation in Ukraine and sets the 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);
- single social security contribution (see Chapter 7.3);
- excise tax and import duties (see Chapter 5);
- land tax (see Chapter 10.6);
- stamp duty (see Chapter 10.6);
- rental fee for oil and gas (see Chapter 10.6);
- subsoil usage fee (see Chapter 10.6).

Starting from 1 January, 2011, the administrative burden on employees and employers was reduced by unifying the social contributions into a single social security tax. In 2011, employers and employees are obliged to make a single mandatory contribution to the state social security fund. The 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).

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. However, in practice, the

STA often issues tax clarifications (general and individual) that are not always consistent with the law; although this could be a reflection of ambiguities in the law itself as much as anything else. The STA is only able to issue individual clarifications from January 1, 2011, which are not binding.

In practice, it is prudent to consider STA interpretations that substantially reduce the risk of conflict with the STA.

9.5 Tax treaties

As of December 2010, Ukraine had 67 double tax treaties in effect out of 69 ratified.

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 should be provided to the tax authorities no less than once every two years.

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 expected to be renegotiated in the nearest future, but the exact date is uncertain.

In addition to the above, the Tax Code requires the recipient of all types of income from Ukraine to be the beneficial owner (actual recipient) of the respective income. Agents, nominee holders and other intermediaries in respect of the received income cannot be beneficial owners of income sourced in Ukraine, and, therefore, are not entitled to favourable treaty provisions.

9.6 Administration of the tax system

National and local taxes are administered by the STA.

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. 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 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 the source (e.g. salaries) are not required to file income tax returns. Personal income tax returns for individual must be filed by 30 April of the following year. Tax returns for private entrepreneurs must be filed by 9 February of the following year.

Corporate income tax returns are filed on a quarterly basis based on cumulative results, 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 no later than the date the income is paid abroad.

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 should be filed in electronic form by all businesses (except small).

Payment of taxes should be generally made within 10 calendar days from the day on which the return is required to be filed or the assessment is issued. Payments are normally made through 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 regional tax office which supervises the tax office that made the assessment. If an appeal is rejected, a taxpayer may appeal in turn to a national office.

An administrative appeal must be filed to the relevant level of the tax authorities within 10 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 administrative court system (there is no separate tax court system).

Submitting an appeal (both administrative and court) 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 finally fails to win the case.

The taxpayer cannot ground administrative or court appeal on the documents not provided to the tax authorities in the course of the tax audit.

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 (and, in some cases, to sole proprietors) and payments to non-residents. Penalties of up to 75% 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 the 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 are not subject to withholding. However, the resident payer is required to pay a 20% tax based on the value of such services from its own cost.

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 the requirements set by the authorized 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 frequency of the scheduled audits performed by the tax authorities depends on the risk rate of activities carried out by a taxpayer. In general, the frequency of scheduled tax audits for high-risk business is limited to one time per year. Business entities must be notified of the audit in writing at least 10 days before the scheduled audit. The scheduled audit should be carried out within a maximum of 30 business days (i.e. for large taxpayers – 30 days, for small – 10 days, for others – 20 days), although the period may be extended by up to 15 days (15, 5 and 10 days respectively depending on the size of the taxpayer).

In addition, the tax authorities may perform unscheduled audits in any of the following circumstances:

- A taxpayer does not respond within 10 days to a request for information from the tax authorities when the latter 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 submits adjusting tax returns for periods covered by the audits of the tax authorities.
- A taxpayer initiates an appeal process against an assessment.
- A business entity is reorganized or liquidated.
- A taxpayer claims a VAT refund for an amount exceeding UAH 100,000.
- If a taxpayer does not provide with VAT invoice or provides with an invalid VAT invoice and a respective claim is submitted, the taxpayer does not respond to the written request from the tax authorities within 10 days from the date of receiving the request.
- Court, investigation authorities, state investigator or public prosecutor takes a decision within a criminal case.

- The tax authorities of the higher levels within an inspection of the tax authorities of the lower levels opens a criminal case or starts an internal investigation after some discrepancies in the tax audit act with legislation in force were observed.

The duration of an unscheduled audit cannot exceed 15 business days for large taxpayers (5 and 10 days for small and other taxpayers respectively), but may be prolonged by an additional 10 business days (2 and 5 days respectively). Before starting an audit, the tax inspector must present a written order to the taxpayer, outlining the scope and period of the tax audit.

9.13 Penalties

Late filing

In addition to a nominal penalty for late filing (UAH 170 for the first and UAH 1020 for a second within one year), if the tax authorities assess tax when a taxpayer fails to file a return, penalties could reach up to 75% of the tax assessed.

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 10 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 exceeding 30 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 75% of the tax assessed, depending on number of similar breaches during the three-year period.

According to the Tax Code, the first breach of the respective tax rules within a three year period will result in penalties of 25%, for a second offense - 50% and for a third and any subsequent breach - 75%. It is unclear how this would apply for multiple offences committed at the same time.

The same penalties apply for overstatement of VAT receivables, VAT refund or tax losses (even if there is no tax understatement).

Tax evasion

The individual taxpayer (or officials) may be subject to criminal penalties if tax evasion is proven. For criminal tax evasion, fines of up to UAH 34,000 for 2011 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 with confiscation of property.

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. Under a general rule, 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. Interest is charged on the entire outstanding tax, including penalties.

For amounts additionally assessed by the tax authorities, interest is accrued from the date the tax was due using the NBU prime rate effective at this date.

Voluntary disclosures

If a taxpayer voluntarily discloses through the submission of an adjusting tax return and pays the underpaid tax before the tax authorities commence an audit there will be a 3% penalty applied to the amount of under-declared tax. If the taxpayer pays the underpaid tax previously disclosed in the return for the tax period (without filing the adjusting tax return) a 5% penalty applies. No further late payment penalty will be charged.

Penalties during appeal

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

Transition period

No penalty will be accrued for the tax understatement during the transition period: from 1 April to 30 September 2011 for corporate profits tax and from 1 January to 30 June 2011 for other taxes. However, the risk of criminal penalties should be considered.

9.14 Tax advice

Tax advice may be sought from the tax authorities, who are required to issue such clarifications. Tax advices are not legally binding and may be challenged in court. A taxpayer may use the tax advice as guidance on the methodology to be applied by the taxpayer. Arguably, in practice the tax advice does not provide solid protection against tax assessments and penalties.

10



Taxation of corporations

Investor considerations

- *The standard corporate tax rate is 23% from 1 April 2011 and will be reduced to 21% in 2012, to 19% in 2013 and to 16% in 2014. Qualifying small companies may opt to use a simplified tax system (with very favourable tax rules).*
- *From 1 April 2011, there will be no separate tax accounting. Taxable profits are to be based on financial statements (with adjustments).*
- *There is no group consolidation.*
- *Five major depreciation methods may be utilised.*
- *Losses may be carried forward indefinitely (but not by non-residents).*
- *The concept of beneficial ownership has been mentioned in the Tax Code.*
- *When companies pay dividends, they are generally required to pay advance corporate tax (ACT) at the standard CPT rate with some exceptions. This is in addition to potential withholding taxes of up to 15%.*
- *Taxable income and respective expenses are based on the date of transfer of the title on goods/ issuance of services acceptance act.*
- *The Tax Code provides for the concept of a “service permanent establishment”.*

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 23% from 1 April 2011 (gradually reduced to 16% by 2014).

Special rules apply to Ukrainian insurance companies from 2011 to 1st quarter 2012. 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. 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 for 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 June 30 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. The tax returns are based on financial statements of the company.

Permanent establishments

The domestic definition for a permanent representation essentially adopts the definition of a permanent establishment found in the OECD Model Tax Convention.

The Tax Code introduced the service permanent establishment test which provides that the provision of services by a non-resident through its employees or other

personnel in Ukraine (apart from the provision of personnel) shall constitute a permanent establishment provided such activities (within the frame of one project) last more than 6 months in any 12-month period.

A construction site in Ukraine may also give rise to a permanent establishment, provided the length of the construction activities exceeds six months.

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 and is rarely used in practice. The tax authorities prefer the notional method, which involves applying a notional margin of 30% to gross revenues earned in respect of activities in Ukraine (generally, all funds are received by 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 normal corporate income tax, but an exemption from income tax may be available for the representative offices carrying out activities of an auxiliary and preparatory nature for a 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%.

Tax holidays may be available until the end of 2015 for small businesses, but unlikely to impact international business.

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. 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, the Tax Code provides for a number of tax “holidays” and incentives. The following businesses are entitled to benefit from them:

- The publishing industry;
- Investment funds;
- The light industry;
- Ship and aircraft-building industry;
- Enterprises which produce machinery for the agricultural industry;
- Cinematography;
- Special rules may apply to the oil and gas industry (Product Sharing Agreements and Joint Investment Activity).

Enterprises selling domestically-produced energy-saving goods in Ukraine and enterprises adopting energy-saving projects (up to 50 % of profits may be exempt).

Temporarily, until 1 January 2020, a tax exemption is available for producers of electric and heat energy generated from bio-energy fuel, bio-fuel producers' profits from the sale of bio-fuels as well as for producers of bio-energy powered domestic equipment. Tax incentives are also available for producers of methane gas.

From 1 January 2011, 2, 4 and 5 star hotels are provided with 10 years of corporate income tax exemption.

Ukraine offers 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" which include 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 "activity related to production and/

or sale of goods, aimed at making profit, and carried out by the person on its own and/ or via its branches, or any other person acting for benefit of the latter person, for example, based on the rendering of services, commission or agency agreements.”

Despite the new Tax Code reconciling tax accounting with financial accounting, some differences still remain. Prior to April 2011, companies were required to prepare separate financial and tax accounts, which was very time consuming. The World Bank Doing Business 2011 estimated that a medium-sized domestic business would require 657 hours per year to comply with its corporate tax requirements. The new Tax Code is aimed at improving this situation.

Accounting for income

Income from the sale of goods is recognised at the date of transition to the buyer of the title of ownership of such goods.

Income from services is recognized at the date of issuance of the Acceptance Statement or another document issued in accordance with existing laws, which confirms the execution of works and services. Ukrainian banks should recognize taxable income from lending on the date when interests are recognised.

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, except for the VAT related to the purchase and repairs of fixed assets, which form their balance value, subject to depreciation.

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

Banks will be entitled to a tax deduction of 20% of loan-loss provisions, excluding off-balance (including interest-accrued, fees, the amount of guarantees issued on the last business day of each tax period and in respect of all securities). From 1 April 2011 to 1 January 2012, there will be a deduction limit of 30% on such provisions. Other financial institutions are entitled to a deduction of up to 10% of all loan-loss provisions.

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 (unless the taxpayer is in the business of providing such services);
- Payments in respect of goodwill and amortisation of goodwill;
- 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);
- Expenses for the goods or services purchased from an individual - single tax payer (except the single tax payer provides services in IT sphere);
- Expenses incurred in connection with the acquisition from a non-resident of consulting, marketing and advertising services at a rate in excess of 4% of the income (net of VAT and excise tax) for the year preceding the reporting year (except if provided through permanent establishments of non-residents, which are taxed accordingly). If the non-resident is the resident of an off-shore, the expenses above are not deductible.
- Expenses incurred in connection with the acquisition of engineering services from non-residents at a rate exceeding 5% of the customs value imported under a related contract (except if provided through permanent establishments, which are taxed accordingly). If the non-resident is the resident of an off-shore, or the enterprise to which the fee is charged for engineering services is not the beneficial owner of such services, the expenses above are not deductible.
- Royalties paid to non-residents have limited deductibility (refer below).

Accounting for expenses

The expenses which form the cost of goods sold, work performed and services rendered should be recognised in the reporting period when income from the sale of such goods or services rendered was recognised. Other expenses

are recognised in the reporting period in which they were actually made with some requirements stated in the law.

Depreciation and amortisation

Assets costing more than UAH 2,500 (UAH 1,000 – for 2011) and with a useful life exceeding one year are subject to depreciation. Depreciation is determined on a monthly basis. Each asset is accounted for separately. Taxpayers will be permitted to define any useful life but not less than the minimum period set by the law (see table for most relevant classes):

Group	Minimum operating period, years
Land	–
Capital costs for land improvement	15
Buildings	20
Transmitting devices	10
Machinery and equipment (including some electronic devices)	5
Vehicles	2
Tools, devices, equipment (furniture)	5
Other fixed assets	4
Temporary facilities	12
Returnable containers	5
	6

Assets may be amortised using any of the following five methods:

1. Straight-line method;
2. Residual value method;
3. Accelerated residual value method (used only for machinery and vehicles);
4. Cumulative method;
5. Production method.

But “other assets”, temporary facilities and returnable containers are only subject to the straight-line and production methods.

Expenses related to repairs of fixed assets (including leasehold) are subject to depreciation in excess of 10% of the aggregate book value of all assets as of the beginning of the tax year (the amount below the limit is deductible).

The following intangible assets may be amortised using one of the above mentioned methods over the period of an asset's lifetime (considering the minimum period set by the law for some classes):

- Rights to use natural resources;
- Rights to use property;
- Rights on intangible assets;

- Technology, know how (not less than five years);
- Copyrights (not less than two years);
- Other intangible assets.

Interest

The Tax Code provides that interest is deductible if the related debt is used to fund business activities of the taxpayer. The tax authorities may interpret this in a very restrictive manner.

Ukraine does not have thin capitalisation rules as such. Instead, there are restrictions on related parties' interest deductibility rules. The interest paid to a related party (as defined in the Tax Code) is deductible within the amount of interest income plus 50% of the company's taxable profit (excluding interest income). Any interest paid to affiliates in excess of this limit is carried forward to future tax periods.

Royalties

Royalties paid to non-residents in an amount exceeding 4% of income (net of VAT and excise tax) for the prior year are not deductible.

Furthermore, royalties paid (i) to non-residents in off-shore zones, (ii) to non-beneficial owners of the respective payment, (iii) to a person which shall not be taxed with regard to such royalty in the country of its residence or (iv) for intellectual property rights generated in Ukraine, are fully not tax deductible.

Operating Leases

Lease payments on operating leases are tax deductible for the lessee. The lessor is entitled 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 is entitled to claim depreciation charges on such property. The lessee would also deduct the interest and commission elements of the lease payments in the period in which they are accrued (and foreign exchange losses). The lessor would recognise 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 amount of the lease payments equals or exceeds the acquisition cost of the property.
- The book value of the leased property at the end of the leasing agreement does not exceed 25% of the original cost of the property at the beginning of the agreement;
- 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.

Notwithstanding the above-determined rules, the parties may 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.

Losses

Tax losses may be carried forward indefinitely (including those recognised prior to 1 April 2011) but cannot be carried back.

10.5 Special tax rules

Dividends – Advance Corporate Tax (ACT)

Companies paying dividends are generally required to pay ACT at the standard corporate tax rate. 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 does not apply to dividends that a Ukrainian entity receives from controlled companies (both residents and non-residents) and then further distributes to its shareholder.

Dividends derived by a Ukrainian entity from their affiliates, both resident and non-resident companies located in non-tax haven jurisdictions, are exempt from corporate tax.

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. Arguably, this does not apply to non-residents.

Foreign exchange

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

Bad and doubtful debts

To claim a deduction for bad or doubtful debts, a taxpayer must initiate an action for collection. A reduction of taxable income 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 creditor has a note of execution for collection executed by a notary.

At the same time, the expenses related to such goods/services income should be decreased as well.

If the taxpayer subsequently recovers an amount that has been deducted as a bad or doubtful debt, the amount recovered is included into taxable income (with respective deductible expenses).

When a creditor pursues action to recover a debt and the debtor fails to pay, the debtor is required to reduce deductible expenses at the period when the court issues the respective resolution or the execution of a note duly executed by a notary. If the debt is subsequently repaid, the debtor may claim a deduction.

There are special transitional rules in the Tax Code for doubtful debts originating prior to 1 April 2011.

Incentives for gas and oil industries (Product Sharing Agreement)

The 2011 Tax Code has a specific section on Product Sharing Agreements (PSAs). According to the Tax Code, parties to a PSA are exempt from paying taxes other than corporate profits tax, value-added tax, personal income tax, a single charge for mandatory state social security in respect of Ukrainian employees and foreign individuals employed in Ukraine, state charge and duty for receipt of state services (if any) and charges for the subsoil charge.

Joint investment activity

The joint investment activity (JIA) qualifies as an autonomous taxpayer and should be registered with the local tax authorities. One of the participants to JIA should be appointed responsible for accounting the results of JIA.

Profits of JIA accrued or distributed between the participants are subject to corporate income tax. The participant authorised for accounting is responsible for the tax payment. JIA is taxable under the general rules and does not benefit from any specific tax incentives.

Other special tax rules

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

The positive difference between output and input VAT for those agricultural enterprises which are subject to the special tax regime is subject to the standard corporate tax rate.

10.6 Related party transactions

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

- legal persons 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;
- individuals (or family members of individuals) who exercises control over a taxpayer; or
- company officials (or family members of company officials) who are authorised 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. 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. The Tax Code introduced a "safe harbour" threshold whereby no adjustments to the tax records are required provided the contractual price in the transactions with related parties and non-CIT payers is within a 20% deviation from the market (usual) price. Starting from 2013, new transfer pricing methods similar to those of the OECD will be introduced.

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

Furthermore, the taxpayers should be able to rely on the conflict of interest clause and benefit from the doubt clauses of the Tax Code.

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 the 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:

- 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 the 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 and 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 waste. The actual rate depends on the type and toxicity of each contaminant.

Charge for subsoil usage

Companies engaged in extracting mineral resource in Ukraine, regardless of the form of their ownership, are liable to a charge for use of subsoil. For gas and gas condensate the specific tax rates are applied to the volume of extracted mineral resources. The payments to be made are calculated as follows:

$$\text{volume of extracted mineral resources} * \text{specific tax rate} * \text{coefficient.}$$

Separate rates of charge for use of subsoil apply to storage of oil and gas products (the amounts are immaterial).

Charges for the use of subsoil are deductible for corporate income tax purposes.

Rental payments (oil and gas industry)

Rental payments are to be made by the companies having the appropriate licenses authorising extraction of oil, gas and gas condensate.

The tax base is calculated as the volume of extracted mineral resources multiplied by the tax rate. The adjusting coefficients apply to tax rates on rental payments for oil, gas condensate and for natural gas other than that sold to the buyer authorised by the Cabinet of Ministers. Such coefficient is calculated by the Ministry of Economy (for oil and gas condensate) and the Ministry of Finance (for natural gas) for each reporting period.

Rental payments are deductible for corporate income tax purposes. Product Sharing Agreements (PSA) covered by the Tax Code provide an exemption from these rental payments.

Local taxes and duties

The principal local taxes and duties that may affect business are:

- Duty charged for certain business activities;
- Tourism duty;
- Tax on immovable property;
- Duty for parking of a transport vehicle
- Unified tax.

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-sourced income.*
- *The standard tax rates of 15% - 17% apply to most types of incomes for both tax residents and tax non-residents. The 17% rate applies to income in excess of UAH 9,410 (approximately USD 1,200) per month.*
- *30% rate applies to income received as winnings or prizes (except for state or non-state money lotteries, sport competitions or gambling) received by both tax residents and tax non-residents.*
- *Social security issues are a major cost and administrative issue in Ukraine and are 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.
- Non-residents are liable for tax only on their Ukrainian-sourced income (including salary paid by a foreign company for work in Ukraine)

Tax residence

According to legislation, a person is a tax resident in Ukraine if he/she has a place of abode in Ukraine. If the person also has a place of abode in another country, he/she is deemed to be resident of Ukraine if he/she has a permanent place of abode (domicile) in Ukraine.

If the individual has a permanent place of abode (domicile) in Ukraine and another country, the person is deemed to be resident of Ukraine if his/her 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/she stays in Ukraine for at least 183 days during the tax year (calendar year).

If residential status cannot be determined based on the aforementioned, an individual will be deemed to be a resident of Ukraine if he/she is a citizen of Ukraine.

Notwithstanding the above, the Ukrainian tax authorities consider that all Ukrainian citizens are tax residents of Ukraine and subject to personal income tax, even if they reside abroad.

An individual may also voluntarily choose that his/her main place of abode (and therefore tax residence) is in Ukraine.

Individuals registered as Ukrainian freelancers or private entrepreneurs also qualify as Ukrainian tax residents.

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 purposes other than taxation.

Tax rates

The following tax rates are applicable for the main types of income in Ukraine:

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%
Interest: <ul style="list-style-type: none"> from Ukrainian and foreign banks until 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%

* For 2011, to be indexed further according to the minimum salary increase

11.2 Private entrepreneurs

General tax system

As a general rule, the taxable income for individuals registered as private entrepreneurs (including foreign nationals having residence permits) is calculated as the difference between gross income and the documented expenses connected to its activity, subject to the standard 15% - 17% rates.

Under the general tax regime, entrepreneurs may deduct business expenses and depreciation charges subject to the rules established by the Tax Code for corporate profits taxpayers.

Tax returns should be filed by 9 February of the year following the reporting year and should indicate all forms of income (i.e. from entrepreneurial and non-entrepreneurial activities). Advance tax is paid in four instalments throughout the year. The final tax payment is due by 19 February of the year following the reporting year.

The rate of Unified Social Contribution can be chosen by an entrepreneur from a minimum 34.7% to a maximum 38.11% of the taxable entrepreneur's income (subject to cap).

Single (unified) tax

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 utilised 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 9 to UAH 86 (approximately USD 1 to USD 11), 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, land tax in respect of their income earned from the entrepreneurial activities. In addition,

such private entrepreneurs required to pay compulsory Unified Social Contribution equal to 34.7% of the statutory minimum salary (for the 1Q 2011 - minimum contribution is USD 40 and will increase by the year end of the year to USD 45). Entrepreneurs can make extra contributions for their social security on a voluntary basis.

Income from independent professional activities

Income from independent professional activities (scientific, literary, educational, accounting, medical etc.) is subject to the standard rates of taxation (15%-17%). Individuals who provide such activity should be registered with the tax authorities. They can utilise the right to deduct expenses as entrepreneurs on the general tax system.

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 an employee.

Additional benefits granted by employers also constitute taxable income and include the following main 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 expenses or losses, except for items specifically exempt 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 market price.
- Amounts paid by an employer in favour of an employee under any voluntary insurance.

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 an essential condition for performing labour functions by an employee or envisaged by a so-called "collective agreement" (an agreement between owners and personnel).
- Limited employer's contributions for voluntary long-term life insurance or non-state pension insurance for the benefit of an employee.
- Amounts paid by employers to educational institutions for training/re-training of employees are not taxable within specific limits.

Rental income

Rental income is subject to tax at the standard 15%-17% tax rates. 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.

Non-residents may rent out their property only through a Ukrainian agent.

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 winnings from state or non-state lotteries, sport competitions and gambling) 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

Ukrainian dividends are subject to 5% tax. Dividends from foreign companies are taxed at the standard rates of 15%-17%.

Income from the sale of investment assets is determined independently from other income. The gain or loss is determined for each investment asset sold (sales proceeds less acquisition costs), and then aggregated for the year. If the aggregate amount is positive, it is subject to tax at the standard 15%-17% rates. If the aggregate amount is negative, it is carried forward and applied against investment income for subsequent years.

For taxation purposes, equity received as a gift or an inheritance is considered as bought for a price equal to the

state duty and tax is paid at the time the gift/inheritance is received.

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

Residents' revenues from the sale of real estate (including incomplete constructions) are subject to tax at either 0% or 5%, depending on the nature of the real estate, the number of years of possession by a seller and the number of real estate sales performed by the same taxpayer during a calendar year. The tax is based on the price indicated in the sale agreement, but cannot be lower than the property's value calculated by an authorised institution.

Income of non-residents is subject to tax according to the same rules at 15%-17% tax rates.

Disposal of movable property

Gross revenue from the sale of movable property is subject to tax at a 5% rate.

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

The tax is based on the price indicated in the sale agreement, but cannot be lower than 25% of a new vehicle.

Income of non-residents is subject to tax according to the same rules at 15%-17% tax rates.

Inheritance and gifts

Income received as an inheritance or gift is subject to tax at a 0% rate if received from a resident spouse, son, daughter or parent. A 5% rate applies if received from resident testators other than those mentioned. 15%-17% rates apply to inheritance and gifts received from/provided to 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).

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 or winnings from state lotteries (not exceeding 50 minimal salaries).
- Alimony received from residents.
- Shares received from capitalisation of undistributed profits, provided that allocation of shares between shareholders remains unchanged.
- Interest income from deposits placed with banks and non-banking financial institutions and from saving certificates. This exemption is available until 31 December 2014.

11.5 Deductions

Non-business

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

- a limited amount of interest on a qualified mortgage provided it is used to finance an acquiring taxpayer's "main place of residence";
- secondary professional or higher education of a taxpayer and his/her family members (spouse, parents, children) in the Ukrainian institutions. For 2011, the credited amount is limited to UAH 1,320 (approximately USD 165) per month of education;
- limited premiums for Ukrainian qualified voluntary long-term life insurance or non-state pension insurance for the benefit of a taxpayer and his/her family members (spouse, parents, children);
- donations to Ukrainian charities and not-for-profit organisations in an amount not exceeding 4% of the taxpayer's taxable income.

The total deductions may not exceed the amount of taxable income received in the form of salary (in practice, salary received from tax agents). Tax deduction not claimed in the reporting year cannot be carried forward.

Social security contributions

Taxable income is reduced by the amount of an employee's mandatory state unified social insurance contribution.

The employer's mandatory state unified social contribution is 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 to claim 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 same income in Ukraine (i.e. maximum 15%-17%). To claim a tax credit, the taxpayer requires an official confirmation of the amounts of income subject to tax abroad and the tax paid there from, issued/verified by the relevant foreign tax authority. This document should be duly legalised or stamped with apostille.

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 is generally taxed under the same rules and at the same rates as for tax residents (15%-17%), unless otherwise specifically provided by the law.

Consideration should also be given to the provisions in Ukrainian tax treaties, which often exempt income earned by individuals from short-term visits to Ukraine from Ukrainian tax.

There is also an unclear provision that was in the previous PIT Law, but was not enforced in practice. If "Ukrainian source" 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 non-residents filed tax returns and paid tax due on a self-assessment basis.

11.8 Tax compliance

Obligations of tax agents

Employers and other business entities that pay income to individuals are defined as tax agents and are responsible for withholding the tax and mandatory unified social contribution and remitting them to the state budget and the appropriate authorities.

The tax is payable before or at the time of the income payment. If income is paid in kind, the tax agent should remit the tax to the state no 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 25%-75% fines, as well as interest penalties depending on the period of delay of payment.

Tax agents must file monthly and quarterly reports on income paid to individuals and the amount of tax withheld from that income.

Tax returns for individuals

An individual is obliged to file a tax return if during the year he/she received income subject to tax at 15% - 17% rates from two or more tax agents and the total amount of such income for any month exceeds 10 minimum salaries established as of 1 January of the reporting year.

Moreover, 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.

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 voluntarily.

A resident or non-resident individual who receives taxable income from entities or sources that are not tax agents (or from more than two tax agents as indicated above) 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 30 April of the year following the reporting year. Tax due on the return must be paid by 31 July of the year following the reporting year. Payment must be made in local currency (hryvnia).

A taxpayer can officially apply for a filing extension to 31 December of the year following the reporting year, if the documents from the foreign jurisdiction are not available by the standard/general deadline for claiming a foreign tax credit.

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.

Overpaid personal income tax should be returned to the taxpayer within 60 calendar days from the date of filing the tax return. Upon the taxpayer's request, the overpayment may be offset against the taxpayer's future tax liabilities.

Penalties for non-compliance:

- Late reporting or non-reporting attracts a penalty in the amount of UAH 170 (approx USD 20).
- Underreporting of income or not filing a tax return which resulted in underpayment of tax is subject to a 25% fine.
- Late tax payment is subject to a 10%/20% penalty and late payment interest depending on the period of delay.

12



Value-added tax

Investor considerations

- *The standard rate of VAT is 20%. Starting from 1 January 2014, the VAT rate will be reduced to 17%. The export of goods and a very limited range of services are zero-rated.*
- *Most services provided to non-residents are either subject to 20% VAT or effectively considered outside the scope of VAT (i.e. exempt services). This has an impact on the recoverability of input VAT. Non-residents are unable to recover Ukrainian VAT.*
- *Refunds are available according to the law, but obtaining them 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 unless the refund is claimed in respect of the purchase/construction of fixed assets.*
- *Buyers must ensure that VAT invoices fully comply with established criteria. The tax authorities look at VAT invoices closely and disallow input tax credits, even if the defects in the invoice are relatively minor.*
- *Partial exemption on temporary import is now available.*
- *VAT returns and payments must generally be made on a monthly basis.*

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. If output VAT exceeds input VAT, the difference is paid to the tax authorities. Otherwise, it is subject to refund (if eligible) or could be carried forward to offset future liabilities.

For 2011-2013, the standard rate of VAT on domestic sales of goods and services and the importation of goods is 20%. Starting from 1 January 2014, the VAT rate will be reduced to 17%. Exported goods and auxiliary services are zero-rated. Other services provided to non-residents could be outside of VAT or subject to VAT at the standard rate depending of their nature.

12.2 Taxable activities

Unless there is an express exemption in the Tax Code, VAT applies to

- the supply of goods and services where the place of supply is in Ukraine, including when supply is made without consideration;
- the transfer of the object of a financial lease to the lessee;
- the import of goods into Ukraine;
- the export of goods out of Ukraine;
- international transportation services.

Place of supply for goods

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

- If goods are to be transported, the supply takes place where the goods are located at the moment of their dispatch.
- If the goods do not need to be transported, the supply takes place where the goods are located at the moment of their sale.
- When goods that require assembly or installation are sold, the supply occurs at the place of such assembly or installation.
- The supply of goods to sea, air or railroad vessels occurs at the place of their departure.

Place of supply for services

The general rule is that the place of supply for services is the place of the supplier's VAT registration.

In respect of certain services, there are specific rules for determining the place of supply. In particular, the place of supply of the following services could be defined as follows:

- **Place of services provision:** Transportation services and auxiliary to transportation services, valuation and expertise of movable property, repair and processing services, services in organizing chargeable exhibitions, conferences, seminars and other similar activities;
- **Place of customer's registration:** Transfer of intellectual property rights, advertising, telecommunication, radio and telecasting, forwarding services and leasing of movable property;
- **Place of immovable property location:** Services of realtors, preparing and conducting construction works and other service related to real estate.

VAT on imports and partial exemption

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 and excise duties.

The partial VAT exemption is available for goods imported temporarily for use in the production or performance of works. The partial exemption from VAT implies paying 3% of the total amount of VAT monthly. The paid amounts of tax would be included in the tax credit. Upon expiration of a three-year period, the customs authorities would extend the temporary import without payment of VAT. If the goods temporarily imported are cleared into free circulation within the initial three-year period, VAT is payable in full less the amounts already paid under the partial exemption procedure plus late payment interest (120% of the prime rate of the National Bank of Ukraine).

12.3 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 the finished goods are then exported from Ukraine).

12.4 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

- consulting, engineering, accounting, legal, audit, actuarial and other similar services of a consulting nature, services on development, supplying and testing of software, data processing and consulting on informational services, including services assisted by computer systems;
- most financial services and the transfer of certain financial instruments; however, as exemptions are defined with respect to specific transactions, the 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, 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; 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;
- the reorganisation of legal entities (i.e. merger, accession, spin-off, division and change of legal form).

12.5 Tax base

In most cases, the amount of VAT will be determined based on the transaction price for the supply of goods or services, but not lower than market price. Starting from 1 January 2013, the market price should be considered as a tax base only if it exceeds the transaction price by more than 20%.

For imported goods, VAT is based on the higher of the contract price or the customs value stated in the customs declaration increased by the costs of bringing those goods into Ukraine, excise taxes and duties payable at the time of import.

12.6 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. The pro-rata coefficient is calculated based on the volumes of sales of the previous calendar year and is applicable within the whole current calendar year. At the end of the year it should be re-calculated based on the actual taxable and non-taxable transactions of the current year. In respect of non-current assets, such recalculation should be done annually within first three years of usage.

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, but not higher than the market price. Starting from 1 January 2013, the market price should be a base for input VAT credit only if the transaction price exceeds the market price by more than 20%.

12.7 VAT compliance

Registration

An entity engaged in taxable supplies is required to register for VAT if its sales for the past 12 months exceed UAH 300,000. Such registration should be done with the tax authorities at the place where its business is located. The application for registration should be submitted by the director of the legal entity within 10 days following the month in which the registration threshold was reached.

The local tax authorities should issue a VAT registration certificate to the applicant within 10 calendar days. VAT registration takes effect from the date specified on the registration certificate.

A taxpayer engaged in business with taxable sales below this threshold may register voluntarily, provided:

- the taxable sales have already been started;
- not less than 50% of the overall sales for the previous 12 consecutive months were made to VAT-registered customers.

Such limitations of voluntary registration introduced since 1 January 2011 will have a negative impact on business during the start-up stage, when substantial investment in fixed assets and goods in stock is required.

Accounting requirements

VAT-registered persons are required to issue VAT invoices, to keep electronic registers of input and output VAT invoices and to keep separate accounts for taxable and VAT-exempt sales and purchases.

Information on VAT invoice

A VAT-registered person is required to provide a VAT invoice for all supplies (except for supplies outside the scope of VAT). 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 address of the supplier;
- The type and quantity of the goods and services provided;
- The sales price (excluding VAT), the tax rate amount of VAT and the total amount payable;
- The type of civil agreement.

Separate invoices are required for taxable and exempt transactions. Invoices for exempt transactions must include the words, "без ПДВ" (*bez PDV* - without VAT) and the reference to the appropriate article of the Tax Code.

Buyers need to pay particular attention to the information contained in VAT invoices, especially 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 the defects in the invoice are relatively minor.

Taxpayers are obliged to account all issued and received VAT invoices in the special electronic Register of input and output VAT invoices which should be submitted to the tax authorities on a monthly basis.

Suppliers should register VAT invoices with amounts of VAT in excess of UAH 10,000 in the Unified Register of tax invoices. The Unified Register will be introduced gradually throughout 2011 depending on the amount of tax:

- UAH 1,000,000 - starting from 1 January 2011;
- UAH 500,000 - starting from 1 April 2011;
- UAH 100,000 - starting from 1 July 2011;
- UAH 10,000 - starting from 1 January 2012.

If the VAT invoice is not registered with the Unified Register, the customer is not entitled to credit input VAT until it submits a claim to the tax authorities.

Date of VAT Output and VAT Input recognition

VAT Output is accounted for as follows:

- VAT on the sale of goods is generally accounted for on the date the 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 ("act of acceptance"), whichever is earlier. It is usual commercial practice for both the supplier and the customer to sign a formal document evidencing the delivery of the service.
- VAT liabilities for imported goods arise at the date of customs clearance.

VAT Input is accounted for as follows:

- Entitlement to an input tax credit for purchases arises on the date of payment to the supplier or the date, on which the goods/services are 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 with the place of supply in Ukraine are subject to the application of a VAT reverse charge. A person required to account for VAT on such a transaction would report the VAT as output tax on 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 small businesses subject to 0% CPT rate). The return must be filed within 20 calendar days following the end of the reporting month (or the next

working day if the 20th day falls on a weekend or a public holiday).

Along with the VAT return, taxpayers are obliged to submit the copy of the Register of issued and received VAT invoices in electronic form.

VAT payments must be made within 10 calendar days following the VAT return submission deadline.

Refunds

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

According to the law, if an application for a 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.

Automatic VAT refund procedure is technically available for eligible taxpayers (exporting companies). Under this procedure, the tax authorities are required to check and confirm the entitlement for VAT refund within 23 days. The State Treasury should then remit money to the applicant's bank account within three business days after receiving approval from the tax authorities.

In case of a VAT refund delay, the government will pay a daily fine of 120% of the National Bank of Ukraine interest rate.

Obtaining VAT refunds has been a major problem area for investors. As an alternative to a cash refund, legislation allows to offset such VAT refund against future VAT liabilities.

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 from which a refund is sought, except where a refund relates to input tax paid on the purchase or construction of fixed assets.
- The amount of the refund claimed exceeds the taxable sales for the last 12 calendar months, except for a refund of input tax on the purchase or construction of fixed assets.

13



Introduction to PwC

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

Drawing on the talents of more than 161,000 people in 154 countries, PwC provides 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.

In FY 2010, PwC member firms provided services for 415 of the companies in the Fortune Global 500 and 415 of the companies in the FT Global 500. In addition, PwC member firms served significantly more than half of the largest companies in each regional market during the year.

PwC 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, PwC provides the highest level of professional services to international and Ukrainian enterprises. Overseen by 21 partners and directors and employing more than 400 specialists and support staff, PwC operates in Ukraine from its offices in Kyiv, Donetsk and Lviv.

The combination of local experience and a one-firm culture enables PwC 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 PwC 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 provide 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.

PwC 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 into context and advise on the likely impact that the pace and direction of economic and financial change will have on commercial activity in Ukraine.

As a result of its long-term presence, PwC 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' strategies 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.

PwC 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 PwC 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 and 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.

PwC 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 the 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.

PwC Ukraine

Key contacts

Boris Krasnyansky

Managing Partner
boris.krasnyansky@ua.pwc.com

Urmaz Kaarlep

Partner, Assurance Services Leader
urmas.kaarlep@ua.pwc.com

Vladimir Demushkin

Partner, Assurance Services
vladimir.demushkin@ua.pwc.com

Nilesh Lad

Partner, Assurance Services
n.lad@ua.pwc.com

Bryan Disher

Partner, Assurance Services
bryan.disher@ua.pwc.com

Oleg Tymkiv

Partner, Advisory Services Leader
oleg.tymkiv@ua.pwc.com

Lev Holubec

Partner, Advisory Services
lev.holubec@ua.pwc.com

Ron Barden

Partner, Tax & Legal Services Leader
ron.j.barden@ua.pwc.com

Marc-Tell Madl

Partner, Tax & Legal Services
m.madl@ua.pwc.com

Slava Vlasov

Partner, Tax & Legal Services
slava.vlasov@ua.pwc.com

Liusia Pakhuchaya

Assurance Director
liusia.pakhuchaya@ua.pwc.com

Julia Paranich

Assurance Director
julia.paranich@ua.pwc.com

Wayne Gordon

Assurance Director
wayne.gordon@ua.pwc.com

Laura Garbenciute

Assurance Director
laura.garbenciute@ua.pwc.com

Elena Tokar

Assurance Director
elena.tokar@ua.pwc.com

Roman Vodolazkyy

Assurance Director
roman.vodolazkyy@ua.pwc.com

Taras Kovalenko

Assurance Director
taras.kovalenko@ua.pwc.com

Andrew Broadhead

Assurance Director
andrew.broadhead@ua.pwc.com

Anna Onyshchenko

Advisory Director
anna.onyshchenko@ua.pwc.com

Svetlana Bilyk

Tax Services Director
svetlana.bilyk@ua.pwc.com

Andy Kuzich

Business Development Director
andy.kuzich@ua.pwc.com

Appendix A

Hints for business visitors

Visas other entry formalities

Citizens of the USA, Canada, countries of the Commonwealth of Independent States (except Turkmenistan), countries of the European Union, 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, unless the shorter period is specifically stated in the visa. 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 global financial crisis hit the stability of the national currency and the hryvnia devalued by more than 70% against the dollar by the end of 2009. As of end of 2010, 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 2011, Ukraine will have the following public holidays:

- New Year's Day (1 January)
- Orthodox Christmas (7 January)
- International Women's Day (8 March)
- Orthodox Easter (24 April)
- Labour Days (1 & 2 May)
- Victory Day (9 May)
- Orthodox Holy Trinity (12 June)
- Constitution Day (28 June)
- Independence Day (24 August)

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 the 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 2011, the Cabinet of Ministers has already recommended to move the following working days:

- Monday 7 March to Saturday 12 March
- Monday 27 June to Saturday 25 June

However, the above recommendations are not applied to the post, treasury and banking institutions and are not compulsory for private entities.

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 Ministers	www.kmu.gov.ua/control/en
Main Department of Civil Service	www.guds.gov.ua/control/en/index
Ministry of Economic Development and Trade	www.me.gov.ua/control/en/index
Ministry of Finance	www.minfin.gov.ua/control/en/index
Ministry of Foreign Affairs	www.mfa.gov.ua/mfa/en/news/top.htm
National Academy of Sciences	www.nas.gov.ua/en/Pages/default.aspx
National Bank	www.bank.gov.ua/Engl/default.htm
State Statistics Committee	www.ukrstat.gov.ua/
State Committee for Regulatory Policy and Entrepreneurship	www.dkrp.gov.ua/control/en/index
State Property Fund	www.spfu.gov.ua/eng/index.php
State Tax Administration	www.sta.gov.ua/control/en/index
Verkhovna Rada (parliament)	portal.rada.gov.ua/control/en/index

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

European Business Association (EBA)

1A Andriyivskyy Uzviz Str.
1st floor, Kyiv 04070
Tel.: +380 44 496 0601
Fax: +380 44 496 0602
www.eba.com.ua

British-Ukrainian Chamber of Commerce

Suite 42, 34A Grushevskogo Str.
Kyiv 01021
Tel.: +380 44 410 5720
Fax.: +380 44 230 2151
www.bucc.com.ua

German Economic Club (DWK)

42-44 Shovkovychna Str.
Kyiv 01601
Tel: +380 44 498 49 96
Fax: +380 44 490 55 29
www.dwk.kiev.ua

Appendix C

Withholding taxes as at 1 March 2011

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	10	10	10	10
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 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		Products originating in CIS, %
	Reduced rate, %	Full rate, %	
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 0.74 per 1 litre
Wine base of grapes	UAH 0.01 per 1 litre
Fortified wine	UAH 2.14 per 1 litre
Wine, sparkling wine, vermouth	UAH 2.14 – UAH 3.1 per litre
Fermented fruit beverages with added alcohol	UAH 42.12 per litre of 100% alcohol
Fermented fruit beverages without added alcohol	UAH 0.42 per litre
Ethyl alcohol and other spirits, liqueurs and other spirituous beverages	UAH 42.12 per litre of 100% alcohol
Spirit distillates and other spirit beverages from grape wine	UAH 42.12 per litre of 100% alcohol
Tobacco raw materials	0
Cigars, cigarillos	UAH 149.66 per 1 netto kilogram
Cigarettes without filter	UAH 43.03 per 1000 sticks and 20% of sale turnover
Cigarettes with filter	UAH 96.21 per 1000 sticks and 25% of sale turnover
Tobacco for smoking, chewing tobacco or snuff	UAH 21.38 – 74.83 per netto kilogram
Other Tobacco	UAH 53.45 per netto kilogram
New cars	EUR 0.03 – EUR 0.05 1 per cubic centimetre
Used cars	EUR 1 – EUR 3.5 per cubic centimetre
Other vehicles	EUR 0.05 – EUR 3.25 per cubic centimetre
Car bodies	EUR 100 - EUR 400 per 1 unit
Motorcycles, motor bikes	EUR 0.20 per cubic centimetre 10 EUR per 1 unit
Petrol and diesel and gas	EUR 17 – EUR 182 per 1000 kilograms

Appendix E

Short form Chart of Accounts under Decree No. 291

Synthetic Accounts (1 st Tier Accounts)		Sub-accounts
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 (Losses)	441-443
45	Withdrawn Capital	451-453
46	Unpaid Capital	
47	Provision for Future Expenses and Payments	471-478
48	Targeted Finance	
49	Insurance Reserves	491-496
Class 5. Long-Term Liabilities		
50	Long-Term Borrowings	501-506

Synthetic Accounts (1st Tier Accounts)		Sub-accounts
Code	Name	Code
1	2	3
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		
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	

