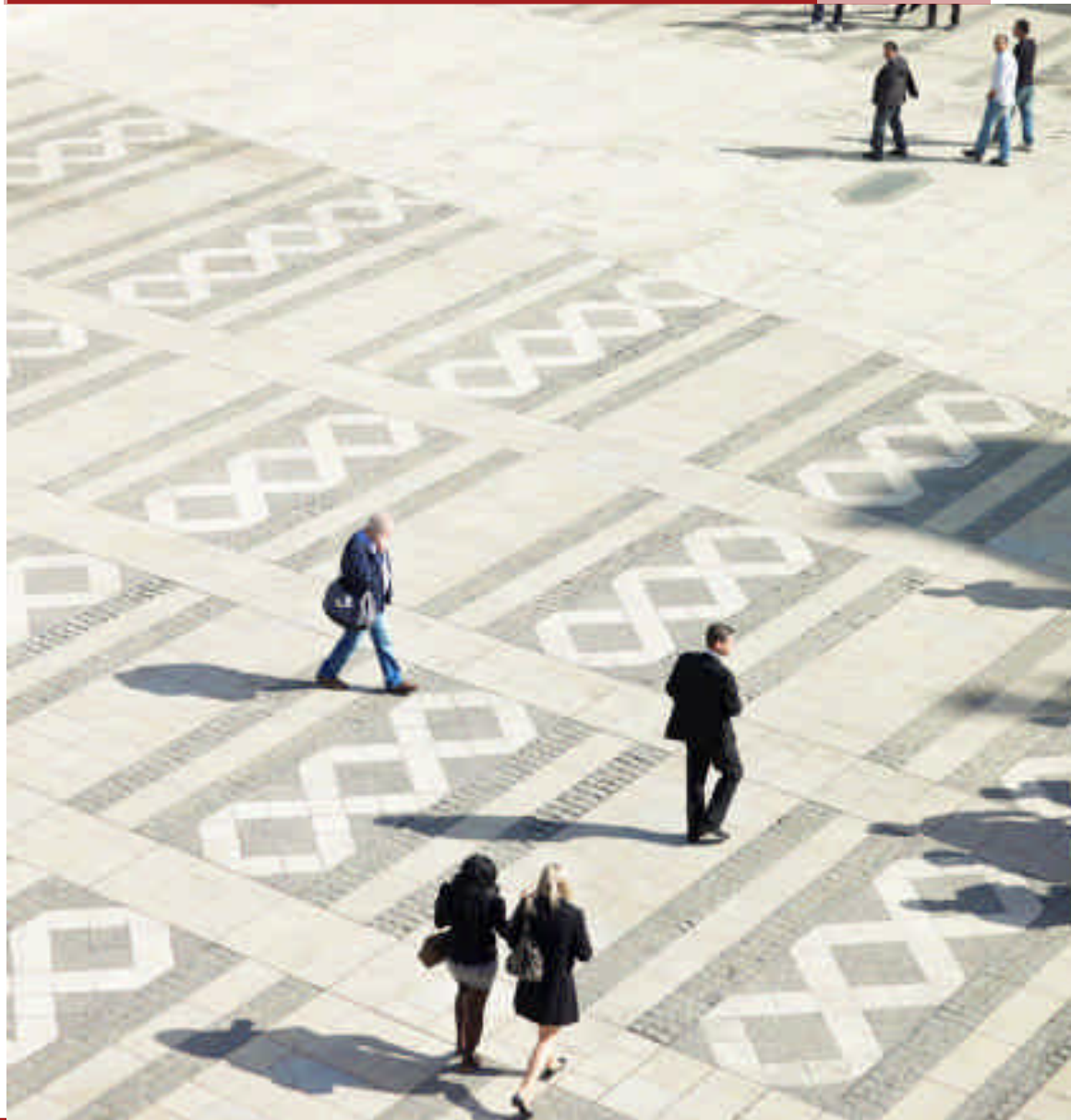


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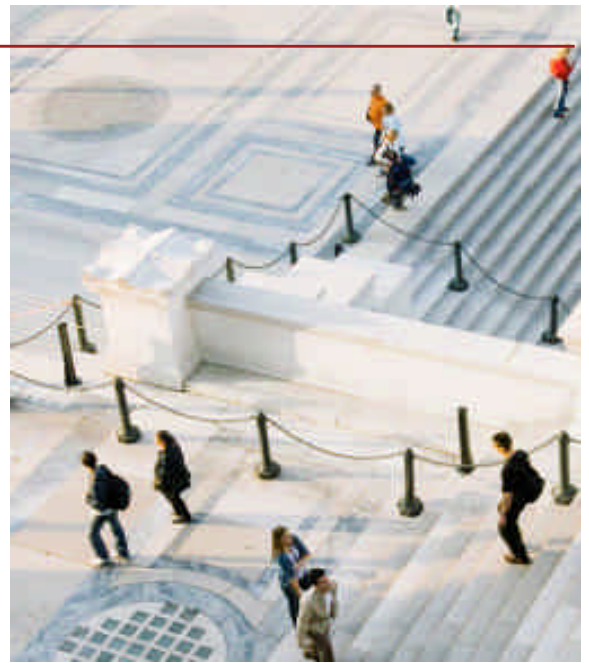
Significant Changes to the Corporate Profits Tax Rules

16 January 2015



Significant changes to the Corporate Profits Tax rules

A number of significant changes to the Corporate Profits Tax (CPT) rules became effective from 1 January 2015. We summarise them below.



I. Tax base and rate

- In 2015 standard tax rate remains 18%. Reduced rates of 0% or 3% are established for qualified insurance activities.
- Annual return for 2015 should be submitted by 1 June 2016, respective tax payment is due by 10 June 2016.
- Starting from 2015 reporting, annual tax base is Net Profits Before Tax (NPBT) as per accounting records, either Ukrainian statutory or IFRS, adjusted for “tax differences” (refer below).
- Taxpayers with the prior year annual income of equal or less than UAH 20 million (net of indirect taxes) may opt not to make the adjustments. They remain eligible for loss carry forward allowance.

II. Tax differences

- NPBT should be adjusted for the tax differences. Below we briefly outline major differences.

1) Depreciation of assets:

- Depreciation of fixed and intangible assets should be recalculated in accordance with tax rules.
- Tax rules establish the list of the expenses which are not subject to tax depreciation, minimal terms of useful life of assets, minimal value of the asset subject to amortisation.
- Reduction in the value of assets due to their impairment is disregarded for tax purposes.
- Special rules are prescribed for calculation of residual value of fixed or intangible assets at their liquidation or disposal.

2) Reserves (provisions):

- Provisions for vacation and salary payments are allowed.
- Other provisions for future costs (i.e. warranty, contingent liabilities, etc.) are disallowed.
- Provisions for doubtful debts are disallowed.

- Respective expenses, covered by these provisions (except vacation and salary payments) are deductible when incurred.
- Special rules are established for banks and financial institutions. We will cover them in a separate newsletter.

3) Thin capitalisation rules:

- These rules apply to taxpayers, whose debts to non-resident related parties exceed equity by 3.5 times (10 times for financial institutions / leasing companies).
- Deduction of interest expense for these taxpayers is limited by the amount of 50% of EBITDA.
- Non-deductible portion of interest can be carried forward indefinitely. However, each following year the residual amount of such interest should be reduced by 5%.

4) Loss carry forward allowance:

- Losses can be carried forward without limitations (including residual amount of losses unutilised from 1 January 2012).

5) Investment income:

- Dividends received from other CPT payers are not taxable for the shareholder.

6) Transfer pricing adjustments:

- Transfer pricing rules are changed significantly. We will cover these changes in a separate newsletter.

7) Limited deductibility of payments to non-residents:

- Only 70% of payments for goods or services to residents of low tax jurisdictions is tax deductible;
- Deduction of royalties paid to non-resident is limited to royalty income plus 4% of net income of the previous year;

- Royalties paid to (a) non-beneficial owners, (b) low tax jurisdictions, (c) non-residents that are exempt from tax on royalties in the country of their residence, (d) non-residents for trademarks originated from Ukraine are not tax deductible.
- The above limitations can be waived if a taxpayer confirms the market level of payments in accordance with the transfer pricing rules (even if transactions are not subject to these rules).

8) Transactions with non-for profits organizations:

- Only 70% of payments for goods or services to non-for-profits organizations (except budgetary ones) is tax deductible;
- Deductibility of costs of goods or services supplied for free to non-for profits organizations is limited by 4% of previous year's net profit;
- Special rules for taxation of non-for-profits organizations are abolished. Such organizations are exempt from CPT , if included into the governmental Register.

III. Liberalization of tax deductibility rules

- There is no longer requirement to prove connection of costs to the company's "business activities". Exception is the need to differentiate between business and non-business fixed assets.
- General requirements for the documentation of the transactions for accounting needs (i.e. contracts, acts of acceptance etc.) will apply for the substantiation of expenses for tax purposes.
- A number of restrictions for tax deductibility of costs are eliminated. This mainly relates to the following costs:
 - Special clothing,
 - Insurance,
 - Trainings,
 - Waste,
 - Hospitality,
 - Business trips,
 - Advertising,
 - Consulting, marketing and advertising fees paid to non-residents.
- The term "royalty" is changed to exclude payments for the use of a computer programs by the end user, and for purchasing electronic copies of intellectual property for final consumption.
- There are no special rules for tax accounting of repair costs. Ukrainian statutory or IFRS rules should apply.
- Tax accounting rules for the receipt (provision) of financial aid are abolished.

IV. Transitional provisions

- There is a number of transitional provisions which need to be followed in order to switch from old to the new rules. They relate to tax depreciation accumulated as of 1 January 2015, provisions, overdue debts, payables and receivables, etc.

V. Cancellation of tax incentives

- From 1 January 2015 incentives for the following taxpayers are cancelled:
 - Producers of gas (methane), bio-energy fuel, electric and heat energy generated from bio-energy fuel, domestic equipment powered with bio-energy power.
 - 'Light' industry (i.e. i.e. manufacturing of some types of consumer goods).
 - Ship and aircraft-building industry.
 - Enterprises that produce machinery for the agricultural industry.
 - The publishing industry and cinematography.
 - The investors of qualifying large investment projects (resulting in job creation) in qualifying industries.
 - Qualifying IT companies.

VI. Advance tax payments

- Taxpayers with an annual income exceeding **UAH 20 million** are required to make **monthly** advance tax payments (MATP). Exception is also made for newly established companies, non-for-profits organizations, collective investment arrangements and agricultural producers.
- MATP from January 2015 through May 2016 shall made in accordance with old rules (effective before 1 January 2015).
- MATP from March 2016 through May 2016 should not be less than 1/12 of the 2014 CPT liabilities.
- From June 2016, MATP for the period from June of the current year through May of the following year is calculated in the amount of 1/12 of the previous year's tax liabilities.
- Taxpayer having loss (no taxable profit) in first quarter of the reporting year no longer have the option of quarterly tax reporting and payment.
- Taxpayers having loss in the previous year but generating profits in first quarter of current reporting year, are required to file half-year, 9 month and annual return, if their annual income exceeding UAH 20 million.
- Rules for advance tax on payment of dividends (ATD) remain the same, except for:

- ATD applies only to the portion of dividends that exceeds profits of the respective dividend year for which CPT is already paid;
- ATD reduces the amount of MATP for the next year.

VI. Tax audits and penalties

- The tax authorities receive the right to audit taxpayer's accounting, correctness and completeness of the calculation of NPBT according to the Ukrainian statutory or IFRS rules.
- Penalties for tax violations in respect of 2015 CPT liabilities (i.e. violation of calculation of tax, tax reporting and completeness of tax payment) will not be imposed.

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