

# TAX & LEGAL AFFAIRS

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## IN THIS ISSUE

SUMMARY OF CHANGES  
IN VAT LEGISLATION

CHARGE TO PENSION  
FUND ON MOBILE  
COMMUNICATION  
SERVICES

RESERVATION  
REQUIREMENT FOR  
FOREIGN LOANS

PROCEDURE FOR  
SETTLEMENTS IN  
RESPECT OF FOREIGN  
INVESTMENTS

VISA FREE REGIME

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## Summary of changes in VAT legislation

The following key changes were introduced to VAT regime (changes are effective from 28 July 2005 unless other date is indicated):

- Toll manufacturing services and services on improvement/repair of movable goods rendered by resident taxpayers to non-resident customers are subject to zero rate VAT;
- Ship's agency and freight services are outside the scope of VAT (effective from 30 June 2005);
- Exemption from VAT applies to temporary import of goods specified in article 206 of Customs Code (goods for display at fairs; ships imported for repair; equipment and materials imported for manufacturing/repairs of ships and aircrafts for non-residents; goods that are imported for educational, scientific and cultural purposes; containers and pallets used for packaging; professional equipment that is used for mass media activities and film production);
- Exemption from VAT applies to import of aircraft under operating lease contract;

With effect from 29 July 2005 VAT regulations make it clear that Ukrainian entities that purchase services from non-resident service providers that have no registered presence in Ukraine can recover input VAT through self-billing procedure.

*(The Law of Ukraine No. 2642 dated 3 June 2005, published in "Uriyadovy Kurier" newspaper dated 30 June 2005; The Law of Ukraine No. 2771 dated 7 July 2005, published in "Uriyadovy Kurier" newspaper dated 28 July 2005; Order of the State Tax Administration of Ukraine "On Introduction of Amendments to VAT reporting" No. 213 dated 15 June 2005; Order of the State Tax Administration of Ukraine "On Introduction of Amendments to Order of State Tax Administration of Ukraine No 165 dated 30 May 1997" No. 244 dated 30 June 2005)*

## Charge to Pension fund on mobile communication services

From 1 August 2005 the rate of charge to the Pension Fund on mobile communication services increased from 6 % to 7.5 %. This charge is not included in the taxable value for VAT purposes.

*(The Law of Ukraine No. 2771 dated 7 July 2005, published in "Uriyadovy Kurier" newspaper dated 28 July 2005)*

## Reservation requirement for foreign loans

The National Bank of Ukraine (NBU) ruled that Ukrainian borrowers must deposit with the NBU 20% of short-term (i.e., up to 180 calendar days) foreign loan funds. Upon expiration of a loan term, NBU will return the money to the borrower. Reservation requirement is effective during 6 months starting from 10 September 2005.

*(Resolution of the NBU No. 291 dated 12 August 2005)*

## Procedure for settlements in respect of foreign investments

Effective from 8 September 2005 the NBU established the following procedures (Regulation No. 280) for settlements in respect of foreign investments in Ukraine:

### Inbound direct investments

Non-resident can remit to residents of Ukraine payments in hard currency in respect of direct investments (i.e., purchase of movable or immovable property as well as contributions to capital of Ukrainian resident entities) using either of the following methods:

- Transfer from non-resident's foreign bank account to current account of Ukrainian resident;
- Transfer from non-resident's investment account with a Ukrainian bank to the current account of Ukrainian resident.

Non-resident can also settle with residents in respect of direct investments in Hryvnia using local investment accounts in Hryvnia. Funds can be sourced to non-resident's investments account in Hryvnia from (i) exchange of hard currency at local investment account or (ii) profits in Hryvnia earned from non-resident's investment activities in Ukraine.

#### Inbound portfolio investments

Regulation No. 280 specifies that all settlements in respect of portfolio investments (i.e. acquisition of securities and other financial assets on stock market) should be conducted through Ukrainian licensed securities traders. The same settlements methods as for direct investments can be used.

#### Repatriation

The rules for payments in respect of repatriation of investments and profits are as follows:

- If original direct investment was remitted to the resident's current bank account, resident entity can remit funds to be repatriated to non-resident's bank account outside Ukraine;
- If original direct investment was remitted via a non-resident's local investment account in foreign currency, resident entity can remit funds to be repatriated to non-resident's local investment account.
- Non-resident investors can also opt to receive funds due to be repatriated to their local investment account in Hryvnia for further reinvestment in Ukraine or remittance outside Ukraine;

No NBU license is required for the above transactions.

Similar to inbound direct investments, Regulation No. 280 prescribes that repatriation settlements in respect of portfolio investments are conducted via Ukrainian licensed securities traders using the same as above payment rules.

In case of liquidation of local enterprise resident entity can remit liquidation funds in Hryvnia to investor's local investment account.

#### Repatriation of cash equivalent of in-kind investments

To repatriate investments, where the original investment was made as in-kind contribution to share capital (e.g. machinery), the value of relevant asset should be supported by valuation report prepared by licensed valuator. This requirement applies to in-kind investment made after 8 September 2005. For in kind investments made prior to 8 September 2005 the value of in-kind investment should be supported by import customs declaration and/or foreign investment registration certificate.

In order to execute transfer of fund subject to repatriation local bank should require a certificate confirming the payment by investor of applicable Ukrainian taxes or investor's residency certificate evidencing that the investor is a resident of country that has treaty with Ukraine for avoidance of double taxation.

Regulation No. 280 does not provide clear guidance for repatriation rules for all situations, and this may complicate contemplated transactions. For instance, it is uncertain whether it is mandatory to structure dividend payments via Ukrainian securities trader when investor acquired shares of Ukrainian company on the stock market. It also not clear whether liquidation funds (funds that are due to shareholders upon completion of local company liquidation procedure) can be remitted in foreign currency to shareholders bank accounts outside Ukraine.

We recommend readers to consider whether Regulation No. 280 will affect repatriation transactions (e.g. dividends payment) and take relevant measures to prevent surprise difficulties with repatriation remittances.

*(Resolution of the NBU No. 280 dated 10 August 2005; Letter of the NBU No. 13-124/4562-9670 of 28 September 2005)*

#### **Visa free regime**

Citizens of the USA, Canada, Japan, the European Union, Switzerland and Liechtenstein do not require a Ukrainian entry visa if the term of stay in Ukraine does not exceed 90 days.

*(President's Decrees No. 1008/2005 of 30 June 2005, No. 1134/2005 of 26 July 2005, No. 1107/2005 of 19 July 2005, No. 1131/2005 of 26 July 2005)*

