Tax Reform in Ukraine – Current Status

Ukraine Tax & Legal Alert

The draft Tax Code of Ukraine, passed at first reading by the Vekhovna Rada of Ukraine on 16 June 2010, was repealed on 7 September 2010 following public hearings. On 21 September 2010, the Cabinet of Ministers of Ukraine submitted to the Ukrainian parliament a new version of the draft Tax Code, which, with account of minor amendments introduced by the Resolution of the Verkhovna Rada, was passed at first reading on 7 October 2010. Please note that the abovementioned minor amendments to the draft Tax Code are contained in the text of the Resolution and are not incorporated into the text of the Tax Code available on the official web-site of the Ukrainian parliament.

Being not technically flawless, the document, in particular, increases tax pressure and makes it impossible to carry on certain business activities. Nonetheless, the state authorities of Ukraine are going to implement tax reform as soon as reasonable practicable in order to ensure that effective from 1 January 2011 the nation is guided by a new Tax Code which will also serve as the basis for the 2011 state budget.

Despite a number of amendments that may still be introduced by the parliamentary committees before the second hearing, please find below some major novelties proposed by the current draft Tax Code.

- The CIT rate is expected to be gradually reduced to 16% in 2014, down from 25% today (the 2011 rate is 19%), and the VAT base rate from 20% to 17% in 2014. Yet the PIT rate applicable to any monthly salary in excess of 10 minimum monthly salaries is expected to reach 17%. However, the PIT rate applicable to dividends will be cut threefold to be fixed at 5%.

- Despite the gradual decreases in the tax rates, the tax base is expected to extend significantly thus putting additional tax pressure on Ukrainian businesses. Specifically, under the current draft Tax Code, the following expenses are non-deductible for tax purposes:
  - Acquisition of goods (works, services) from individual entrepreneurs registered as single tax payers (except for IT expenses);
  - Acquisition of consulting, marketing, advertising, engineering services/works from non-residents (except where such services/works are acquired through such non-residents' permanent establishments in Ukraine);
  - Accrual of royalties in favor of any non-resident or tax exempt resident.

- Just as the previous version of the Tax Code, the current draft document aims to harmonize accounting and tax rules, and introduces new depreciation rules.

- No restrictions on tax losses carried forward are referred to in the draft Tax Code.

- The current version of the Tax Code contains a new definition of "tax residence" for individuals. A foreign national who obtained a permanent residence permit or employment permit in Ukraine or stays in Ukraine for at least 183 days within a year is deemed a tax resident of Ukraine.

- The draft Tax Code (at least formally) compels the tax authorities of Ukraine to accept the tax returns unconditionally and imposes administrative liability for the tax officials who refuse to accept the tax returns from the taxpayers.
- Unlike the previous version of the Tax Code, the current one envisages that accrual of fines and penalties is suspended for the whole period of tax litigations.
- According to the current draft Tax Code, the frequency of tax audits depends on the risk level assigned to taxpayers.
- Violations of labor legislation continue to be considered as a ground for a tax audit. The provision is rather disputable given that such violations are clearly out of the tax authorities' control.
- Based on the draft Tax Code, single tax payers' income shall not exceed UAH 300,000 per annum. Additionally, the Tax Code extends the list of business activities that are not subject to the single tax system, including foreign economic activities (except for IT services), e-commerce, etc.
- Only IT service providers retain the right to register as single tax payers if 50% of their income is received from one customer.
- Apart from local taxes and duties, the draft Tax Code introduces a real estate tax levied on both legal entities and individuals possessing residential real estate. The tax rate is up to UAH 10 per sq m, depending on the area of residential real estate and the number of persons residing in a house / apartment. The 0.5-1.5 coefficient may apply to the tax rate, depending on the location and overall condition of a real estate object.

Source: Deloitte Ukraine