



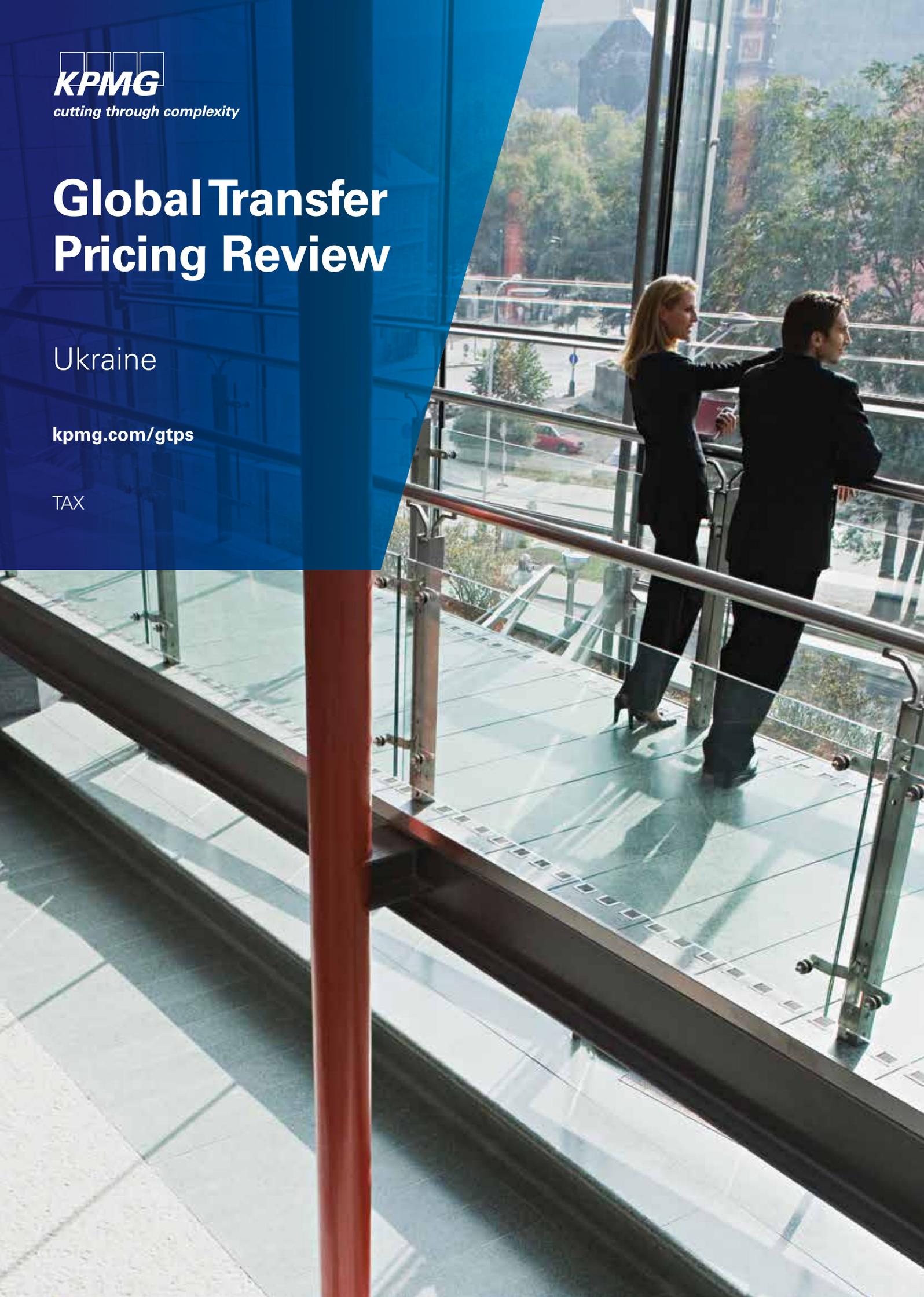
cutting through complexity

Global Transfer Pricing Review

Ukraine

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TAX



Ukraine



KPMG observation

A law in Ukraine concerning transfer pricing, that is effective as of 1 January 2015, enhances the compliance rules for taxpayers. Concerning transfer pricing, the law:

- expands the criteria for those that qualify as related parties
- revises the requirements for controlled transactions
- imposes new compliance requirements
- increases the penalty regime; and
- introduces a new mechanism for transfer pricing adjustments.

Under the new transfer pricing law, the arm's length principle is introduced, and this standard must apply to all controlled transactions.

Transactions with non-resident related parties as well as with non-related parties registered in certain jurisdictions, as listed by the Cabinet of Ministers of Ukraine, are deemed controlled if the following criteria are satisfied:

- a taxpayer's and/or the related parties' joint annual revenue exceeds 20 million Ukrainian Hryvnia (UAH) (approximately 757,000 US dollars (USD)); and
- the transaction volume exceeds the lesser of UAH1 million or three percent of the taxpayer's annual revenue.

Given the devaluation of the Ukrainian currency, it appears that the vast majority of business transactions of all types involving (non-resident) related parties will be deemed to be controlled transactions, thereby imposing an additional compliance burden on Ukrainian companies with foreign capital.

Prices in controlled transactions are assumed not to be at arm's length, unless otherwise proved by the taxpayer. Companies must also prove that the commercial and economic conditions of a controlled transaction are comparable to those for transactions between unrelated parties. The burden of proof, thus, shifts from the tax authorities to taxpayers engaged in controlled transactions.

Ukrainian companies need to review their intra-group transactions and prepare thorough transfer pricing documentation (in the Ukrainian language) so as to confirm that the arm's length principle has been applied in such transactions.

An advance pricing agreement (APA) between the taxpayer and the tax authorities can provide a level of certainty against adjustments and penalties.

Transfer pricing study snapshot

The purpose of a transfer pricing study

	Applicable	Required to be contemporaneous	Submission to tax authority required
Legal requirements	●	●	
Protection from penalties	●	●	●
Reduce risk of adjustment	●	●	●
Shifts burden of proof	●	●	●

Basic information

Tax authority name

State Fiscal Service of Ukraine (SFS).

Citation for transfer pricing rules

Tax Code of Ukraine (TC):

- Paragraph 14.1.159 (definition of related parties)
- Article 39 (arm's length principle, definition of controlled transactions, transfer pricing methods, advance pricing agreements); and
- Articles 133 — 142 (corporate profit tax).

Effective date of transfer pricing rules

1 September 2013. Enhanced transfer pricing rules came into force on 1 January 2015.

What is the relationship threshold for transfer pricing rules to apply between parties?

- Ownership of at least 20 percent of capital, directly or through third entities. If an entity is owned by another entity or physical person both directly or through third entity(ies), all direct and indirect ownership will be added to calculate effective ownership.
- Entities under common control (by ownership, voting power, common management) will be recognized as related.
- If the amount of all loans provided and/or guaranteed by one party to another exceeds a ratio of 3.5 of the recipient company's own capital, parties are recognized to be related.

- Moreover, the tax authorities can prove in court that the parties are related "based on facts and circumstances" by demonstrating that one legal entity (or physical person) had practical control over another entity's (or both entities') business decisions.

What is the statute of limitations on assessment of transfer pricing adjustments?

Seven years.

Transfer pricing disclosure overview

Are disclosures related to transfer pricing required to be submitted to the revenue authority on an annual basis (e.g. with the tax return)?

Yes. Taxpayers engaged in controlled transactions during the reporting year must file a Report on Controlled Transactions with the Ukrainian tax authorities no later than 1 May of the next calendar year.

Transfer pricing documentation must be prepared at the time when a transaction is performed, but submitted upon request of the tax authorities only.

What types of transfer pricing information must be disclosed?

The Report on Controlled Transactions must contain detailed information on the subjects of controlled transactions, including (physical) characteristics, industry-specific codes, prices applied, transfer pricing method used, arm's length price etc.

What are the consequences of failure to submit disclosures?

300 minimal wages, as set at the beginning of the reporting year (UAH 1218 or ca. USD55 for 2015) for failure to file the Report on Controlled Transactions in a timely fashion.

One percent of the volume of transactions not disclosed in the Report on Controlled Transactions (but not more than 300 minimal wages).

Three percent of the transaction volume for failure to submit transfer pricing documentation at request, but not more than 200 minimal wages for all controlled transactions.

Minimal wages = UAH1218 as of 1 January 2015 (ca. USD55 using the exchange rate for 18 August 2015). This amount is reviewed annually by the Government of Ukraine.

Transfer pricing study overview

Can documentation be filed in a language other than the local language? If yes, which ones?

No.

When a transfer pricing study is prepared, should its content follow Chapter V of the Organisation for Economic Co-operation and Development (OECD) Guidelines?

Yes, for all transactions.

Does the tax authority require an advisor/tax practitioner to have specific designation in order to prepare or submit a transfer pricing study?

No.

Transfer pricing methods

Does your country follow the transfer pricing methods outlined in Chapter II of the OECD Guidelines? If exceptions apply, please describe.

No. Transfer pricing methods described in Chapter II of the OECD Guidelines are recognized and used in Ukraine. However, a specific hierarchy of these methods applies:

- 1) CUP method
- 2) Resale Price or Cost Plus method; and
- 3) TNMM or Profit Split method.

If a taxpayer engages in a transaction with a counterparty (whether related or not) registered in a so-called "low-tax" jurisdictions, and subject(s) of the transaction are listed commodities, CUP method must be applied. In other cases, the taxpayer must submit to the tax authorities copies of contracts used in the entire supply chain of such commodities, up to the first unrelated party.

Transfer pricing audit and penalties

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? And if so, how many days?

Yes, 30 days.

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? Please explain.

Yes, 30 days.

If an adjustment is proposed by the tax authority, what dispute resolution options are available?

Following the administrative procedure, a taxpayer can apply to the tax authority

of a higher ranking. If still dissatisfied, the taxpayer can file a claim to District

Administrative Court, Administrative Court of Appeal, High Administrative Court and Supreme Court of Ukraine (for limited instances only), in that order.

If an adjustment is sustained, can penalties be assessed? If so, what rates are applied and under what conditions?

If a transfer pricing adjustment results in additional tax liabilities, the taxpayer can be subject to penalties of 25 percent and up to 75 percent of the tax underpayment if there is a recurring violation.

A taxpayer can reassess own tax liabilities in connection with transfer pricing adjustments and reflect them in the tax return. In this case, no penalties apply. Such reassessment can also be made and filed separately after the tax return is submitted. In such case, penalties will apply to the amount of underpaid tax for each day of delay.

The penalty for violations (use of non-arm's length transfer prices) committed in 2013 and 2014 is UAH1.

To what extent are transfer pricing penalties enforced?

Strictly enforced.

What defenses are available with respect to penalties?

Contemporaneous transfer pricing documentation.

What trends are being observed currently?

The Ukrainian tax authorities have already requested about 60 transfer pricing documentations from taxpayers. The first special tax audit in the field is underway. We expect numerous court disputes between the taxpayers and the tax authorities to begin in the nearest future.

Special considerations

Are secret comparables used by tax authorities?

No. The use of secret comparables is forbidden.

Is there a preference, or requirement, by the tax authorities for local comparables in a benchmarking set?

Yes. Ideally, the comparables should be local or derived from the geographically closest market. However, this only applies if the selected tested party is a resident of Ukraine. The Tax Code states that the selected tested party does not necessarily need to be a resident of Ukraine.

Do tax authorities have requirements or preferences regarding databases for comparables?

The tax authorities give preference to state statistical information and databases.

The following official sources of information will be acceptable for establishing the arm's length price:

- information sources officially approved by the Cabinet of Ministers of Ukraine
- statistical data of the state authorities and agencies
- commodity exchange prices and stock exchange quotation
- benchmark prices of specialized commercial publications, including electronic and other databases
- reports and data provided by economic departments of Ukrainian diplomatic missions abroad
- results of public auctions; and
- internal comparable prices of taxpayers.

If the official sources do not contain sufficient information for the analysis of prices in controlled transactions, other information sources, including commercial databases (RUSLANA, Amadeus, Thomson Reuters, ktMINE and Bloomberg etc.) can be used.

Does the tax authority generally focus on the interquartile range in a TNMM analysis?

No.

Does the tax authority have other preferences in benchmarking? If so, please describe.

The Ukrainian transfer pricing legislation prescribes the use of a range that is

calculated slightly differently from the interquartile range, though resembles it closely.

What level of interaction do tax authorities have with customs authorities?

High.

Are there limitations on deductibility of management fees beyond the arm's length principle?

Yes, some. Management fees are generally deductible in full.

Management fees payable to a non-resident service provider are deductible in the amount of 70 percent of such fees if paid to a non-resident registered in a "low-tax" jurisdiction.

The above limitation does not apply to transactions, for which a taxpayer has a contemporaneous transfer pricing documentation substantiating the arm's length level of prices in such transactions (even if such transaction is not deemed controlled for transfer pricing purposes).

Are management fees subject to withholding?

No.

Are there limitations on the deductibility of royalties beyond the arm's length principle?

Yes. Royalties are only deductible in the amount not exceeding 4 percent of the previous year's revenue.

Royalties are fully non-deductible if:

- paid to a non-resident registered in a "low-tax jurisdiction"
- paid to any non-resident with regard to intangible property, the ownership rights for which were initially created in Ukraine
- paid to a non-resident who is not the beneficial owner of royalties
- paid to a non-resident who is not subject to tax with regard to royalties in their jurisdiction; or
- paid to any legal entity (resident or non-resident) who is not subject to income tax or pays it at a different rate, or pays it included in the amount of other taxes.

The above limitations do not apply, and royalties are deductible in full if proved to be at arm's length (via a contemporaneous transfer pricing

documentation), even if such transaction is not deemed controlled for transfer pricing purposes.

Are royalties subject to withholding?

Yes.

Are taxpayers allowed to file tax return numbers that differ from book numbers?

Yes. True-up adjustments are allowed; true-down adjustments are not allowed.

Generally, the numbers in the tax return will differ from the book numbers due to adjustments, as prescribed by the Tax Code.

Other unique attributes?

Information available at the moment when controlled transaction is performed and/or information available from previous years can be used. Common practice is to use multiple-year data (usually, data is used from three years preceding the year when controlled transaction took place).

Tax treaty/double tax resolution

What is the extent of the double tax treaty network?

Extensive (nearly 70 effective double tax treaties).

If extensive, is the competent authority effective in obtaining double tax relief?

Yes. Historically, double tax relief has been available to a taxpayer if there was a valid tax residence certificate of its counterparty confirming that the latter is tax resident in a jurisdiction which has an effective double tax treaty with Ukraine.

Since 2011, the Tax Code introduced a beneficial ownership concept as an additional mandatory prerequisite for the application of a double tax treaty relief. The tax authorities have already started challenging certain structures (e.g. trademark sublicensing contracts) which they believe have been introduced to benefit from the double tax treaty protection.

When may a taxpayer submit an adjustment to competent authority?

If a corresponding adjustment is applicable, the taxpayer may only claim

a corresponding adjustment after its counterparty has paid the amount of tax resulting from the adjustments of their tax liabilities. Documents verifying that such payment has been made must be available in order for the taxpayer to claim a corresponding adjustment.

May a taxpayer go to competent authority before paying tax?

No (see above).

Advance pricing agreements

What APA options are available, if any?

Unilateral, bilateral, multilateral.

Is there a filing fee for APAs?

No.

Does the tax authority publish APA data either in the form of an annual report or through the disclosure of data in public forums?

No.

Are there any difficulties or limitations on the availability or effectiveness of APAs?

Yes. APAs are only available to large taxpayers.

KPMG in Ukraine

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