

Tax and Legal Newsletter for September 2012

Contents

Amendments to legislation	2
President signs package of laws aimed at encouraging investment activity in priority economy sectors	2
Changes to taxation of personal income are adopted	2
Verkhovna Rada adopts law on amendments to the Tax Code.....	3
Verkhovna Rada adopts law on improving taxation of alienation of vehicles	3
New procedure for formalizing customs declarations takes effect on 1 October 2012	3
Tax authority entitled to consider large taxpayers' complaints about the decisions of the specialized State Tax Inspections is changed	3
Clarifications from the tax and other state authorities	4
Verkhovna Rada of Ukraine requests the State Tax Service to reconsider its approach regarding rules for deducting of losses from transactions with securities and derivatives.....	4
State Tax Service issues clarification regarding tourist charge payers..	4
Changes to the VAT registration procedure are commented on	4
Clarification on tax authorities reviews of business entities is published	5
Draft amendments to tax legislation	5
Two draft laws regarding improving administration of taxes and charges are submitted to Verkhovna Rada	5
Transition to unified VAT return is planned.....	5
Court practice	5
Higher Administrative Court of Ukraine clarifies the procedure for carry-forward of losses from past periods to the 2 nd quarter 2011	5

Contacts:

Vladimir Kotenko
+380 (44) 490 3006
Vladimir.Kotenko@ua.ey.com

Jorge Intriago
+380 (44) 490 3003
Jorge.Intriago@ua.ey.com

Igor Chufarov
+380 (44) 492 8231
Igor.Chufarov@ua.ey.com

Amendments to legislation

President signs package of laws aimed at encouraging investment activity in priority economy sectors

On 28 September 2012 the President of Ukraine signed three laws aimed at encouraging investment activity. The Verkhovna Rada had adopted these laws on 6 September 2012. They are:

- Law of Ukraine "On Encouragement of Investment Activity in Priority Economy Sectors Aimed at Creation of New Jobs" No. 5205-VI;
- Law of Ukraine "On Amendments to Paragraph 4 of Section XXI 'Closing and Transaction Provisions' of the Customs Code of Ukraine Regarding Taxation of Investors That Perform Investment Projects in Priority Economy Sectors" No. 5210-VI;
- Law of Ukraine "On Amendments to Section XX 'Transaction Provisions' of the Tax Code of Ukraine Regarding Taxation of Investors That Perform Investment Projects in Priority Economy Sectors" No. 5211-VI.

Investors (agents of investment activity) who perform investment projects in priority economic sectors will theoretically be eligible for the following state support starting 1 January 2013:

- a reduced corporate profit tax (CPT) rate:
 - 0% from 1 January 2013 until 31 December 2017;
 - 8% from 1 January 2018 until 31 December 2022
 - 16% from 1 January 2023 (standard rate).
- depreciation of group 2 (capital improvements of land not associated with construction) and group 3 (buildings) of fixed assets by the accelerated declining balance method during the period of the investment projects performance;
- equipment and constitutive elements that are carried for performance of investment projects are exempt from import duty until 1 January 2018 (provided that they are not subject to excise; are manufactured not earlier than three years before the realization of the project; are not manufactured and have no equivalents in Ukraine);
- on condition of formalization of a customs cargo declaration, voluntary issuance of a tax promissory note for VAT subject to payment for import of equipment and constitutive elements that are carried for realization of investment projects and import of which is exempt from import duty (the redemption date of such a

promissory note is the 60th day after the date of its issuance to the customs authority).

These incentives will not apply automatically. The mandatory conditions for their application are the decision of the Cabinet of Ministers to include the economic sector in which the investment project is performed on the list of priority economy sectors; and the Cabinet of Ministers' approval of the particular investment project. There are also a number of auxiliary conditions, the performance of which is required for the application of tax incentives during the performance of investment projects.

The envisaged tax incentives may be used in investment projects either at newly constructed companies or at functioning companies that will undergo reconstruction or modernization, provided that a particular subdivision is separated in order to realize the investment project.

The laws establish that the amount of tax incentives granted to the investor during the realization of the project cannot exceed the volumes of investment this agent has actually made. Business agents will be obliged to keep separate tax accounting of income and expenses associated with gaining profits from the realization of investment projects. They will also be obliged to file, alongside with the corporate profit tax return, information on the free form about the amount of incentives they have received.

The laws also envisage the mandatory designated usage of funds released as a result of these corporate profit tax incentives.

Changes to taxation of personal income are adopted

Law of Ukraine "On Amendments to Section XX 'Transaction Provisions' of the Tax Code of Ukraine Regarding Taxation of Investors That Perform Investment Projects in Priority Economy Sectors" No. 5211-VI, in addition to the above-mentioned amendments related to the taxation of investment activity in priority economy sectors, also changed the taxation of personal income.

Under Paragraph 6 of Subsection 1 of Section XX "Transaction provisions" of the Tax Code the individuals' income charged before 1 January 2011 shall be taxable at the tax rates effective before 1 January 2011, notwithstanding the date of actual payment of income.

Starting 1 January 2013 the abovementioned provision will be canceled. Accordingly, personal income accrued before 1 January 2011 and paid after 1 January 2013 will be taxed at the standard PIT rate (15/17 % depending on the amount of income).

Verkhovna Rada adopts law on amendments to the Tax Code

On 10 October 2012 the Verkhovna Rada adopted the Law "On Amendments to the Tax Code of Ukraine Regarding Regulation of Certain Taxation Issues." This law combines amendments to the Tax Code that had originally been contained in five separate draft laws.

In particular, the law establishes:

- changes to the taxation of production sharing agreements, including those concluded with investor-non-residents and multilateral agreements;
- changes to taxation of insurance companies, namely - prolongation for an indefinite term of the 3% rate for taxation of profits received from insurance activity and application of 0% to income received from long-term life insurance and non-state pension insurance;
- shortening to three working days the duration of the tax authorities reviews of private-entrepreneurs without employees in relation to their closing down;
- inclusion in other direct expenses of cooperative payments to individuals-members of agricultural cooperatives who are not private entrepreneurs and who participate in the activity of the cooperative.

Verkhovna Rada adopts law on improving taxation of alienation of vehicles

On 2 October 2012 the Verkhovna Rada adopted the Law "On Amendments to the Tax Code Regarding Improvement of Taxation of Alienation of Vehicles."

The law obliges taxpayers to define income arising from the sale of automobiles, auto bikes and mopeds at prices that are not lower than the average market price of the vehicles or not lower than their assessed value (at the taxpayer's choice). It also establishes the procedure for defining the average market prices of vehicles.

Based on the text of the draft law, which is at our disposal, the charge to the Pension Fund upon alienation of used automobiles will be cancelled (today it is charged at the rate of 3 % of the vehicle's value).

On 8 October 2012 this law was sent to the President of Ukraine for signature.

New procedure for formalizing customs declarations takes effect on 1 October 2012

On 1 October 2012 there took effect the following regulations:

- The Procedure for filling in the customs declaration on the letterhead of the uniform administrative document, approved by Order of the Ministry of Finance of Ukraine No. 651 of 30 May 2012 (the Procedure for filling in the CDs);
- The Department classifiers of information regarding state customs procedures that are used in the process of formalization of customs declarations, approved by Order of the Ministry of Finance of Ukraine No. 1011 of 20 September 2012.

The Procedure for filling in the customs declarations establishes the rules for filling in the customs declaration in the uniform administrative document form (МД-2 form) and the annexes hereto (МД-3 form, МД-8 form and МД-6 form). The Procedure also envisages the algorithm for distributing copies of the customs declarations and their subsequent use.

Accordingly, starting 1 October the Instruction on the procedure for filling in the customs cargo declaration, approved by Order of the State Customs Service of Ukraine No. 306 of 9 July 1997, becomes obsolete.

Tax authority entitled to consider large taxpayers' complaints about the decisions of the specialized State Tax Inspections is changed

The State Tax Service adopted Order "On the Consideration of Complaints of Large Taxpayers" No. 776 of 27 August 2012, which changes the tax authority entitled to consider complaints about the decisions of the specialized state tax inspections (the SSTI).

The higher body of the tax service - the Central Office on Servicing Large Taxpayers - will consider large taxpayers' complaints, submitted according to the administrative procedure.

The State Tax Service will exclusively consider complaints, submitted according to the administrative procedure, about decisions of the Central Office on Servicing Large Taxpayers.

This order also obliges the State Tax Service of Ukraine in Kyiv and in the Autonomous Republic Crimea and the regional tax services, which earlier considered such complaints, to immediately send large taxpayers' complaints to the Central Office on Servicing Large Taxpayers until the appropriate changes to the procedure for submitting and

considering taxpayers' complaints are made. Also, it is prohibited to refuse the complaint based on a violation of the application term if it occurred due to forwarding of the complaint to the Central Office on Servicing Large Taxpayers.

Clarifications from the tax and other state authorities

Verkhovna Rada of Ukraine requests the State Tax Service to reconsider its approach regarding rules for deducting of losses from transactions with securities and derivatives

The Committee of the Verkhovna Rada on issues of financial and banking activity and tax and customs policy (VRU Committee) has in its letter No. 04-39/10-990 of 10 September 2012 criticized the letter of the State Tax Service of Ukraine of 9 August 2012 No. 320/0/71-12/15-1217 regarding carry-forward of losses from transactions with securities and derivatives (see our comments about this letter in the Newsletter of 13 August 2012).

The VRU Committee's letter states that the restriction on carry-forward of losses in future tax periods as per Article 150 of the Tax Code was not envisaged to apply to the definition of profits from transactions with securities. In addition, it in no way restricts the taxpayer's right to deduct the full losses from the transactions with securities in future tax periods, as these (losses for corporate profit tax purposes and losses from transactions with securities) has different economic substance and nature.

Based on the above, the VRU Committee suggested the tax authorities reconsider their approach.

State Tax Service issues clarification regarding tourist charge payers

The State Tax Service in its letter No. 1091/0/71-12/15-2217 of 20 August 2012 has confirmed that persons on business trips cannot be payers of the tourist charge.

The letter clarifies that to confirm the right to enjoy the tax incentive the tax agent must keep copies of documents confirming that he belongs to the privileged category in question. Such a document could be an order (regulation) from the company's head concerning the travel assignment and indicating the designated place, the name of the company to which the employee is sent and the term and purpose of the trip. It should also be a document confirming the business trip's relevance to the company's main activity.

Individuals who do not provide appropriate documents confirming their belonging to this privileged category must pay the tourist charge according to the general rules.

Changes to the VAT registration procedure are commented on

The State Tax Service in its letter No. 3208/0/71-12/18-3117 of 12 September 2012 has underlined that starting 1 July 2012 a person who does not perform taxable transactions and is not a VAT payer because the taxable transaction volumes are less than the established sum (UAH 300,000) and who believes that it is expedient to voluntarily register as a VAT payer can be registered in accordance with his/her application.

In such a case it is not mandatory to file the row of section 7 of the VAT registration application on the 1-ПДВ form concerning volumes of supplies of goods/services to other VAT payers. Nor is it mandatory to file sections 8 and 9 of the application concerning charter capital data (the assets' balance value).

VAT registration applications (along with supplements) are filed with the general department (registry) of the tax authority. Afterwards they are transferred to the department of informatization and registration of taxpayers.

The State Tax Service underlines that the established procedure does not envisage any preliminary consideration and/or approval of the registration applications by other the tax authority departments: the tax police working in the areas of VAT registration and issuing VAT payers certificates, for example, should not be involved.

VAT payer registration is performed based on the results of a review of the registration applications and the submitted documents by officials of the department of informatization and registration of taxpayers exclusively. If necessary, the department of taxation of legal persons (individuals) participates in the review. Letters to the taxpayers offering that they submit new applications or informing them that their VAT registration has been refused are formalized and sent by the department of informatization and registration of taxpayers.

The letter also draws attention to the new terms for VAT payer registration (re-registration) - five working days.

Clarification on tax authorities reviews of business entities is published

Letter of the State Tax Service No. 20727/7/10-0217/2986 of 31 July 2012, which was issued based on the results of a round table at the Higher Administrative Court, has been published.

The letter states:

- the investigators of the law enforcement bodies are entitled to assign the tax authorities reviews of business entities by issuing the appropriate and reasonable resolutions;
- the tax authorities are not allowed to issue tax notifications-decisions based on the results of audits performed at the law enforcement bodies' initiative until an appropriate court decision takes force;
- the taxpayer could not appeal acts of the tax authorities reviews in the court, as it is not the decision of the tax authority;
- administrative courts are not entitled to assign the tax authorities reviews;
- the grounds for renewing the term for appealing a court decision in case of the untimely receipt of the decision will be a copy of the motion for the issuance of the court decision and a copy of the court decision that is being appealed, with confirmation of the date of their actual receipt.

Draft amendments to tax legislation

Two draft laws regarding improving administration of taxes and charges are submitted to Verkhovna Rada

On 2 October 2012 two draft laws on further improving the administration of taxes and charges were submitted to the Verkhovna Rada of Ukraine. The laws were elaborated by the Cabinet of Ministers. They were registered under Nos. 11285 and 11284.

The draft laws envisage changing the Tax Code and other legal acts (such as the Law of Ukraine "On Foreign Economic Activity" and the Law of Ukraine "On Usage of Registrars of Payments Transactions in Trade, Catering and Services").

The draft laws propose:

- to change the procedure for taxing transactions with securities;
- to simplify the procedure for registering VAT payers;
- to include the register of issued and received tax invoices in VAT tax reporting;

- to change the procedure for paying the excise tax and its rates, including expanding the list of excise goods;
- to change the procedure for taxing persons who are on simplified taxation system.

The draft laws are being reviewed by the Committee of Verkhovna Rada.

Transition to unified VAT return is planned

On 21 September 2012 the Ministry of Finance published for public discussion the draft Order "On Introduction of Amendments to the Form and Procedure for Filling In and Submission of VAT Tax Reporting."

The draft order envisages a transition from the existing four VAT return forms (general, shortened, special and for a processing enterprise) to a single form for all payers of this tax.

Court practice

Higher Administrative Court of Ukraine clarifies the procedure for carry-forward of losses from past periods to the 2nd quarter 2011

The Higher Administrative Court of Ukraine (HACU) in its letter No. 2019/12/13-12 of 13 September 2012 addressed to the appeal administrative courts has clarified the procedure for implementing Paragraph 3 of Subsection 4 of Section XX "Transition Provisions" of the Tax Code of Ukraine on carry-forward of losses of past periods when defining the tax base for 2nd quarter 2011.

The HACU stated in the letter that losses of the 1st quarter 2011 are subject to deduction in the 2nd quarter 2011. Losses of the 1st quarter 2011 should include the losses that occurred in previous tax periods before 1 January 2011.

HACU does not exclude that the court could, in considering the legality of losses carry-forward, analyze underlying transactions for violations of other taxation rules that are not related to the implementation of Paragraph 3 of Subsection 4. HACU thus in fact supports the existing court practice of going beyond the subject matter of a dispute when considering carry-forward of losses.

Please see our comments about the HACU's approach in our Newsletter of 27 September 2012.

Ernst & Young

Assurance | Tax & Law | Transactions | Advisory

About Ernst & Young

Ernst & Young is a global leader in assurance, tax, transaction and advisory services. Worldwide, our 167,000 people are united by our shared values and an unwavering commitment to quality. We make a difference by helping our people, our clients and our wider communities achieve their potential.

Ernst & Young expands its services and resources in accordance with clients' needs throughout the CIS. 4000 professionals work at 19 offices in Moscow, St. Petersburg, Novosibirsk, Ekaterinburg, Kazan, Krasnodar, Togliatti, Vladivostok, Yuzhno-Sakhalinsk, Almaty, Astana, Atyrau, Baku, Kyiv, Donetsk, Tashkent, Tbilisi, Yerevan, and Minsk.

Ernst & Young established its practice in Ukraine in 1991. Ernst & Young Ukraine now employs more than 500 professionals providing a full range of services to a number of multinational corporations and Ukrainian enterprises.

For more information, please visit www.ey.com/ua.

The information contained in this publication is for general guidance only. You should neither act, nor refrain from acting, on the basis of such information. The application of laws and regulations will vary depending on particular circumstances and may also undergo frequent change. You should take appropriate professional advice relating to your particular circumstances and the current status of the laws and regulations. Ernst & Young disclaims all responsibility, including negligence, for all consequences of any person acting on, or refraining from acting in reliance on, information contained in this publication.

© 2012 Ernst & Young LLC

All Rights Reserved.

Contacts

Kyiv

+380 (44) 490 3000