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Customs treatment of royalties in Ukraine

Experts from the Chamber's Customs and Tax Committees express their opinion on the current situation regarding royalties in Ukraine, including methods of calculation, related taxation aspects, determining royalties, and customs treatment of royalties and its impact on Ukraine's business community.

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Customs law itself does not provide for defining royalties and license fees that are included into customs value. Even if definitions available in the other legal acts are used as points of reference, there remain uncertainties, since these definitions are not fully compatible. Still, uncertainty about the principal definition of royalties appears only in certain specific cases, while the available definition suffices for the bulk of general cases. The main current issues have to do with implementation procedures. The government can still do a lot to bring the regulations in line with international requirements in this area.While the principal provision for including royalties into customs value has been in place for years, the conditions under which this inclusion will actually be carried out and the relevant procedures are still far from being clear. For instance, the effective Procedure for Filling the Declaration of Customs Value, which State Customs Service of Ukraine Order # 828 initially approved on December 2, 2003 still provides that only those royalties are subject to inclusion that are payable to the seller of the imported goods under the purchase/sale contract.

The issues that remain to be resolved at the level of regulations are (1) the proper and clear definition of criteria for when royalties shall be included and (2) the procedures for how it will be done, mainly for tax purposes.

In respect to the first issue, general expectations are that it will be done in line with relevant European Community guidelines.

The second issue is really more local. Under the VAT Act and the Law "On Import Tariff," the customs authorities will assess the said taxes. As a matter of practice, importers assess it. Bringing the practice in line with what the law literally stipulates is quite important: when the customs authorities perform the assessment the importers will be responsible not for it as such, but rather only for making the proper payment. Technically, even when royalties are included into the customs value upon import, they are included with some degree of approximation (given that the final amount of royalties often depends on factors that are determined only after the sale of imported goods). In cases of post audits by customs authorities, therefore, the difference might reasonably be identified between the amounts used for customs valuations upon import and the ones finally determined upon sale. The customs authorities' current intention is to penalize the importers for this discrepancy, even when it is clear enough that they have committed no error or omission. Applying procedures consistent with what is literally in the law might resolve this issue.

There is a clear need to develop and adopt clear and comprehensive regulations as until then, the royalty issue will not be clearly regulated.