Transfer Pricing in Ukraine and Law No. 466-IX

Implementation of BEPS and other changes

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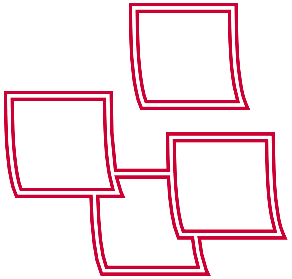
Top-3 Amendments to the TP

1. New reporting and documentation requirements for multinational groups of companies.

2. Constructive dividends.

3. Justification of business purpose (economic expediency) in the TP documentation.



TP Reporting – new requirements

New requirements are applicable to:

A resident who is a constituent entity of “the multinational group”

A multinational group is two or more enterprises the tax residence of which is in different jurisdictions.

Main feature – preparing of consolidated financial statement is required or could be required, if shares (corporate rights) are quoted.

1 Notification about participation in the multinational group of companies

Who shall submit: the taxpayers conducting controlled transactions

When: till October 1st of the subsequent fiscal year

Submit to: the State Tax Service in electronic form

2 Notification about participation in the multinational group of companies includes:

- Data on **parent company** – address, residence, codes
- Data on the member of the group **authorized to submit** Country-by-Country **report**
- Date of the group’s **fiscal year** closure
- Consolidated **revenue** for the previous fiscal year

1 Criteria for filing Country-by-Country Report by the resident

Consolidated group profit for previous year > or equivalent to **EUR 750 million**

+

A taxpayer is a parent company / authorized entity to file report OR

The country of parent company residence does not require filing the report, there is no authorized entity for filing, OR

The procedure of CbC reports exchange does not come into force yet/ there has been systematic failure to follow the procedure by the country of parent company residence.

2 The content of CbC Report

Among all jurisdictions in which there are members of multinational group or business activity has been carried out for fiscal year:

- tax jurisdiction;
- allocation of income obtained from transactions with related and unrelated parties;
- profit/revenue/earnings;
- amount of corporate tax paid and accrued;
- amount of stated capital;
- accumulated earnings;
- number of employees;
- tangible assets book value;
- nature of the main business activity.

3 Country-by-Country Report shall be filed

Where: to the State Tax Service in electronic form

When: no later than **12 months** after the last day of the fiscal year/calendar year

Purpose: assessment of TP risks during monitoring – cannot be the only ground for TP adjustment

1 Global TP documentation (Masterfile)

Who shall file: the taxpayer – constituent entity of multinational group – with consolidated group revenue > equivalent to EUR 50 million

Where: to the State Tax Service in paper/electronic form in Ukrainian

When: no later than **90 calendar days period** beginning from the day of request receipt

2 Global TP documentation shall contain the following information:

Group’s organizational structure

General description of business activity:

- important drivers of business profit;
- the supply chain and pricing for the group’s five largest products and/or service offerings by turnover plus any other products and/or services amounting to more than 5 percent of group turnover;
- a list and brief description of important service arrangements between members of the group;
- a brief written functional analysis, description of important business restructuring transactions.

3 Global TP documentation shall contain the following information:

Intangibles of the group:

- strategy for the development;
- a list and description of intangibles;
- a list of important agreements related to intangibles;
- a general description of the group’s TP policies related to intangibles;
- a general description of any important transfers of interests in intangibles.

Description of financial activities:

- a general description of how the group is financed;
- identification of members of the group, that provide a central financing function, specifying the countries of their residence;
- a general description of TP policies related to financing arrangements.

4 Global TP documentation shall contain the following information:

Consolidated financial statement of the group / in the absence of it – other consolidated reporting

A list and brief description of:

- unilateral advance pricing agreements;
- tax rulings of relevant authorities of countries (territories) which are applied among the constituent entities of multinational group and related to the allocation of income among countries (territories).

Effective date

Notification about participation in the multinational group of companies

In 2021 for 2020

Masterfile

For 2021 fiscal year

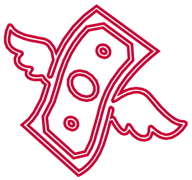
Country-by-Country Report of the multinational group

For fiscal year of 2021 (but not earlier than the year after the conclusion of agreement on automatic exchange of Country-by-Country Reports)

Liability

Document	Amount of penalty (minimum subsistence level for body-abled person (Subsistence Minimum) as for January 1, 2020)
Report on Controlled Transactions	300 Subsistence Minimums (**UAH 630 600**)
TP Documentation	3 % of the Controlled Transactions which have not been documented, but no more than 200 Subsistence Minimums (**UAH 420 400**)
Notification about Participation in Multinational Group	50 Subsistence Minimums (**UAH 105 100**)
Masterfile of the Group	300 Subsistence Minimums (**UAH 630 600**)
Country-by-Country Report	1000 Subsistence Minimums (**UAH 2 102 000**)

Constructive Dividends in the sphere of TP



Starting from January 1, 2021 the following amounts shall be deemed as dividends:

- amounts of income in favor of non-residents from disposal of securities (corporate rights) within controlled transactions exceeding the amount which complies with “arm’s length” principle;
- value of goods (works, services) purchased form non-resident within controlled transactions, exceeding the amount which complies with “arm’s length” principle;
- amount of underestimated value of goods (works, services) sold to non-resident within controlled transactions compared to the amount = “arm’s length” principle.

What does it mean?

Since 2021 reporting period the amount of TP adjustment = dividends

Amended subpara. 141.4.2 of the Tax Code of Ukraine: such dividend distribution would be subject to withholding tax (WHT) in Ukraine under a regular WHT rate of 15% (unless otherwise provided by applicable double tax treaties).

Such withholding tax shall be **paid before the deadline for submission of the report on controlled transactions** for respective reporting (fiscal) year.

Business purpose in the TP Documentation

The Law (subpara. 140.5.15 of the Tax Code of Ukraine) envisages new adjustment –

on the amount of expenses incurred by the taxpayer carrying out transactions with non-residents, **if such transactions have no business purpose**.

Burden of proof of the circumstances, envisaged by this subparagraph, is placed upon the controlling authorities.

But is this burden of proof really placed upon tax authorities in case of controlled transactions?

When purchasing **works (services), intangibles, objects of business transactions other than goods**, it is required to include the following information into TP documentation:

justification of **economic efficiency** (economic gain obtained within the controlled transaction) and presence of **business purpose** of their purchase.

If it is not possible to justify, you have the right to carry out self adjustment according to TP rules.

Transaction has no economic substance (business purpose) in the following cases:

- if the main purpose or one of the main purposes of the transaction and/or its result is nonpayment (partial payment) of tax amounts and/or reducing amount of taxable profit of the taxpayer;

- in comparable conditions the person would not be prepared to purchase works (services), intangibles, objects of business transactions other than goods, from unrelated persons.

Effective date of these regulations is May 23, 2020 –

namely, the rules of business purpose justification shall be applied already **for transactions of this year**

Other Changes to TP

Changes to the Criterion of Related Party

The increase of the threshold of ownership from 20% to **25%** is important for:

- identification of related parties;
- conducting comparative analysis based on the data on comparable entities.

An organization without status of legal entity can also be a related party.

New type of controlled transaction – full or partial transfer of functions together with assets, gains, risks and opportunities

Features:

- reducing of income and/or financial result;
- such transfer among unrelated parties would not take place without compensation, irrespectively of such operations' reflection in accounting.

Amendments to the Rules of Risk Analysis

When analyzing allocation of risk the following should be considered:

- which party controls risk creation and management, has respective power and authorities;
- which party has financial sufficiency and resources for covering risk;
- whether actual conduct of the parties corresponds to formal allocation of risks.

Refusal of the TP methods hierarchy

In the analysis the TP method which is the most reasonable/appropriate to the facts and circumstances should be applied, unless otherwise is directly stated in the law.

Deleted rule: If the TP method, which have been applied, corresponds to regulations of this article, the controlling authorities when assessing compliance of controlled transaction with “arm's length” principle will base on that method which has been applied by the taxpayer, except for the cases, when controlling authorities will substantiate that the method used by the taxpayer is not the most reasonable one.

1 The third “incarnation” of special rules for commodities

… commodities are goods for which a **quoted prices** are used by unrelated parties as a **marker (benchmark)** to set prices for uncontrolled transactions.

2

What are quoted prices?

are prices for commodities in a respective period, received at international market and includes:

- exchange quotations;
- price indices published by recognized agencies,
- statistical and government agencies.

where such indices **are used as markers (benchmarks) by unrelated parties** for pricing in transactions among these parties.

3

- **The Cabinet of Ministers of Ukraine** would adopt **the list of commodities**
- Before the beginning of fiscal year **the State Tax Service** would publish **the recommended (non-exclusive) list of sources of information** on its web portal where one can find quoted prices
- **The Ministry of Finance of Ukraine** may establish … **separate procedures** for assessment of compliance of controlled transactions' conditions regarding commodities with the "arm's length" principle

Method of assessment for TP purposes

If it is not possible to apply standard TP methods for transactions:

- with intangibles;
- on transfer of functions (new type of controlled transaction);

determination of intangibles' prices or of amount of respective compensation may be carried out under **the methodology of comparable price assessment, based on calculation of present value (discounted value) of projected future income streams**.

The TP documentation – other amendments

Now information on beneficiary in Documentation is **required**

Supply chain (value-adding)

New documents:

- material intercompany agreements;
- advance pricing agreements;
- auditor’s report on financial statements of the taxpayer and others.

1

The procedure of proportional adjustment is defined

Proportional adjustment is the right of one party of controlled transaction to make **adjustment of its tax liabilities under the results of adjustment of the other party of controlled transaction** based on the conditions that meet the “arm’s length” principle.

2 Adjustment can be carried out only if:

The controlled transaction has been conducted with related party

The treaty on the avoidance of double taxation is concluded with the residence country of other party of transaction

3

When does the right to proportional adjustment arise?

After receiving **notification** from other party of controlled transaction **on actual conducting of adjustment of tax liabilities** by this party based on the conditions which complies with the “arm’s length” principle.

4 The procedure of proportional adjustment

The taxpayer files an application regarding intention to make adjustment + the calculation of the amount of adjustment for each period, the grounds for adjustment made by the other party and the TP documentation

The tax authority reviews the application within 30 working days

5 The procedure of proportional adjustment

The tax authority makes one of the following decisions:

- notifies that adjustment is possible;
- refuses such an adjustment in whole or in part;
- assigns a check for TP rules compliance.

In case of full or partial refusal, the taxpayer has the right to apply to the State Tax Service to initiate the procedure of mutual adjustment under the Treaty on the Avoidance of Double Taxation.

Quasi-Transfer Pricing:

30% of adjustment has been extended to transactions on supply of goods (works, services) to non-residents.

Thank you for your attention!

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