



# UKRAINE IN BRIEF

INVESTOR'S GUIDE

2014





# UKRAINE: GENERAL INFORMATION

Ukraine is located in Eastern Europe and has a land area of 603,700 square kilometers, and a coastline of 2,782 kilometers. It is the second largest country in Europe after the European part of Russia.



## Population

Ukraine has a population of approximately 45.5 million (as of 2013), with a population density of about 75.4 people per square kilometer. Approximately 78 percent of the population are ethnic Ukrainians and 17 percent are ethnic Russians. The remaining 5 percent of the population include ethnic Byelorussians, Moldovans, Poles, Jews, Bulgarians, Tatars, Hungarians, Romanians, Greeks and other nationalities.

## Territorial-administrative establishment

Ukraine is subdivided into 27 regions: 24 oblasts, one autonomous republic, and two "cities with special status" - Kyiv and Sevastopol. Since Russia annexed the Autonomous Republic of Crimea and federal city of Sevastopol in February–March 2014, Ukraine de facto does not control these two subdivisions.

The administrative division in Ukraine was directly inherited from the local republican administration of the Soviet Union, the Ukrainian Soviet Socialist Republic, and has not changed majorly since the middle of the 20th century. It is somewhat complex as beside having couple of levels of a territorial subdivision, it also has its own classification for various settlements.

## Political system of Ukraine

The government of Ukraine is often associated with the Cabinet of Ministers of Ukraine. However it should be considered that Ukraine is a country under a semi-presidential system with separate legislative, executive, and judicial branches of government. And like a lot of European countries with the semi-presidential system a head of state, the President of Ukraine, has a great influence on the executive branch of the government. The highest government body of the executive branch is the Cabinet of Ministers of Ukraine not the president. The legislative branch is represented by a unicameral parliament, Verkhovna Rada, consisting of 450 People's Deputies (members of parliament).

# LEGAL SYSTEM OF UKRAINE

Ukraine follows a civil law system, under which the Constitution of Ukraine provides the framework for its legislative system and establishes general guidelines for national policy and a foundation for the development of a democratic state.



The legal system of Ukraine contains three major layers of normative acts: the Constitution of Ukraine; laws adopted by the Verkhovna Rada and international agreements of Ukraine duly ratified or acceded to by the Verkhovna Rada; and other normative acts. The Verkhovna Rada ratifies or accedes to international agreements in the form of laws of Ukraine.

Since Ukraine is a civil law country, the exercise of judicial power is based solely on the application of statutes. Court decisions do not constitute binding precedents, although the Supreme Court of Ukraine and the High Commercial Court of Ukraine decisions are summarized, to introduce uniformity to the interpretation and application of the applicable legislation, and are followed by the lower courts on a quasi-mandatory basis.

## Court System

Ukraine's court system consists of the Constitutional Court and the courts of general jurisdiction. The Constitutional Court has exclusive jurisdiction over interpretation of the Constitution and laws of Ukraine and acts as final arbiter on constitutional issues. Courts of general jurisdiction are responsible for civil, criminal, and administrative cases. they are organized by territory and specialty and include: (i) local courts; (ii) appellate courts;(iii) High specialized courts; and (iv) the Supreme Court of Ukraine.

Commercial courts of Ukraine accept jurisdiction over disputes between legal entities, including foreign legal entities, Ukrainian legal entities and individual entrepreneurs, arising out of the conclusion, modification, termination, and performance of commercial agreements (including privatization). Commercial courts are also in charge of administering bankruptcy cases, privatization and certain anti-trust disputes.

Administrative courts are entrusted to resolve disputes with public administration (i.e. with state and municipal authorities). This includes, in particular, tax litigation and appeal against unlawful acts or omissions committed by the state officials.

## Foreign courts decisions

Subject to certain exceptions, the courts of Ukraine can recognise or enforce a judgment obtained in a court established in a country other than Ukraine if such enforcement is envisaged by an international treaty to which Ukraine is a party providing for recognition and enforcement of such judgments or on the basis of the principle of reciprocity. Ukrainian law provides that unless proven otherwise, reciprocity is deemed to exist in relations between Ukraine and the country where the judgment was rendered.



## Arbitration awards

Ukraine is a member of the New York Convention of 1958 on the Recognition and Enforcement of Foreign Arbitration Awards. A foreign arbitral award should be recognized as binding and enforced upon the filing by a party of an appropriate motion with the competent Ukrainian court, unless the losing party proves the existence of any of the grounds established by the 1958 New York Convention or the applicable Ukrainian legislation for the denial of the recognition and enforcement of the foreign arbitral award.

## Property rights

The Ukrainian legislation recognizes, as a general principle, private ownership of property by Ukrainian nationals and foreigners. Under the Ukrainian Constitution, foreign citizens enjoy the same rights and freedoms and bear the same responsibilities as Ukrainian citizens, including property rights. According to the Civil Code of Ukraine, foreign citizens and legal entities are entitled to own property in Ukraine unless otherwise provided for in the international treaties of Ukraine or other Ukrainian laws. At the same time, Ukrainian law sets certain restrictions on the ability of foreigners to own property in Ukraine. For example, agricultural land cannot be owned by foreign individuals or legal entities.

The Ukrainian courts ensure protection of property rights in accordance with the applicable Ukrainian laws.

## Currency regulations

The primary purpose of currency controls in Ukraine is to impede capital outflow by Ukrainian companies and individuals. Therefore, even though repatriation of investments and dividends is not

limited, it is subject to applicable currency control regulations intending to verify valid economic reasons for sending money out of the country. Generally, payments out of Ukraine can be done fairly quickly if such regulations are observed.

Payments out of Ukraine for the services or intellectual property rights with the value exceeding EUR 100,000 or equivalent are done subject to prior obtaining of price evaluation act from competent state authority confirming economic justification of prices.

Some currency transactions (such as granting and receiving foreign currency loans from residents if the amounts of these loans exceed established limits or making investments abroad) are subject individual and general licenses issued by the National Bank of Ukraine.

General licenses are issued to commercial banks and other financial institutes of Ukraine, and to the national postal company for the whole period of currency regulations in effect. Individual licenses are issued to residents and non-residents to perform a one-time currency transaction for the period needed for the transaction to be accomplished.



# AVAILABLE CORPORATE STRUCTURES

The basic rules governing various issues concerning the establishment, maintenance and liquidation of business legal entities in Ukraine are provided in the Civil Code of Ukraine and the Commercial Code of Ukraine, both adopted on 16 January 2003, and effective from 1 January 2004. Under the Civil Code of Ukraine, legal entities, which carry out entrepreneurial activities in order to earn profits, must be established in the form of companies.



The following types of companies may be established in Ukraine:

- joint stock company ("JSC");
- limited liability company ("LLC");
- additional liability company;
- general partnerships; and
- limited partnerships.

The above forms of business entities not only differ in registration requirements, incorporation and maintenance costs, but also in types of business activities each type of business entity can carry out.

Business practice in Ukraine shows that JSCs and LLCs are the corporate forms most commonly used, and in our experience foreign investors prefer their subsidiaries or joint ventures to be organized in either of these two forms.

## Joint Stock Company

A JSC is a company in which the charter capital is divided into a specific number of shares of equal par value, similar to US corporations and UK limited companies. A JSC may be established and may be owned by a single shareholder (either a legal entity or an individual). However, JSCs cannot be established by a legal entity which itself has only one participant. At the same time Ukrainian law imposes certain restrictions on establishment and operation of a JSC, in particular: (i) JSC may not have among its shareholders only legal entities which are wholly-owned by the same person; (ii) JSC wholly-owned by a foreign company may own only non-agricultural land in Ukraine inseparable of real estate object that are owned or will be constructed by such JSC (however, this restriction apply to all corporate forms of legal presence of foreign companies in Ukraine). The personal liability of shareholders is limited to the total value of shares owned.

As of today, a minimum charter capital of a JSC is UAH 1,522,500.00 (approximately USD 117,000). JSC may be established either in form of public or private company. Public JSCs may make public and private placement of their shares whereas private JSCs may only make private placements. Shares issued by a public JSC must be listed on a stock market. Shares of a public JSC are freely tradable on

stock exchanges, with no requirement for the shareholder to obtain the prior consent of other shareholders or the company before transferring the shares. In contrast, shares of a private JSC are distributed among co-founders and cannot be publicly traded.

The corporate governance structure of a JSC consists of a (i) General Shareholders' Meeting (supreme governing body, responsible for policy decisions of JSC), (ii) Supervisory Board (exercises control over management body of JSC), (iii) Management Board or Director (management of day-to-day business activities) and (iv) Audit Committee (carrying out special audits of JSC).

### **Limited Liability Company**

LLC is the most common form of company incorporation in Ukraine. Moreover, business practice in Ukraine shows that foreign investors prefer their subsidiaries to be organized in the form of LLC. The ownership interest of investors (referred to as "Participants") in an LLC is expressed by "participatory interests" in the capital of the company, rather than by shares or stock. Participatory interests in LLC are not qualified as "securities" by Ukrainian legislation and, therefore, are not subject to registration with the State Securities and Stock Market Commission. An LLC's capital is set out in its charter, and each participant owns a percentage of the capital. The personal liability of a participant of an LLC is limited to the value of the participant's respective contribution to the company's capital. An LLC may be founded by one or more participants. The law requires, however, that an LLC cannot be 100% owned by a company which in its turn has a sole participant or shareholder.

There are no limitations regarding the minimum amount of charter capital of an LLC. Participants must pay the balance of their contributions in full within one calendar year of state registration. There are no legal restrictions on how the participatory interests of an LLC may be distributed, remaining within the discretion of its founders. The corporate governance structure of an LLC consists of (i) General Meeting of Participants (supreme governing body, responsible for policy decisions of LLC), (ii) Management Board or Director (executive body of LLC) and (iii) Audit Committee (carrying out control over executive body of LLC).

# TAX REQUIREMENTS

In Ukraine, taxes and statutory charges are levied in accordance with the Tax Code of Ukraine. Principal applicable taxes are: corporate profit tax ("CPT"), value added tax ("VAT"), personal income tax ("PIT") and withholding tax ("WHT") applied to non-residents.



## Corporate Income Tax

As of today the rate of CPT is 18%.

The following persons and entities are subject to the Corporate Profit Tax:

- Resident business entities, state, public, and other types of enterprises, institutions, and organizations that generate profits from their activity, both within and outside of the territory of Ukraine
- Foreign legal entities that derive profits from Ukrainian sources (with the exception of diplomatic establishments and other organizations enjoying immunity from taxation)
- Branches, divisions, and other separate units of the taxpayers identified above that are not legal entities and are located in a territorial community other than the territorial community of such taxpayer
- Permanent establishments of foreign entities, which such foreign entities may acquire either through their fixed place of business in Ukraine or through a Ukrainian resident entity.

Starting 1 January 2013 the CPT rate for the sale of securities and derivatives was decreased to 10 percent. Agricultural businesses may qualify for a reduced CPT rate and are subject to a favourable tax regime. Special tax treatment also applies to insurance companies, which are taxable on the rates 0% and 3%. IT sector can benefit from reduced tax rate of 5%.

In Ukraine, CPT administration is centralized, no additional corporate profits taxes are imposed at regional or local levels. CPT is calculated on a self assessed and currently adjusted basis, for each reporting period. One year is set as a standard tax reporting period for CPT purposes, however may vary depending on financial outputs of the company.

## Value Added Tax

In general terms, VAT is levied on the supply of goods and services in the customs territory of Ukraine and on the importation of goods and services to Ukraine at a standard rate of 20 per cent. Reduced rate of 7% is applicable to certain goods (pharmaceuticals, medical devices, etc).

Supplies of certain goods and services (e.g., charitable aid, financial services, etc.) are exempt from or not subjected to VAT. Export supplies of goods and related services, as well as other designated types of supply, are zero-rated.

VAT registration (i.e. registration as a VAT payer) is compulsory for all Ukrainian companies, individuals and permanent establishments of non-resident companies who qualify as VAT payers (i.e. whose volume of transactions subject to VAT exceeds UAH 300,000 (circa USD 37,500) (starting from 01.01.2015 will be UAH 1 mio) for any preceding 12 months of operation). Voluntary registration as a VAT payer is also possible under the current legislation and may be applied for by any prospective VAT payer.

The amount of VAT which a registered VAT payer incurs on local purchases of goods and services (so-called input VAT or VAT credit) can be credited against the VAT liabilities of this taxpayer in computing the final VAT payable to (or refundable from) the budget. The input VAT amount in excess of the VAT liabilities may be used to offset VAT liabilities of subsequent tax periods or refunded in cash.

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VAT on import of services is collected through a reverse-charge mechanism. This mechanism implies self-assessment and payment of the 20 per cent VAT by the Ukrainian importer in (or for) the tax period (month) when services are imported to Ukraine. The paid VAT can usually be claimed by the Ukrainian importer as a VAT credit. If the goods or services imported are used in transactions not subject to VAT, and outside the business activity of the Ukrainian importer, the “import” VAT becomes a cost to the Ukrainian importer. The reverse-charge mechanism does not apply if a non-resident service provider has a permanent establishment registered as a VAT payer in Ukraine. In this case, the representative office is in charge of assessing VAT liabilities, offsetting them against the input VAT, and transferring the positive difference to the state budget.

As of 1 January 2013 companies which implement investment projects in the priority sectors defined by the Cabinet of Ministers of Ukraine, temporarily, from 1 January 2013 to 31 December 2022 inclusive, may issue promissory notes to customs authorities, when importing to the customs territory of Ukraine equipment (hardware) and components to it, which are exempt from import duties, provided there has been registration of the requisite customs declarations. Debt recovery under such promissory notes due on the 60 day after its issuance.

## Personal Income Tax

In Ukraine, individuals are subject to PIT, regardless of whether they are tax residents or not. Individuals – tax residents of Ukraine are taxed on their worldwide income, while tax non-residents are taxed on their Ukraine-sourced income only. Ukrainian laws determine Ukraine-sourced income as income derived by an individual as a result of any business activity performed in Ukraine, which, inter alia, includes remuneration for the work performed in Ukraine, whether paid by a Ukrainian or a foreign company.

In Ukraine, both resident and non-resident individuals are taxable at the same tax rates, being 15% and 17%:

- the 15% rate applies to monthly income up to a threshold of 10 minimum wages per month (in 2013, UAH 11,470, circa USD 1,430)
- the 17% rate is applicable to monthly income in excess of a threshold of 10 minimum wages per month.

It should be emphasized that if effective international treaties of Ukraine (i.e. double taxation treaties) provide for a tax treatment other than those provided in the Ukrainian laws, the rules of international treaties should prevail over domestic legislation.

## Withholding Tax

Any Ukrainian-sourced income received and paid to a non-resident company is subject to a withholding tax ("WHT") in Ukraine at a rate of 15 per cent. Such income includes, *inter alia*, dividends, interest, royalties, capital gains, lease payments, brokerage and agency commission, *etc.* Income received as consideration for goods/services/works provided to a resident is mostly WHT exempt. Different WHT rates apply to certain types of non-resident's income (*e.g.*, freight, insurance premiums paid abroad and advertising fees).



# INVESTMENT CLIMATE IN UKRAINE

By April 1, 2013, investments into Ukraine came from 136 countries. The total volume of the direct foreign investment in the first quarter of 2013 amounted to USD 1.559 billion.

Leading countries-investors are Cyprus, Germany, the Netherlands, Russia, Austria, France and the United Kingdom.

Among the main advantages of investing in Ukraine are the following:

- 44 million consumers - one of the largest markets in Eastern Europe;
- High scientific and educational potential - powerful network of universities and research centers;
- A competitive skilled labour force - according to research company Brain Bench, Ukraine has the 4th place in the world in number of certified professionals in the field of hi-tech;
- Strategic advantages of location - Ukraine is at the crossroads of trade routes East- West and North-South;
- Widely developed transport infrastructure; railways, ports in the Black Sea and the pan-European transport corridors;



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## Recently Ukraine has seen a steady improvement of the legal business and investment environment

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Recently, Ukraine has seen a steady improvement of the legal business and investment environment by adopting a number of laws and establishing the State Agency of Ukraine for Investments and National Projects to facilitate the relationships of foreign investors with state bodies and local authorities. The advantages in legal environment include:

- Foreign investors on the territory of Ukraine enjoy national treatment for investment and other economic activity. Foreign investments in Ukraine shall not be nationalized;
- In the event of termination of investment activity, a foreign investor has the right to recoup his investment. The investment can be recovered in-kind or in the currency of investment in the amount of the actual contribution without payment of duty, along with profits from those investments in monetary form or in goods;
- The State also guarantees to foreign investors an unimpeded and prompt remittance abroad of their profits and other sums in foreign currency obtained legally as a result of foreign investments.

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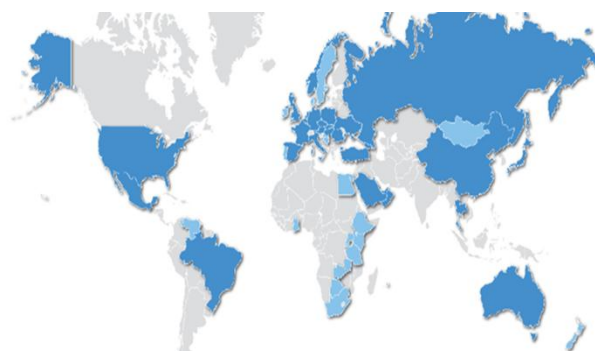
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- In order to systematize the tax legislation, the Tax Code (TC) has been adopted. It is the first codified legislative act in Ukraine regulating taxation issues. The main innovations of the TC relating to investment activities are:
- Promotion of Ukraine's transition to innovation model of development, including through the phased reduction of corporate tax rate from 25 to 18 percent (23% in 2011 , 21% in 2012 ,19% in 2013, and 18% in 2014);
- Temporary (until January, 1 2020) income tax exemption for producers of biofuels for electricity and thermal energy and profits from the extraction and use of gas (methane) of coal deposits;
- 10-years income tax exemption starting January 1, 2011 of income from selling electricity produced from renewable energy sources, profit shipbuilding and aircraft industries;
- Introduction of “automatic” refund of VAT to the “honest” payers of taxes and the single register of tax invoices and the implementation of the State's responsibility for the late refund of value added tax for such payers.



# ABOUT DLA PIPER

DLA Piper is one of the largest international law firms with 4,200 lawyers working in more than 30 countries of the world. We have equal representation on both sides of the Atlantic, our offices operate in the Americas, Europe, Asia, the Middle East and Africa. We provide full legal support to our clients wherever they choose to do business.



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## **DLA Piper was acknowledged as the Foreign Law Firm of the Year in Ukraine in 2014**

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in local and international rankings including Legal 500 and Chambers and Partners.

DLA Piper has a well-established multidisciplinary practice in Ukraine with over 30 lawyers in our Kyiv office advising on a broad range of legal issues. Our expertise in Ukraine includes the following areas of law: Corporate / M&A, Banking and finance, Real estate and construction, Tax, Intellectual Property and Technology, Competition law, Regulatory, Capital markets, Energy and natural resources, Employment law.

DLA Piper is one of the first law practices to bring an international legal presence to the region and has built a reputation for providing high-quality, client-driven legal services to leading local, international and multinational companies operating in Ukraine. Our Kyiv office is recognized

## Setting up business in Ukraine

### **Our services in this area include:**

- Setting up Ukrainian companies and representative offices of foreign companies
- Setting up and operational support of joint ventures
- Legal support in the course of privatization
- Termination and reorganization of legal entities and representative offices
- Assisting foreign investors in the tax structuring of the market entry

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### **Our expertise in Ukraine includes the following areas of law:**

Corporate / M&A, Banking and finance, Real estate and construction, Tax, Intellectual Property and Technology, Competition law, Regulatory, Capital markets, Energy and natural resources, Employment law

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## Our selected experience related to investments into Ukraine:

- Providing legal support to **a foreign strategic investor to acquire OJSC Baltsem**, Ukraine and Europe largest cement plant, including assisting in negotiations, conducting full scope due diligence, performing a privatization review, obtaining required permits from the Antimonopoly Committee of Ukraine, drafting and negotiating transaction documents and assisting in completion and post-completion matters.
- Advising **UPEC Industrial Group on its sale of 97% of shares in Factorial Bank to the Swedish financial group SEB** (value: USD 120 million), including obtaining clearances from the Antimonopoly Committee and the National Bank of Ukraine NBU. The work of our team also included structuring of the deal, drafting and negotiation of the various English law transaction documents (term sheet, share purchase agreement, escrow agreement etc), advice on pre-sale restructuring, participation in signing and closing of the transaction, etc.
- Advising **Europe Virgin Fund (EVF), a private equity fund, sponsored by Dragon Capital** in set up of a joint venture with Ucraftarma S.A. The parties invested into Lux PHARMA Participations SA, a Luxembourg-based holding company, with Ucraftarma S.A. transferring various pharmaceutical assets including its 95% stake in Sperco Ukraine LLC, one of the top 10 pharmaceutical manufacturers of Ukraine, and EVF providing capital for further development. DLA Piper provided full legal support to the transaction, including legal due diligence of Ukrainian and Spanish assets, drafting and negotiating transactional documents governed by English, Ukrainian and Spanish law, support of closing of the deal.
- Legal support to **Eni, an Italian public oil & gas company**, during the acquisition of control over Ukrainian companies holding special permits for operation and natural gas extraction on Zagoryanske and Pokrovske fields in Poltava Oblast (Ukraine), including drafting transactional documents and obtaining the consent of the Antimonopoly Committee of Ukraine for concentration.
- Full legal support to **Inditex S.A., one of the world's biggest cloth retailers (TM Zara and other)** in entering the Ukrainian market and expansion of its business presence thereon.
- Full legal support to **OBI AG, the leading German Do It Yourself (DIY) retail chain**, in entering the Ukrainian market and expansion on it.
- Advising **the selling shareholders of Concern Stirol, one of the largest producers of ammonia and mineral fertilizers in Europe** in sale of more than 90% of the shares to a Ukrainian investor; work included legal due diligence of more than 20 companies of the concern, negotiating of complex transaction documents and closing of the deal.
- Providing full legal support to **a major international oil and gas company** with regard to its acquisition of two chains of gas filling stations in Ukraine. Legal work here included preparation of all necessary acquisition transaction documents, preparation of a share purchase agreement, negotiations and execution.

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