

STARTING A JOINT VENTURE IN UKRAINE

This note includes a brief description of issues related to registration and taxation of joint ventures, employment procedures in Ukraine as of 14th May 2021. More detailed information may be provided by Ukraine's state institution "Investment Promotion Office" (SI "UkraineInvest") upon respective request.

1. Regulation on joint ventures in Ukraine

Under the Ukrainian legislation joint ventures may be legally organized via two different legal mechanisms: 1) by incorporating a respective legal entity – joint venture company (hereinafter referred to as the "JVC"); or 2) by entering into a joint activity agreement (hereinafter referred to as the "Unincorporated joint venture").

1.1. Joint venture company (JVC)

A new legal entity (so-called joint venture company or JVC) may be incorporated as any type of a legal entity. Ukrainian legislation provides for a variety of legal entity types including the equivalents of the types commonly used worldwide. Constant developments in company law approximate Ukrainian regulatory field to the European legislation providing investors with well-known and transparent instruments.

Depending on the specifics of their projects, investors usually incorporate their business in Ukraine as one of the following entity types:

1.1.1. Limited liability company

LLC is an equivalent of GmbH (Germany), private limited company (UK) or société à responsabilité limitée (France). An individual and/or an entity (or a group of them) can establish an LLC. There are no limitations with regard to a maximum number of shareholders.

To become an LLC's shareholder, it is necessary to make a contribution to the company's charter capital. These cash or other assets contributions define the participants' share in the charter capital and constitute the extent of their liability for the company's commitments.

An LLC has a convenient governance system that consists of the following governing units: a meeting of shareholders as the highest governing body, an individual or collective management and a supervisory board. The latter is optional and LLCs are entitled to decide whether to establish this governing body on their own. Shareholders can enter into a corporate agreement to establish a framework for mutual understanding with regard to exercising their rights, e.g. the right to sell or buy one's share. An LLC's charter can include provisions setting special rules for entering into high-value transactions or related-party transactions.

LLCs can engage in various business activities, enter into M&A transactions or quit the market quickly when needed. These and many other advantages gain LLCs a reputation of a very flexible entity type.

1.1.2. Joint stock company

This type of entity is an equivalent to Aktiengesellschaft (Germany) or société anonyme (France). A JSC's characteristic feature is its charter capital, which has to be composed of shares of equal par value, and may not be lower than 1250 government-determined minimum wages (some USD 217, 000 as of 2020). As well as with LLCs, a joint stock company's shareholders shall not be held liable for the company's commitments beyond the value of the shares they hold.

There are two types of JCSs: private and public. The difference comes down to the way these companies hold initial and following share sales. Private JCSs are not allowed to undertake public offerings and shall distribute the shares exclusively among the company's founders. Public JCSs may go either way, but have to list their shares on a Ukrainian stock exchange.

Ukrainian legislation sets up additional reporting requirements associated with issuance of shares obliging JCSs to work closely with the National Securities and Stock Market Commission. Joint stock companies have a more

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extended management structure and stricter internal procedures if compared to LLCs. Apart from a shareholders' meeting and management, JSC's compulsory governing units include a supervisory board.

JSC's stock can be composed of ordinary and privilege shares setting up a priority in dividends distribution and limiting participation of shareholders in voting on company's management issues.

Similar to LLCs, shareholders of joint stock companies can enter into a shareholders' agreement to decide on how they are going to exercise their rights, obliging each other to carry out or refrain from certain activities.

JSCs are obliged to follow special rules when conducting high-value transactions and related-party transactions (generally, a supervisory board's approval is required). Legislation sets up various procedures to ensure JSC shareholders' rights, e.g. in buyouts.

These and other features allow JSCs to welcome a high number of shareholders and preserve their interests effectively. JSCs are a strong instrument when it comes to raising financing at initial business stages or further during the company's operations.

1.2. Taxation of JVC

According to the Tax Code of Ukraine JVCs are taxed with the following taxes:

1.2.1. Corporate income tax (CIT)

CIT is accrued on income minus expenses from entrepreneurial activity. JVC that derive profits from Ukrainian sources and permanent establishments are subject to an 18 % CIT rate calculated as the financial results according to Ukrainian Accounting Standards (UAS) or International Financial Reporting Standards (IFRS) adjusted to certain differences.

UAS differ from IFRS on specific rules applicable to corporate transactions. Typically, legal entities are free to choose which accounting rules apply, except in some cases when IFRS must apply, including for:

- Entities of public interest, including:
 - issuers of securities listed on the stock exchange;
 - banks;
 - insurance companies;
 - private pension funds;
 - other financial institutions; and
 - big enterprises (with assets exceeding EUR20 million, annual income exceeding EUR20 million and the average number of employees exceeding 250 persons).
- Public joint stock companies.
- Entities conducting activities in extraction (mining) industries.
- Other entities specified by regulatory acts adopted by the Ukrainian Cabinet of Ministers.

Therefore, which corporate transactions will be subject to CIT will depend on the specific accounting rules (either UAS or IFRS) applicable to the particular transaction.

1.2.2. Withholding tax (WHT)

The Tax Code of Ukraine provides a 15 % WHT to be withheld by a resident entity or by the permanent establishment of a foreign entity from the amount of any Ukrainian-sourced income, unless otherwise provided by an applicable bilateral double taxation treaty.

Ukrainian source income includes:

- Interest payable under loans and other debt obligations issued by non-resident companies.
- Gains from a disposal or other transfer of ownership of shares, derivative securities or any other corporate rights.
- Royalties.

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- Gains from joint ventures' activity in Ukraine.

Income sourced in Ukraine in the form of gains from the disposal of shares or corporate rights relate only to those issued by Ukrainian companies (paragraph 14.1.54 of the Tax Code of Ukraine). Therefore, a disposal of shares or corporate rights issued by non-resident companies is not currently subject to WHT in Ukraine.

A resident entity or permanent establishment of a non-resident entity is liable to withhold tax when paying Ukrainian source income to a non-resident (paragraph 141.4.2 of the Tax Code of Ukraine).

1.2.3. Value added tax (VAT)

Sale of goods (services) within the customs territory of Ukraine, import of goods into the customs territory of Ukraine and export of goods out of the customs territory of Ukraine are subject to VAT. The basic VAT rate is 20% of the contractual value of the relevant goods (services). Non-residents may be subject to VAT through permanent establishments that are registered for VAT.

1.3. Joint venture without incorporation of JVC (Unincorporated joint venture)

A joint venture may be organized without JVC incorporation (so-called an Unincorporated joint venture) if business entities enter into a joint activity agreement, envisaging common business objectives, but act as separate legal entities.

1.4. Taxation of joint venture activity (Unincorporated joint ventures)

As there is no specific regulation on taxation of Unincorporated joint ventures in Ukraine, operations conducted via Unincorporated joint ventures have to be taxed according to the general provisions of the Tax Code of Ukraine. This means that all joint activities conducted on the territory of Ukraine are taxed with corporate income tax (CIT), value added tax (VAT), withholding tax (WHT), etc. Non-resident legal entities' income, received from its income source in Ukraine (i.e. income received from Unincorporated joint venture activity), thus, is also taxed in Ukraine (gains from Unincorporated joint ventures earned by non-residents in Ukraine are subject to at 15% WHT).

For taxation purposes, two or more entities that carry out joint activities without an incorporation of a legal entity are considered a single entity with regard to such activities (i.e. Unincorporated joint venture).

According to part 2 of article 1134 of the Civil Code of Ukraine, parties to a joint activity agreement that form an Unincorporated joint venture have to entitle one entity (party to this agreement) to be liable for conducting accounting of such Unincorporated joint venture (hereinafter referred to as the "**Authorized entity**").

Therefore, an accounting for the results of joint activities has to be carried out by the Authorized entity (taxpayer) in accordance with the terms of a joint activity agreement, separately from the accounting of economic results of such a taxpayer, which are not related to an Unincorporated joint venture.

In case of initiating an Unincorporated joint venture where 50 % of its charter capital will be owned by a foreign private company, it is considered to be reasonable to entitle a Ukrainian legal entity as an Authorized entity of a potential Unincorporated joint venture.

In this regard, a joint activity agreement has to be registered by the respective tax authorities as is stipulated by article 64.6 of the Tax Code of Ukraine. Such registration has to be carried out by the tax authorities as an additional registration of the Authorized entity to the joint activity agreement as a taxpayer - responsible for withholding and adding taxes to the budget during the execution of the contract. An Authorized entity – taxpayer is obliged to submit an application for accounting of an Unincorporated joint venture within 10 calendar days after the registration of the respective joint activity agreement.

For taxation purposes, all transaction related to functioning of an Unincorporated joint venture between its participants are considered transactions under contracts, meaning that transfers of results of the performed works and provided services to the Authorized entity (as the contribution to a Unincorporated joint venture),

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as well as their returns by such an Authorized entity after the end of joint activity under the joint activity agreement shall be deemed a supply of services according to the Tax Code of Ukraine. The same rule applies to providing goods between participants of JVC.

That means that above mentioned transactions on goods and services related to the joint venture will be subject to VAT if conducted by taxpayers in Ukraine. This applies to both incorporated (JVC) and Unincorporated joint ventures.

1.5. Taxation in aerospace industry

Provisions of subchapter 2 of chapter XX of the Tax Code of Ukraine provide for tax reliefs in aerospace industry, namely:

1.5.1. Temporary VAT exemption (till 1st January 2025) for business entities in aircraft industry

Legal entities that carry out business activities in the field of aircraft construction are temporarily (till 1st January 2025) exempt from 20 % VAT for transactions on importing into the customs territory of Ukraine goods used for aircraft construction purposes, as well as for transactions on supplying to the customs territory of Ukraine results of research and design works performed for aircraft construction purposes.

In order to apply for such VAT exemption a legal entity – resident of Ukraine shall carry out business activities in aircraft construction industry, obtain all legally required licenses and certificates of conformity and meet at least two of the requirements provided by the article 2 of the law of Ukraine “On development of aircraft construction industry”.

1.5.2. Temporary VAT exemption (till 1st January 2023) for business entities in space industry

Legal entities that carry out business activities in the field of space construction are temporarily (till 1st January 2023) exempt from 20 % VAT for transactions on importing into the customs territory of Ukraine goods used for space construction purposes, as well as for transactions on supplying to the customs territory of Ukraine results of research and design works performed for space construction purposes.

In order to apply for such VAT exemption a legal entity – resident of Ukraine shall comply with requirements provided by the law of Ukraine “On space activity”.

2. Currency control

Ukraine has made a strong move towards a liberal regulation of currency regulations in recent years, marked by the adoption of the Law of Ukraine “On Currency and Currency Transactions” in 2019. The underlying principle is that any cross-border payment, foreign currency purchase or currency exchange transaction is permissible unless expressly restricted in accordance with the law.

Non-residents enjoy the same rights in respect of foreign currency transactions as granted to Ukrainian residents.

The Ukrainian national currency, Hryvnia (UAH), is the only lawful means of payment on the territory of Ukraine and UAH is acceptable without any limitations. Foreign investments in Ukraine transactions and repatriation of dividends and other investment profits are among the transactions permitted in foreign currency. Transactions between residents and non-residents may be carried out in both UAH and foreign currency.

3. Hiring foreign workers in Ukraine

Foreign nationals legally residing in Ukraine have the same rights in terms of employment as Ukrainian citizens. In order to hire a foreign national, an employer should obtain a work permit issued by the employment center, except for the case when such a worker has a permanent residence permit in Ukraine. If the worker is to be employed in the representative office of a foreign company work permit is not required.

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Work permit is generally issued for a period of 1 year. A longer period – up to 3 years – can be granted to the founders of legal entities in Ukraine, IT specialists and highly paid professionals whose monthly salary exceeds 50 minimum salaries established for Ukrainian citizens (UAH 236 150 – approximately USD 8 760). It takes up to 7 working days to get a work permit and up to 3 working days to renew it.

Documents an employer is required to submit in order to receive a work permit include:

- Application form,
- Passport copy of a foreign worker (translated into Ukrainian and certified),
- 3.5 x 4.5 cm photo of a foreign worker,
- Copy of the draft employment agreement (contract) with a foreign worker.

The **fee** for the issuance or renewal of a work permit is (as of January, 2021):

- for permits issued for a period of 1 to 3 years - UAH 13 134 (approximately USD 470);
- for permits issued for a period of 6 months to 1 year - UAH 8756 (approximately USD 320);
- for permits issued for a period of up to 6 months - UAH 4378 (approximately USD 160).

After a work permit is obtained, a foreigner has to apply for a **long-term visa (D-type)** and on its basis for a **temporary residence permit** in order to legally reside on the territory of Ukraine. Temporary residence permit is issued for a period of 1 year with the possibility of renewal. There are some exceptions with regard to the length of the validity period. For instance, temporary residence permits for the foreigners and stateless persons who arrived in Ukraine for the purpose of employment are issued for the duration of the term indicated in the employment contracts, and the temporary residence permits for foreigners and stateless persons who are founders, participants or beneficiary owners (controllers) of legal entities registered in Ukraine are issued for a period of 2 years.

All **tax and duties**, rates, exemptions, rules as well as procedures and mechanisms for tax assessment and payments are defined in the Tax Code of Ukraine. Income with a source of origin from Ukraine which is received by a non-resident from a resident of Ukraine is subject to personal income tax at 18% rate. Additional Military Tax at 1,5% is levied on the income that is subject to personal income tax. Employers are also liable to make payroll-based Unified Mandatory State Social Insurance Contributions for insured employees to the State Pension Fund at 22% rate.

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