



**UKRAINE**

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The Ukraine is one of those countries which could become very significant for foreign investors.

The Ukrainian economy has a very high potential with a large sales market of 46 million inhabitants, a well educated population, fertile land (30 % of the black earth soils of the world) and oil, gas, and coal reserves. Apart from that, the Ukraine occupies a very strategic position between EU and Russia. Roughly 80 % of all gas pipelines in Europe pass through the territory of the Ukraine. In addition, the Ukraine is an important transit country between Europe and Eurasia.

The Ukraine aspires to EU membership in the near future. A decision here will depend on the signing of the association agreement.

### Legal forms of business

According to Ukrainian law business partnerships and joint stock companies are possible as conceivable legal forms.

#### Business partnerships:

##### **Full company (comparable with the German OHG)**

In the full company the shareholders are liable with their personal assets for the liabilities of the company. The company has, however, in contrast to a German OHG, its own legal personality.

##### **Company with additional liability**

In this company form the shareholders are liable for the liabilities of the company not only to the extent of their contribution according to the articles of association, but also additionally with their own private assets corresponding to the amount of their shareholding. The foundation documents define the maximum liability amounts.

##### **Limited partnership**

The limited partnership is similar to the German limited partnership. It is a company where the general partners assume liability for the obligations of the company with their full assets and the limited partners only to the extent of their capital contribution. They are not involved in the company management.

The business partnership is not chosen very often as the company form in the Ukraine. It hardly offers the shareholders tax advantages, but is associated with high risks for personal liability. For these reasons joint stock companies are the most common legal forms in the Ukraine.

## Joint stock companies

### The company with limited liability

This is a "TOV" company in the Ukraine. The company is comparable to a German GmbH. The shareholders only assume liability for the obligations of the company to the amount of the value of their contributions. The company can be founded by natural persons or legal entities. A sole trader TOV is also possible in the Ukraine. Here there is, however, a restriction to take into consideration. The law prohibits that the founder of a sole trader TOV can also be a sole trader TOV.

In the Ukraine, the number of shareholders of a TOV company is defined by law. The number must not exceed one hundred persons. If the number of shareholders of a TOV company reaches one hundred, within one year the company must be converted into a joint stock company.

There are no legal regulations in the Ukraine which define the minimum amount of share capital. The share capital can also be increased at any time. Such changes are subject to registration with the state register. The share capital must be paid in within one year after registration.

### Joint stock company (in the Ukraine called ZAT or VAT)

Differentiation is made in the Ukraine between two forms of joint stock companies, the private and the public joint stock company. In the private joint stock company the number of shareholders must not exceed one hundred persons. The shares of this type of company can only be offered privately. The public joint stock company may have an unlimited number of shareholders. The share capital here is divided between a certain number of shares which must have the same nominal value. The law stipulates a minimum amount of share capital. The share capital must not amount to less than a factor of 1250 of the minimum wage in the Ukraine. The minimum wage in the Ukraine currently amounts to 1147 Hryvnia. The share capital must therefore be a minimum of 1,433,750 Hryvnia. The shareholders of a public joint stock company assume liability for the obligations of the company up to half of the shares they hold.

## Forms of activity for foreign investors

Foreign legal entities and natural persons can engage in economic activity in the Ukraine to an unlimited extent. Foreign investors can found new companies according to Ukrainian law or acquire shares in an existing Ukrainian company. In addition, it is also possible to open a representation or branch office in the Ukraine of a foreign company. In the Ukraine, domestic and foreign investors are free to act to exercise the business activity. A number of types of activity, for example, which are classified as particularly dangerous, require the issue of a licence which is obtainable from the respective ministry or other administrative bodies. The types of activity which require a licence are defined by Ukrainian law.

## Labour law

Ukrainian labour law is relatively bureaucratic. Each foreign citizen who would like to take up an employment relationship in the Ukraine with a Ukrainian employer needs a work permit. On the basis of a work permit, a business visa is issued and after entering the country a residence permit is issued. The procedure leading to the issue of a work permit can be very lengthy. For example, a check is made of whether the same position cannot be taken up by a Ukrainian employee. In the Ukraine the working week amounts to 40 hours. The employee has by law a minimum of 24 days holiday per year.

## Real estate and acquisition of property

The land reform is one of the most important reforms carried out in recent years in the Ukraine. The reform abolished the collective and state forms of ownership. The areas were divided into so-called lots (Paj). A lot is only a right to receive a piece of land with the equivalent area. The conversion of lots into right of ownership started in 2008 and up to the present time the greater part of the lots has been transformed into property.

In 2000 a moratorium took effect in the Ukraine which will only be lifted with the passing of two important laws concerning the "Property market" and "Land register". The law concerning "Land register" was signed by two presidents and on July 7, 2011 was adopted by the Ukrainian parliament. The law determines the introduction of the nationwide land register. The draft law for "Property market" has not yet been adopted.

The acquisition of agricultural land is strictly prohibited in the Ukraine for foreigners. Foreign citizens may acquire residential property and building plots which are not classified as agricultural land.

From the draft law for the “Property market” it is clear that the acquisition of agricultural areas by foreign persons will continue to be prohibited. An open agricultural property market is not planned at the current time. Foreign investors will continue to have the only option of leasing land for an investment. Of the 41.6 million hectares of agricultural land in the Ukraine, approx. 17.4 million hectares are leased out.

## Foreign exchange law

In the Ukraine, the principle of freedom to carry out foreign currency operations is applicable for example to carry out transfers, purchasing of securities, purchasing of hard currency, etc.). This principle was restricted for a number of foreign currency operations. The restriction depends on whether the affected person is considered to be a resident or non-resident. Residents are natural persons who have their residence in the Ukraine. Legal entities are considered to be residents if they have their domicile in the Ukraine and were founded according to Ukrainian law. Non-residents are persons who are only temporarily staying in the Ukraine or who have their residence abroad. Legal entities are non-residents if they were founded and operate according to foreign law. According to the Ukrainian foreign exchange law foreign exchange transactions between residents and non-residents may only be carried out by banks which have been issued with the licence by the national bank of the Ukraine which permits the execution of such transactions.

The only means of payment in the Ukraine is the Hryvnia. In certain transactions between certain persons the payment can be made in a foreign currency. It should be observed that here an authorisation from the national bank of the Ukraine is often required.

Legal entities which are residents or non-residents can purchase or sell foreign currency for international transactions, but can only do this with the institutions which have licences issued by the national bank of the Ukraine. Foreign currency which has been purchased and which is not used for the obligations of the foreign partner within ten days have to be converted back within five days.

Natural persons who are residents or non-residents can also purchase or sell foreign currency with the institutions which have the licences issued from the national bank, whereby a person per day can only convert a maximum of 150,000 Hryvnia.

## Tax law

Ukrainian law is frequently subject to changes. On January 1, 2013 in the Ukraine a wealth tax on residential property was introduced. The taxation is relevant for flats, residential houses and other residential property. The tax applies to natural persons and legal entities including non-residents who own residential real estate. There are plans next year to expand the wealth tax to include all types of real estate. The amount of the tax depends on the area of the residential property. For the taxation of natural persons the law foresees exemptions. In the Ukraine, the tax rate for the taxation of profits of legal entities currently amounts to 19 %. A sales tax rate of 20 % currently applies for sale transactions in the Ukraine. Special product groups are subject to various tax rates and exemptions. There were plans to reduce the tax on profits to 16 % and sales tax down to 17 %. The draft budget for 2014, however, does not include any such tax reductions. The changes will possibly only be implemented in 2015.

# Practical examples

## Auditing

### Background facts:

A German company in the Ukraine operates in the field of waste disposal and for cost reasons has decided to take the cheapest local auditor to audit the annual financial statement because one believes that everything is under control in the Ukrainian subsidiary and in addition that the company has a very competent person in charge of financial accounting.

In order to ensure that he himself does not make a loss, the local auditor undertakes no audit actions whatsoever and confirms the financial statements without reading them and gives them his unqualified audit opinion.

This carries on for some time without incident until the company management discovers irregularities in the financial accounting. In addition, the social security authorities announce an audit.

### What can be done now?

The audit by the social security authorities cannot be avoided. However, through a co operative approach it is possible to establish a good basis for possible negotiations concerning the social security contributions which have not been paid. In addition, a detailed internal audit has to be made in order to completely examine the financial accounting of the last years for errors and irregularities.

### What should one have done differently from the beginning?

As a foreign investor it should always be clear that foreign companies have to take into account an increased requirement for controls and the associated costs. If the German company management is not aware of this, it will make decisions on cost cutting measures which can lead to considerable problems. For example, the competence of the financial accounting should have been checked much earlier by an independent and reliable auditor. In this respect Rödl & Partner is able to provide an auditor who has international expertise and experience, who through the auditing of the German parent company may already know your company and who is therefore able to carry out a cross-border audit. Rödl & Partner is also your contact person for the implementation, execution and/or control of your financial accounting on which you can depend.

## Law / Fraud

### Background facts:

A German company trading in building materials also has a large branch office in the Ukraine which has office space and a warehouse with goods to the value of 5 million euros. A Ukrainian managing director is taken on to manage the branch office and all the responsibility is transferred to the managing director while the German management formally withdraws. The trustworthy managing director therefore has a free hand. The managing director reports a few facts every now and then, but not regularly and not comprehensively. Representatives of the German company fly to Kiev once or twice a year to have a look at the situation, whereby there is no person in Germany who is responsible for the Ukrainian branch office throughout the year. The way in which the daily operations are organised and are run is of secondary importance as long as the branch office records a profit.

However, for some time now profits have gone down considerably and there is a suspicion that something is not right due to the fact that the reports of the managing director do not correspond to the available facts.

Indeed the managing director has in parallel founded an own company with a confusingly similar name and is now guiding the main business through this second company. In addition, the managing director has cancelled the rental contract in the name of the branch office and concluded the main rental contract with the second company. The Ukrainian branch office now only has a sublease contract. The German company now no longer has access either to its business premises or to its warehouse with goods to the value of several million euros. The customers think that the German company no longer operates in the Ukraine as they have been informed by the managing director about the closing of the Ukrainian branch office.

### What can be done now?

The managing director has to be dismissed with immediate effect and a competent and reliable person chosen to take over the company management. In parallel the goods and important business documents must be secured to collect evidence in order to initiate civil and criminal proceedings against the managing director. The Ukrainian branch office also very quickly requires a new domicile and a tax registration.

In this case, Rödl & Partner fully “came to the rescue”, transported the documents away, secured the goods with the aid of a court order and the police and assumed interim

management of the financial accounting and company management. As a result of all these activities carried out by Rödl & Partner it was possible to secure, consolidate and restructure the business.

The comprehensive support offered by Rödl & Partner in this emergency situation was possible through the availability of all the necessary legal experts and experts in the field of financial accounting which enabled Rödl & Partner to make a contribution to save the business operations of this company in the Ukraine.

### What should one have done differently from the beginning?

As a foreign investor one should never blindly trust employees. A systematic control mechanism is also appropriate for an allegedly trustworthy managing director and is not assessed as a loss of confidence when it is applied regularly right from the start. In addition, a closely linked monitoring and control system should be introduced for the complete foreign branch office. Especially if there are no plans to send employees from the parent company to the Ukraine, it is absolutely essential to appoint a person who is responsible for the company in the Ukraine and who several times in the year will visit the subsidiary and report what he has seen with his own eyes.

## Financial Accounting, Taxes

### Background facts:

A company in the field of construction has a perfect product which enables the execution of renovation work particularly in old buildings after water damage without the need for breaking and masonry work. The brand name is only protected as a trademark in Germany. Initially German employees are used for the managing director and sales manager and in addition a Ukrainian employee with very good contacts is taken on for the operative part of the sales activities. It only takes a few pleasant trips and some visits to folklore evenings to persuade the management back home that the German employees are too expensive and completely unnecessary which is also true for the expensive financial accounting and reporting. As a result the personnel are replaced. The Ukrainian employee becomes general director, his son becomes the sales manager and a further member of his family takes over the financial accounting. This person cancels the recognised financial accounting program and makes all the financial accounting entries in Excel. In parallel he founds an own company, registers the brand at the Ukrainian patent office as his own and also registers the brand in a number of other important CIS countries. He carries out the same procedure with the internet domain. Due to the fact that

the liquidity goes down and the parent company now asks in connection with the financing where the revenues are, the managing director claims that the main customer (a large city in the Ukraine) has not paid.

Rödl & Partner is commissioned to take an internal review, whereby the results should lead to clear knowledge and clear measures. Nearly a year passes without any further developments. Then Rödl & Partner is asked to visit the customer (in the large Ukrainian city) and exert pressure to collect the amount which has now risen to 800,000 euros. The city treasurer is able to document each claim and prove that the full amount has been paid. Finally the investor realises that the family has built a large villa and continues to cheerfully distribute the services and products under the "protected" name. In addition, there is an additional demand from the tax authorities for unpaid import turnover tax on construction materials and goods for a three digit number.

### What can be done now?

First of all the company management has to be taken over and the other family members are given notice of termination. The financial accounting has to be taken over and all the processes, as far as they are transparent, have to be reposted in order to prevent a tax prosecution. Furthermore, efforts must be made to contest the registrations of the trademarks and to have the internet domains deleted.

### What should one have done differently from the beginning?

As a foreign investor, one should not have relied on the promises and advice of the local employees. One has to recognise that a combination of business and family is conspicuous. One should have been put on guard at the latest with the takeover of the financial accounting and the lack of information flow. In this case Rödl & Partner helped to clarify tax questions, to correct the financial accounting and to delete the domains.