

Advance Pricing Agreements: terms and conditions, benefits, challenges

Terms and Conditions

- Only large taxpayers can sign Advance Pricing Agreements (“**APA**”)
- The APA sets out the criteria for future controlled transactions of the taxpayer (including the transfer pricing method, arm’s length price/profitability levels).
- The validity term of the APA cannot exceed five years.

Benefits

- Reducing the level of uncertainty in determining whether the controlled transactions are arm’s length, which may protect the taxpayer from additional tax liabilities, fines and penalties
- Cost- and time-saving by making transfer pricing audits redundant
- Avoidance of double taxation by means of bilateral and multilateral APAs.

Challenges

- Insufficient mutual trust to commence the APA process
- No clarity about the approach adopted by the tax authorities in the analysis of typical controlled transactions
- No efficient mechanism to ensure the confidentiality of taxpayer information
- Rigid terms of controlled transactions. External factors can complicate compliance with the APA for the taxpayer (changes in market conditions etc.).

Advance Pricing Agreements: stages (1/3)



Taxpayer's actions

- Send an appropriate letter to the State Fiscal Service of Ukraine (the "SFSU") by e-mail, facsimile, or regular mail
- Provide, either in the form of a presentation or any other convenient form, the information related to:
 - The subject matter and terms of the controlled transaction(s)
 - The business carried out by the parties to the controlled transactions
 - The possible method of determining the prices/profitability level for transfer pricing purposes.

The application is to be supplemented with:

- Draft APA. The preliminary APA structure contains the following:
 - Section 1. Parties to the agreement
 - Section 2. Validity term
 - Section 3. Transactions covered
 - Section 4. Method(s) for determining the prices/profitability level for transfer pricing purposes
 - Section 5. Additional provisions and material assumptions
 - Section 6. Agreement compliance monitoring
 - Section 7. Enforcement of the agreement
 - Section 8. Agreement prolongation
 - Section 9. Agreement termination
 - Section 10. Confidentiality
 - Section 11. Details of the parties
- The taxpayer's constituent and registration documents, financial statements, etc.

- The SFSU notifies the taxpayer of creating a working group and of the necessity to discuss the draft APA and/or to submit additional information
- The SFSU informs the taxpayer of the time, date, and venue of this discussion at least five business days in advance

Advance Pricing Agreements: stages (2/3)

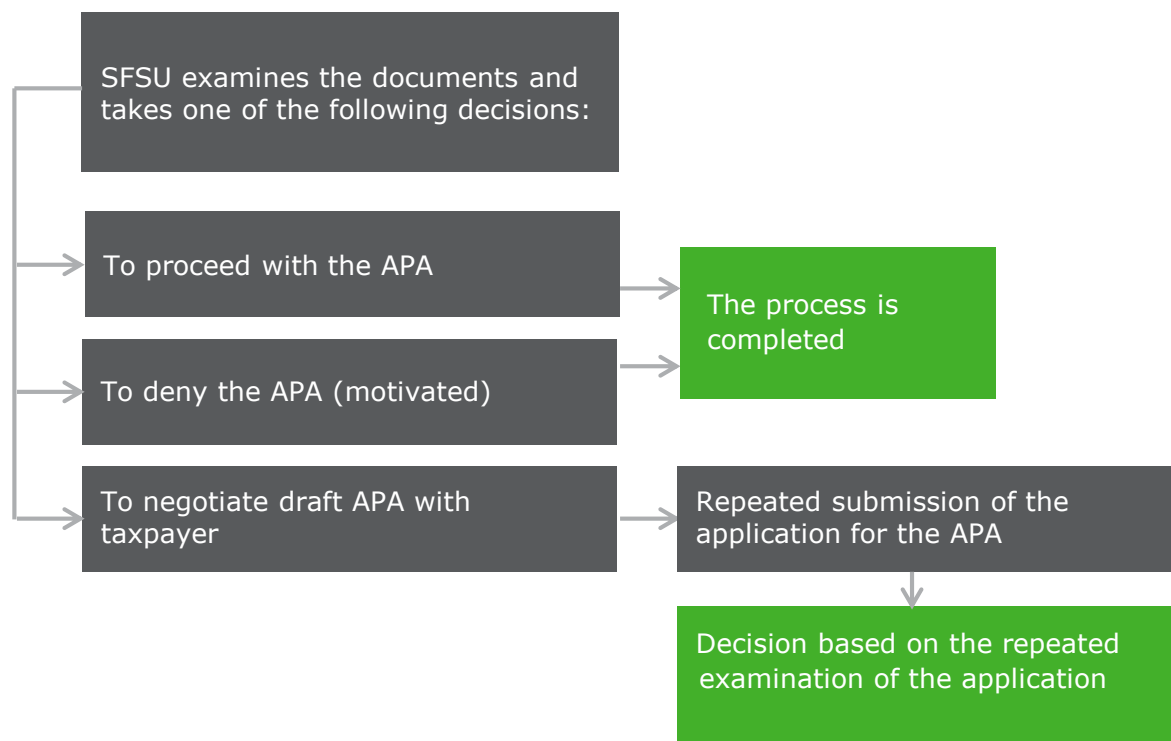


Decision-making regarding conclusion of the APA



Sign the APA

Taxpayer's/SFSU actions



- The APA's **validity term** is established by the parties, but cannot exceed five years
- The APA **takes effect** from January 1 of the calendar year following the year of signing or from the date agreed by both the SFSU and the taxpayer
- The APA must **be signed** by the taxpayer's authorised representative and the Head (Deputy Head) of the SFSU.

Advance Pricing Agreements: stages (3/3)



Taxpayer's/SFSU actions

- The taxpayer should notify the SFSU of all its controlled transactions
- After signing the APA, the taxpayer annually reports on compliance with its terms (by 1 May of the year following the reporting year); the form and substance of the report are specified in the APA

- The prolongation of APA is not envisaged by the current legislation regulating the APA process in Ukraine.

Possible reasons for termination

- Expiry
- By decision of the Head of the SFSU's authorized body, following a breach by the taxpayer
- Early termination by mutual consent
- Non-reporting/submission of inaccurate and/or incomplete information.