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Ukraine's Tax System Reform: Myth or Reality

Government in collaboration with experts has worked out Concept for Ukraine's tax system reforms, which has been introduced to the public recently. The Concept is to determine trends, mechanisms and timings to form an efficient tax system that will provide a favourable environment for the growth of economic activity of both businesses and the economy as a whole, including through its legalisation.

The Concept for the tax system reforms provides:

I. The tax system simplification, meaning:

1) Reducing the number of taxes and duties that are collected in Ukraine. Reducing the amount of taxes and duties from 22 to 8 and providing tax management transparency. Sometimes the expenses for tax management are higher than the tax revenue.

2) Reducing the number of annual dues, time and funds expenditures for maintenance of tax records and tax payments by means of simplification the tax declaration form and implementation of electronic workflow between taxpayers and the regulatory body (including every category of taxpayers).

3) Reforming the tax system to legalise the economy:

a) reforming the VAT system – by introducing differentiated VAT rates which are based on reducing the rate at settlement between VAT payers to 7%, and for transactions with VAT non-payers to 17%;

б) reforming the Consolidated social tax system – by integrating all social security funds into a single consolidated fund and reducing the consolidated social tax from 36.77% to 18% for a six months transition period for those taxpayers who will double their salary budgets.

4) Widening the taxable base for taxes and duties that will be collected to compensate revenue from cancelled taxed and duties, including gradual reduction of tax relieves and special taxation treatments in certain sectors, on the assumption of simultaneously introduced adequate compensatory mechanisms of state support for the sectors that receive such support in competing countries – the EU, USA.

5) Granting tax incentives under the priorities of state social and economic policies, only. Drawing on the European experience, it is reasonable to preserve the social-oriented incentives and the incentives aimed at innovation, power saving and energy efficiency, and simultaneously to increase the level of control over efficiency and the taxpayers responsibility for the failure to achieve social (economic) effect using the tax incentives.

II. Accounting and taxation management harmonisation, meaning:

1) Providing accounting and financial statements based on the International Financial Reporting Standards, with the exception of the enterprises that are defined as SME.

2) Using the financial statements with the purpose of the taxable item estimation for profits tax, in particular, adjustments of financial profit or loss before tax by applying clearly defined list of adjustments which are stimulating or restrictive and which meet the strategic objectives of the state policies.

3) Strengthening the state control over the quality of accounting and financial reporting by involving professional experts in IFRS with the authority to control quality, and implementing the financial monitoring functions; consistent implementation of this Concept, starting from the enterprises of high social impact which are chosen according to their total turnover, total assets and number of employees.

4) Placing increased responsibility on the part of an enterprise management for the quality of accounting and financial reporting. Simplification in taxable item estimation according to the International Financial Reporting Standards and the effective state control will allow meeting the needs of all financial statements users (the state, investors, shareholders and the management) and will promote transparency and legalisation of the taxable items

III. Building-up partnership relations between the tax authorities and tax payers, meaning:

1) Legislative regulation on responsibility of the tax communication parties. The Tax Code should provide kinds of responsibility for illegal actions that may be taken under the tax laws not only to taxpayers but also to the regulatory bodies and officials, as well as a clear mechanism of actions taxpayers should take if their rights are violated.

2) Building-up harmonised communications with taxpayers to ensure willing and unenforced payments of taxes and duties. Ukraine needs to implement the world's principle of regulatory bodies' communications with taxpayers: an explanatory work of a highest standard to inform taxpayers and prevent possible violations, instead of acting on the today's principle of punishment taxpayers for tax offenses.

3) Reducing the pressure on taxpayers through monitoring and checkout measures. Revising and reducing the list of tax audits of taxpayers; creating a separate Financial Investigations Agency; guarantees for the taxpayer's right to choose the auditor for tax compliance audits: regulatory bodies or audit firms that comply with certain criteria.

4) Performing the tax amnesty to legalise the economy.

5) Improving the VAT management, in particular concerning misappropriation and non-refunding of VAT, implementing an efficient regime of automotive refunds.

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