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THE WAYS TO BRING UKRAINE'S TAX LEGISLATION TO EUROPEAN STANDARDS

The main purpose of the study is to analyze the rules of taxation of non-resident payments for consultancy; engineering; construction; legal services; accounting; auditing; software development, supplement and testing services; freight forwarding services; cargo and passenger transportation services; telecommunications and other services.

The urgency of solving this scientific problem lies in the fact that in the process of the study such a poorly researched circumstance as cooperation with foreign companies is taken into account. It requires additional time and money from Ukrainian businesses, not only to pay taxes, but also to obtain additional information and extra documents from their foreign partners confirming the tax presidency of the non-resident counterparty.

The object of the study is to select individual taxation processes for cash payments to non-resident companies for the services provided, as they are a specific indicator in compliance with European standards of tax legislation in Ukraine. The article presents the results of an empirical analysis of the implementation of such rules.

The study confirms that the current tax rules for cash payments to non-resident companies for the services provided are not in line with the tax rules of most EU countries and require improvement. The authors also offer their own alternative recommendations for solving these problems.

Keywords: payments, income, tax legislation, non-resident; taxation; entrepreneurship, economy, services, tax evasion, tax rate.

1. Introduction.

Sustainable taxation is one of the main traditional effective ways of both improving and effective functioning and significant development of social relations of the economic sphere, and its material basis of entrepreneurship. Therefore, the improvement of any legal measures, methods and forms of taxation should be considered as a possible positive step and practical task of the state authorities to reform both the economy of the country as a whole and its material base, the sphere of entrepreneurship in particular.

It is worth noting that, both today and in the past, there have been practically two approaches to convergence and unification of taxation processes in the EU Member States over a long period of time. The content of these approaches can be considered as: substantially divergent and almost similar understanding of the functions, legal and economic implications that the general legal rules (mainly in the form of recommendations) of the European Union taxation can and should be expected in the process of regulation the economies of EU Member States. Today, according to the authors of the article, the last approach prevails in this process. Today there is a general trend in the whole set of institutional and procedural reforms that enable the EU: to establish almost a single legal framework and institutional structure for the creation of an area of freedom, equality, justice and security, in particular in the economic sector of the public relations that are now noted and were noted in the past by foreign scientists and researchers of various economic practices[1] as well as analysts-practitioners of different countries[2].

[1] Coppe, A. (1978*)* Why is it so difficult to achieve monetary union in the EEC? Speech by A. Coppe on a US speaking tour. April 1978. *Archive of European Integration* <http://aei.pitt.edu/11236/1/11236.pdf> (2020, November, 10).
[2] Liivamägi, E. (2017). E-Residency enables anyone to conduct business globally so international taxation must be easier for everyone too. *E-Estonia* <https://e-estonia.com/how-do-e-residents-pay-taxes/> (2020, November, 10).

Trends of reforming the elements of taxation systems in European countries over the years can be observed at the regulatory and analytical level.

The views of some national scholars and economists who specialize in this field have been constantly appealed to bring to European standards separate processes of reforming certain elements of taxation systems[123456].

In both the above mentioned studies and foreign publications, we can find materials dedicated to highlighting unresolved issues that are part of the resolving conflicting issues regarding tax payments to non-resident companies for the services they provide. The issues, which are complex and thoroughly delineated in the title of the article, were not considered or considered as an applied issue in the scientific literature. Therefore, the main purpose of this article is to initiate a scientific and applied discussion regarding taxation of non-resident companies cash payments for services they provide, and to search the methodology of scientific knowledge using, first of all, formal logic methods, comparison, analysis, philosophical method, optimal ways and means of regulation process by the state.

2. An outline of the legal basis

Currently, the tax legislation of Ukraine provides for taxation of payments to non-residents for services rendered by income tax. It is a so-called "repatriation tax" or income tax (similar but not identical to foreign tax – capital income tax, etc.), as well as the analogy of the application, mitigation and optimization of the collection procedure which can be observed and analyzed on various overseas examples.

The procedure of accrual and payment of the mentioned tax in Ukraine stipulates that the resident (tax agent in this case) withholds the specified tax when paying the income and transfers it to the budget. The base rate of the specified tax is 15%, other rates are also applicable, for example, for the 6% freight. This tax creates additional obstacles in the way of cooperation of domestic companies with foreign partners and limits the choice of contractors for doing business. Similar obstacles are observed and noted by researchers of taxation processes for non-resident corporate executives in the UK[7]. In the same context, attention is drawn to possible liability measures for breach of tax rules of certain entities of the US Federation. And this is despite the fact that "in the UK (as in the US) there are clear legal mechanisms and relevant subdivisions under state business support bodies for a long time", also "there is a system of subcontracting that allows large enterprises to transfer part of the orders to small businesses"[8], in such cases, in practice, there is often a tax on cash payments to non-resident companies for the services they provide. It can be stated that in the EU countries, the USA, the UK, Canada and in some other economically developed countries, "micro-level intervention has become a major part of the national economic strategy"[9]. In some cases, where the counterparty cannot be replaced, it may complicate business processes and taxation processes

[1] Саніахметова, Н. О. (1988). Регулювання підприємницької діяльності в Україні (організаційно-правові аспекти): *дисертація на здобуття наукового ступеню доктора юридичних наук*. Одеса: Одеський національний університет ім. І. Мечнікова, 403.

[2] Юлдашев, О. Х. (2005). *Проблеми вдосконалення державної регуляторної політики в Україні*. Київ, 336.

[3] Клим, О. В. (2009). Адміністративно-правове регулювання підприємницької діяльності в Україні: *дисертація на здобуття наукового ступеню кандидата юридичних наук*. Київ: НАН України, Ін-т держави і права ім. В.М.Корецького, 205.

[4] Бояринова, К. О. (2007). Механізм організаційного забезпечення інноваційного підприємництва: *автореферат дисертації на здобуття наукового ступеню кандидата економічних наук*. Київ: Національний технічний університет України «Київський політехнічний інститут імені Ігоря Сікорського», 21.

[5] Галахова, Т. О. (2015). Креативний компонент у менеджменті міжнародних компаній: *дисертація на здобуття наукового ступеню кандидата економічних наук*. ДВНЗ «Київський національний економічний університет імені Вадима Гетьмана» <https://kneu.edu.ua/userfiles/d-26.006.02/2015/ Dis_Galahova.pdf> (2020, November, 10).

[6] Диндар, А. С. (2015). Регулювання АРТ-бізнесу в креативній економіці ЄС: автореферат дисертації на здобуття наукового ступеню кандидата економічних наук. Київ: ДВНЗ "Київський національний економічний університет імені Вадима Гетьмана". <https://drive.google.com/file/d/1nkRuyYX2JmSxCJ6BmheTqL0VVPyl1wIM/view> (2020, November, 10).

[7] Knight, L. (2019). The perils and pitfalls of non-UK resident directors. *TAX Adviser Magazine* <https://www.taxadvisermagazine.com/article/perils-and-pitfalls-non-uk-resident-directors> (2020, November, 10).

[8] Клим, О. В. (2009). Адміністративно-правове регулювання підприємницької діяльності в Україні: *дисертація на здобуття наукового ступеню кандидата юридичних наук*. Київ: НАН України, Ін-т держави і права ім. В.М.Корецького, 205.

[9] Саніахметова, Н. О. (1988). Регулювання підприємницької діяльності в Україні (організаційно-правові аспекти): *дисертація на здобуття наукового ступеню доктора юридичних наук*. Одеса: Одеський національний університет ім. І. Мечнікова, 403.

in particular, which almost always leads to an increase in the cost of foreign counterparty services or the time spent to obtain additional certificates in order to avoid double taxation and other difficulties[12].

The main normative act that provides for taxation of payments to non-residents by income tax (repatriation) is the Tax Code of Ukraine. In particular, paragraph 141.4 "Peculiarities of taxation of non-residents" of Article 141 is entirely devoted to the ordering of public relations related to these issues. Sub-paragraph 141.4.2 of paragraph 141.4 of Article 141 of the Tax Code stipulates that "a resident or permanent establishment of a non-resident who performs for the benefit of a non-resident or a person authorized by him (except for the permanent representation of a non-resident within the territory of Ukraine) any payment from the income with source of origin from Ukraine obtained by such non-resident activities withholding tax on such income specified in the sub-paragraph 141.4.1 of this paragraph, at the rate of 15 percent (except for the income specified in sub-paragraphs 141.4.3-141.4.6 and 141.4.11 of this paragraph) of their amount and at their expense paid to the budget at the time of such payment, if otherwise, the provisions of the international treaties of Ukraine with the countries of residence of the persons in favor of which the payments have entered into force, are not stipulated".

Thus, as noted, the base rate at which non-resident income tax is 15%, for some types of non-resident income, such as freight, the rate is set at 6%, and for non-resident income producing and distributing advertising is 20%. The tax is withheld by a resident company of Ukraine at the time of payment of non-resident income and transferred to the budget. This is a non-resident income tax, or sometimes referred to as a "repatriation tax", although there is no such formal definition of tax in the Tax Code of Ukraine.

Let us emphasize that the income for the services provided by a non-resident is paid by the resident company of Ukraine with the deduction of the "repatriation tax" and only when receiving advertising services is paid at the expense of the resident's own funds.

3. Analysis of the described situation and its comparison with foreign analogues

What kind of payments will be taxed by the specified tax? This is the payment for the services specified in sub-paragraph 141.4.1 of Article 141 of the Tax Code, such as freight and engineering income, income from the sale of real estate, leasing/rent and other income from the conduct of non-resident economic activity within the territory of Ukraine. As the definition of "other income" includes a wide range of services, it turns out that in fact, the vast majority of revenues for any services the place of provision of which will be determined by the territory of Ukraine will be subject to this tax. It should be emphasized that only income with source of origin from Ukraine is subject to taxation, not any income received by a non-resident from a resident. According to paragraphs 141.4.1 of Article 141 of the Tax Code the repatriation tax is not deducted from income in the form of proceeds or other types of compensation for the value of goods, works performed, services rendered, transferred, performed, provided to a resident by such non-resident (permanent establishment), including the cost of services provided by international communication or international information support.

As a result, the logical question arises: "Is it always necessary to withhold tax when paying income to non-residents?" Based on the current legislation of Ukraine it is necessary to answer: "No, not always".

In this context, firstly, it is necessary to determine clearly whether the type of income and the place of provision of services for which the non-resident pays income tax are subject to the repatriation tax. In other words, it is necessary to determine correctly the object of taxation. If a particular form of income is not subject to tax, then there should be no repatriation tax. For example, agency services which are provided by a non-resident person but within the territory of another state will not be subject to taxation or non-resident income in the form of compensation for the use of a computer program (the conditions of use being limited by the functional purpose of such program and its reproduction limited by the number of copies required for such use), including compensation for the cost of servicing such software, if such services do not fall within the definition of "engineering".

In this case, the resident does not need to obtain a certificate from the non-resident confirming the residence of a particular state, since the transaction is not subject to taxation under paragraph. 141.4.1 of Article 141 of the Tax Code.

[1] Бояринова, К. О. (2007). Механізм організаційного забезпечення інноваційного підприємництва: *автореферат дисертації на здобуття наукового ступеню кандидата економічних наук*. Київ: Національний технічний університет України «Київський політехнічний інститут імені Ігоря Сікорського», 21.

[2] Галахова, Т. О. (2015). Креативний компонент у менеджменті міжнародних компаній: *дисертація на здобуття наукового ступеню кандидата економічних наук*. ДВНЗ «Київський національний економічний університет імені Вадима Гетьмана» <https://kneu.edu.ua/userfiles/d-26.006.02/2015/ Dis_Galahova.pdf> (2020, November, 10).

Secondly, if the payment is made for the service that is subject to tax by the specified tax, the information about the residence of a foreign partner should be found out. If he is a resident of the country with which the double tax treaty is concluded, the domestic business entity that is the tax agent for that tax, the rules of the double tax treaty for possible exemption from taxation or the application of a reduced rate to the specified tax should be analysed.

Thus, in accordance with the provisions of paragraph 103.2 of Article 103 of the Tax Code of Ukraine, the application of international treaty in respect of tax exemption or the application of a reduced tax rate is allowed only on condition that the non-resident person (tax agent) provides a certificate (or a duly certified copy thereof) issued by the competent authorities of a foreign state that confirms that a non-resident is a resident of the country with which Ukraine has concluded an international agreement. In addition, there are additional requirements, for example, the specified certificate must be translated into Ukrainian and legalized in due course.

For the States Parties to the 1961 Hague Convention, an apostille document is sufficient. However, if an international legal aid agreement is signed with a foreign country, an official document issued by the competent authority of that state may be accepted without additional certification. Such countries include Bulgaria, Georgia, Estonia, Latvia, Lithuania, Poland, Czech Republic and others. This reference should be updated annually. Pursuant to paragraph 103.8 of Article 103 of the Tax Code, a resident who pays non-resident income in the reporting (tax) year may apply the rules of the international agreement of Ukraine on exemption (reduction) from taxation on the basis of the certificate for the previous year, provided that the new certificate (for the current year) will be received after the end of the reporting (tax) year.

Thus, from the above we summarize that to avoid repatriation tax payment or lower its rate in Ukraine, it is possible in the following cases:

Firstly. When income is not subject to tax.

Secondly. Subject to receipt from the non-resident of a certificate confirming that the foreign partner is a resident of the country with which the international agreement (convention) of Ukraine is concluded, stating that the income paid by the resident is not taxed or taxed at a reduced rate. In addition, according to paragraph 103.2 of Article 103 of the Tax Code of Ukraine to apply the tax exemption or reduced tax rate stipulated by the relevant international agreement, it is possible only on condition that the non-resident is the beneficial (actual) recipient (owner) of the income.

In the first case, the evasion of repatriation tax is clear. It has no taxable object – no tax is paid. A similar case can be illustrated as follows. Non-resident income in the form of compensation for the use of a computer program, provided that the use is limited by the functional purpose of such program and its reproduction is limited by the number of copies required for such use (use by the "end consumer"), simply, when such income is not royalty; compensation for the cost of servicing such software, if such services do not fall under the definition of "engineering" and so on. In these cases, there will be no taxable object according to the rules of the tax legislation of Ukraine.

On the contrary, regarding the second case of tax evasion or reduction, it should be emphasized that it requires more detailed clarification, because in practice domestic business entities face problems in obtaining certificates and defining the beneficial owner status. In our view, this is mainly because Ukrainian tax legislation needs to be improved and brought in line with certain modern European standards. Accordingly, tax authorities still have the possibility of interpreting the rules of tax legislation at their discretion, which does not always contribute to the improvement of public relations in the sphere of entrepreneurship of Ukraine. In this sense, it should be agreed that business regulation should not only be compelled and justified in terms of management and economics, but also be as fair and equitable as any governmental influence on justified economy and entrepreneurship, first of all, supporters of the "market failures" theory. According to this theory, when a completely free market fails, government regulation can and should improve the economic situation[1].

We will analyze these problematic issues in details and pay attention to the concept of beneficial (actual) recipient (owner) of income. In this context, should a domestic entity determine whether the foreign partner is the ultimate beneficial owner of the income and what documents or information should be available from the domestic entity to confirm that its foreign business partner is the beneficial owner of the income.

In this context, it is important to note that it is not clear to define response from the domestic legislator in the field of taxation. The list of necessary documents depends on the specific situation, which is stated

[1] Ronen, J. (1993). *Some insights into intrepreneural process. Entreprenership*. Lexington, 208.

in the publicly available information and reference resource of the tax authority, which also can not be attributed to the positive means and measures of public relations adjustment in the field of business of Ukraine, since by analogy of legal regulation through the administrative discretion of tax authorities EU countries should regard this measure as a compelled exclusive measure of legal influence on the behavior of the taxable entity. In this sense, it is appropriate to turn to the theory of "public interest". The essence of this theory is that if the free market is not able to efficiently allocate resources and meet consumer demands, it is the state, at the legislative level, which should regulate this market to transform the economic situation in the public interest.[1] In the context of this study, it is in the interests of domestic entrepreneurs and non-resident business entities providing certain services in the consumer market of Ukraine.

For example, the question "What supporting documents should a taxpayer have to prove that a non-resident person in favor of whom dividends, interests, royalties are the beneficial (actual) recipient (owner)?" Its answer is placed in the paragraph 102.21 of the public information and reference resource, for example, Article 52 of the Tax Code of Ukraine to obtain individual tax advice orally from the State Tax Service bodies or in a written form from the Regional Tax Offices, Kyiv, or Large Taxpayers Office of the State Tax Service, or the State Tax Service of Ukraine, since the documents for recognition of a non-resident are beneficial (factual) the recipient (owner) of income with the source of their origin from Ukraine are considered separately on a case-by-case basis. In our opinion, it demonstrates that today it is necessary to improve radically the national legislation, which defines the legal capacity of control and supervisory bodies and is an obstacle to the implementation of reforms in the public administration system as a whole[2]. In our study, it concerns, first of all, the current legal framework that defines the tasks and functions, forms and methods of activity of the State Tax Service of Ukraine.

So, without having a clear answer to the regulatory solutions to the practical situations described above, let us try to look into their possible settlement. Namely, let us turn to the consideration and analysis of the application of individual tax consultations, which the officials of the State Tax Service of Ukraine provided to specific payers according to Article 52 of the Tax Code.

In particular, in the individual tax consultation dated 06.12.2017 №2858/6/99-99-15-02-02-15/IPK the tax specialists state that any document confirming the factual right may be a document for recognizing a person as the actual owner of income for such income. That is, in accordance with the logic of the tax authority, in the case of payment of royalties, the actual owner of such income must confirm the actual right (copyright) to receive such income, duly certified and, accordingly, documented by a license, patent, official trade mark and so on. In addition, relevant licensing agreements for the use of intellectual property rights, as well as franchise agreements, etc., are required.

In another individual tax consultation dated July 25, 2017, No.1344/6/99-99-15-02-02-15/IPC, domestic officials explain the procedure for taxation of income tax received from a non-resident freight forwarder from Ukraine registered in Austria. In fact, there are two cases: 1) if the international transportation was performed directly by the non-resident forwarder; and 2) in case of involvement of a third party by the freight forwarder.

According to the tax authority, the provisions of the international agreement on avoidance of double taxation, concluded between Ukraine and Austria, which provides for exemption from taxation for this type of income, apply only to the first case, namely – when the freight forwarder carries out international transportation.

But when the freight forwarder attracts other persons to carry out the transportation, the resident customer, according to officials of the domestic tax authorities, will still have to withhold the tax on the income of the non-resident. And interestingly, the tax authority this time does not exploit the thesis that the freight forwarder is not a beneficial recipient of income. After all, the Supreme Administrative Court of Ukraine in its decision of 24.03.2014. No. K/800/52155/13 argued that the concept of "beneficial (actual) income earner" should be interpreted in a narrow technical sense.

According to officials of domestic tax authorities, such payment does not fall under the provisions of a bilateral international legal act on the application of tax exemption. In fact, saying that transportation

[1] Саніахметова, Н. О. (1988). Регулювання підприємницької діяльності в Україні (організаційно-правові аспекти): *дисертація на здобуття наукового ступеню доктора юридичних наук*. Одеса: Одеській національний університет ім. І. Мечнікова, 403.

[2] Гаращук В. М. (2003). Теоретико-правові проблеми контролю та нагляду у державному управлінні: *автореферат дисертації на здобуття наукового ступеню доктора юридичних наук*. Харків: Національна юридична академія України ім. Ярослава Мудрого, 35.

services are not exactly the same, but are some other services, without specifying which ones. In our opinion, this is quite controversial, unsubstantiated and unconvincing. So, Letter of the State Tax Service of Ukraine has all the elements of a void regulatory act.

In addition, the same individual tax consultation states that: **"**Paragraph 103.3 of Article 103 of the Code establishes that the beneficiary (actual) recipient (owner) of income for the purposes of applying the reduced tax rate in accordance with the rules of the international agreement of Ukraine to dividends, interest, royalties, rewards, etc. of the non-resident received from sources in Ukraine, is considered a person entitled to obtaining such income. "However, the beneficial owner (actual) recipient (owner) of the income may not be a legal person, even if such person is entitled to income, but is an agent, a nominal holder (nominal owner), or is only an intermediary in respect of such income".

The decision of the Supreme Administrative Court of Ukraine dated 24 March, 2014, No. K/800/52155/13 contains an interpretation of the term "beneficial (actual) income recipient (owner)". So, "actual income earner" should not be interpreted in a narrow, technical sense, its meaning should be determined based on the purpose, objectives of international double tax treaties, such as "tax avoidance", and taking into account such basic principles as "prevention of abuse of the contract." In order to identify a person as the actual recipient of income, such a person must not only have the right to receive income, but also, in accordance with the international practice of applying double tax treaties, must be a person who determines the further economic share of income. The document for recognizing a person as the actual owner of income may be a document confirming the person's right to such income, including but not exclusively a document issued by the competent authority of the country with which the international treaty of Ukraine is concluded.

Taking everything into account, it should be considered that if, within the framework of an agreement on the provision of freight forwarding services between a resident of Ukraine (who is a customer) and a resident of Austria (who is the freight forwarder), the carriage of goods by road is carried out directly to the freight forwarder, freight paid by a resident of Ukraine in favor of an Austrian resident freight forwarder is exempt from taxation in Ukraine under the Convention subject to the provision of an Austrian resident certificate of residency that meets the requirements defined by Article 103 of the Tax Code.

If an Austrian resident forwarder engages third parties for the purpose of the contract of carriage of goods, compensation for the cost of services rendered by such non-resident forwarding client to Ukraine shall not be subject to the provisions of the Convention for the application of tax exemption.

Absence of the status of beneficiary makes it impossible to apply the procedure of avoidance of double taxation according to Article 103 of the Tax Code of Ukraine. In this case, the status of the beneficiary to the non-resident who is the executor under the contract of carriage, but when carriers are indicated in the international transport documents? In practice, such a contract of carriage provides for the right of the contractor to attract third parties to perform services under this contract. Currently there is no clarification or case law regarding the status of the ultimate (beneficial) recipient of a non-resident who has recruited third parties to perform the contract. Therefore, analyzing the provisions of the Tax Code, it will be correct to state that a non-resident in such agreements retains its beneficiary status in relation to the income received.

Thus, it should be concluded that the taxpayer has the right to use the double taxation procedure for the payment of income in the form of freight.

In addition, there are some views that the introduction of capital duty tax is contrary to Ukraine's fulfillment of its international obligations in the field of taxation and counteracting tax evasion. For example, Ukraine's initiative to join the MLI (Multilateral Agreement, which provides for almost automatic amendments to the double taxation conventions) may raise some questions for Ukraine's Western partners in good faith. That is, the question of the future proper implementation of such conventions in the case of capital injections remains debatable[1].

4. Conclusions

Summarizing that despite the fact that the authors support the opinion on the introduction of capital tax, which is appropriate to be introducd instead of income tax, we believe that to choose the optimal model of taxation, including cash payments to non-resident companies for their services, it is worth considering foreign experience, but do not put implementation of foreign measures and means in the field of taxation in the first place when choosing domestic tax rules, in particular regarding cash payments to non-resident companies for providing their services.

[1] Боксер, І. (2019). Ратифікація MLI-конвенції: наслідки для України. *Юридична Газета* <http://yur-gazeta.com/publications/practice/podatkova-praktika/ratifikaciya-mlikonvenciyi-naslidki-dlya-ukrayini.html> (2020, November, 10).

First of all, in order to achieve optimization of public relations in the field of taxation, law enforcement activities must first be based on the principles of honesty[1] and justice[2], which should be legally enshrined in tax law, which has become a regular rule for many legal systems in EU countries, and which have long been called upon by research scientists on pressing economic and legal issues[3], at the same time we support the position on the justification of the idea of convergence of the financial and tax systems of European countries by the European governing institutions. At the same time, we believe that, in practice, the implementation of these principles in the consciousness and legal understanding of the highest level of national statesmen will be a step forward in the development and construction in Ukraine of the so-called "modern Dicey's concept of rule"[4] on the fair and honest optimization of public relations in the field of taxation, and on the cash payments to non-resident companies for the services they provide, in particular.

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