With effect from 1 January 2013, reformed transfer pricing rules have introduced an anti-avoidance tool aimed at transactions between local companies and unrelated counterparties located in so-called black-listed jurisdictions.

1. Introduction
With effect from 1 January 2013, reformed transfer pricing rules (article 39 of the Tax Code) have introduced an anti-avoidance tool aimed at transactions between local companies and unrelated counterparties located in so-called black-listed jurisdictions.

This article presents the current key features of this tool.

2. Definition of Controlled Transactions
Transactions that meet value thresholds between a Ukrainian company and a resident of a black-listed jurisdiction are defined as controlled transactions for transfer pricing purposes, even if parties to the transaction are not related entities. The value thresholds are as follows (per reporting year):

- total revenue of a local entity: over UAH 50 million; and
- total value of transactions between a local company and a foreign counterparty: over UAH 5 million.

Local entities must file an annual transfer pricing report and prepare transfer pricing documentation in respect of controlled transactions. Such transactions are subject to transfer pricing audits.

3. Enforcement Measures
Non-compliance with the above requirements triggers the following implications:

- fine for failure to file a report on a controlled transaction: UAH 365,400;
- fine for non-disclosure of a controlled transaction in the controlled transactions report: 1% of the controlled transaction value, with a maximum fine of UAH 365,400 for all controlled transactions; and
- fine for failure to file transfer pricing documentation: 3% of the controlled transaction value, with a maximum fine of UAH 243,600 for all controlled transactions.

In addition, there is a limitation on the deductibility of expenses incurred on purchases from residents of black-listed countries (article 140.5.4 of the Tax Code). In particular, the amount of the deduction for purchases from residents of such jurisdictions is limited to 70% of the actual expense. However, this limitation does not apply if a local company prepares a transfer pricing report and maintains documentation.

The deduction limitation also applies to transactions that are below the threshold for controlled transactions. For such transactions, there is no requirement to prepare a transfer pricing report or documentation. However, a local company should be prepared to justify that contractual prices are in line with market prices.

4. Black-Listed Countries
Black-listed jurisdictions for 2015 were determined by Cabinet of Ministers Orders 1042 (25 December 2013), 449 (14 May 2015), 677 (1 July 2015) and 977 (16 September 2015). The black list was amended several times during 2015 and, as at 1 November 2015, the list includes 65 jurisdictions.

Black-listed jurisdictions are specified below, along with an indication (where applicable) of a period for which relevant country was on the list.

Albania (1 January 2015-14 May 2015), Andorra, Anguilla, Antigua and Barbuda, Aruba, Austria (14 May 2015-1 August 2015), Bahamas, Bahrain, Barbados, Belize, Bermuda, Bosnia and Herzegovina, British Virgin Islands, Brunei, Bulgaria, Canary Islands, Cape Verde, Cayman Islands, Cook Islands, Curacao, Cyprus, French Guiana, Georgia (1 January 2015-16 September 2015), Gibraltar, Grenada, Guadeloupe (1 January 2015-16 September 2015), Guernsey, Hong Kong (from 14 May 2015), Ireland, Isle of Man, Jamaica (1 January 2015-16 September 2015), Jersey, Kosovo, Kyrgyzstan, Labuan, Lebanon (1 January 2015-16 September 2015), Macau, Macedonia, Madeira, Maldives, Malta (1 January 2015-16 September 2015), Mariana Islands, Marshall Islands, Martinique, Micronesia, Moldova, Montenegro, Montserrat, Morocco (1 January 2015-16 September 2015), Nauru, Niue (from 14 May 2015), Palau, Panama, Paraguay, Qatar, San Marino, Sao Tome and Principe, Seychelles, Singapore (1 January 2015-16 September 2015), St. Kitts and Nevis, St. Lucia, St. Martin, St. Vincent and the Grenadines, Sudan, Switzerland (1 January 2015-16 September 2015), Timor-Leste, Turkmenistan (from 14 May 2015), Turks and Caicos Islands, United Arab Emirates (1 January 2015-16 September 2015), US Virgin Islands, Uzbekistan and Vanuatu.
5. Risk Management Actions

There is a risk of a dispute with the tax authorities and fines due to the fact that it is not clear whether the value threshold (UAH 5 million per single counterparty) should apply in respect of transactions conducted for the entire year or only in the period during which the country was on the black list.

Consider the following example that illustrates this uncertainty: Austria was on the list from 14 May to 1 August 2015. The value of the transactions of a Ukrainian retailer with an unrelated resident of Austria during the period from 1 January to 1 April 2015 was UAH 12 million, while the value of the transactions during the period from 15 April to 30 July 2015 was UAH 4 million. Under a literal reading of the law, transactions with a resident of Austria should be treated as controlled if the total value of transactions in 2015 exceeds UAH 5 million. However, it is possible to argue that only transactions conducted during the period when the country was on the black list should be taken into account. Under such an interpretation, transactions will not be viewed as controlled ones, as the UAH 5 million threshold is not reached. At the time of writing this article, the tax authorities have not issued any ruling on this matter.

In order to avoid the risk of fines and corporate profit tax exposure, the management of Ukrainian companies is advised to pay special attention to transactions in 2015 with residents of Albania, Austria, Georgia, Guadeloupe, Hong Kong, Jamaica, Lebanon, Luxembourg, Morocco, Singapore, Switzerland, Turkmenistan and the United Arab Emirates.