Introduction of VAT on electronic services of non-residents, abolishment of tax on non-residents' income from creation and/or distribution of advertisement

On 3 June 2021, the Verkhovna Rada of Ukraine adopted a draft law “On Amendments to the Tax Code of Ukraine on Abolishment of Taxation of Income Received by Non-residents in the Form of Payment for Production and/or Distribution of Advertisement and Improvement of Value Added Tax Procedure for Transactions on Supply of Electronic Services to Individuals by Non-residents” (registration No. 4184; hereinafter - the “Law”) in the second reading. The Law introduces value added tax (“VAT”) rules on supplies of electronic services by non-residents to individuals as well as provides some other amendments to the Tax Code of Ukraine (“TCU”). The Law shall become effective after its signing by the President from the date following its publication, except for certain provisions that come into force starting 1 January 2022. At the same time, new VAT rules on supplies of electronic services by non-residents will be applicable to the tax periods from 1 January 2022.

There is no final wording of the Law so far. This review is based on the available tax of the draft Law for the second reading. In addition, implementation of the Law will require adoption of bylaws and issuance of rulings that would explain application of the Law's provisions.

Non-resident as a VAT payer

A non-resident, who does not have a permanent establishment and who supplies electronic services within the customs territory of Ukraine to individuals, including private entrepreneurs not registered as VAT payers (hereinafter - “Individuals”), can be considered as a VAT payer. At the same time, a non-resident shall not qualify as a VAT payer when it:

- supplies electronic services under intermediary agreements, if the invoices provided to services' customers define a list of electronic services and their actual provider;
- only processes payments for electronic services, but does not participate in the provision of electronic services;
- supplies electronic services directly through its permanent establishment in Ukraine.
A non-resident is obliged to register as a VAT payer if the volume of its electronic services (with their place of supply within the customs territory of Ukraine) supplies to Individuals in the previous calendar year exceeds UAH 1 million according the NBU exchange rate as of 00:00 AM January 1 of the respective year. Such registration application shall be submitted by 31 March inclusive of the respective calendar year following the year in which the non-resident has reached the specified volume of transactions.

Non-residents who have reached the above indicators in 2021 have to apply for registration as a VAT payer by 31 March 2022. Various interpretations of this provision cannot be excluded, namely regarding determination of supplies' volume in 2021, that requires registration of a non-resident as a VAT payer.

The Law provides a possibility of voluntary registration as a VAT payer if a non-resident has not reached mentioned supplies' threshold.

In case of non-resident's registration as a VAT payer, such non-resident is automatically registered within the tax authorities at the same time.

**Electronic services: definition and list**

According to the Law, electronic services are the services provided via the Internet, automatically, by virtue of information technologies and mainly without human intervention, including by installing a special application on smartphones, tablets, television receivers and other digital receivers.

The Law establishes a non-exclusive list of electronic services, particularly including:

- supply of electronic copies, granting access to images, texts and information
- providing access to databases
- supply of electronic copies and/or provision of access to audiovisual works, video and audio on demand, games, including supply of services on participation in such games, supply of services for access to TV programs (channels) or their packages, except for access to TV programs simultaneously with their broadcasting through the television network
- access granted to information, commercial, entertainment electronic resources and other similar resources
- supply of distance learning services via the Internet, which conducting and providing does not require human participation (with certain exceptions)
- supply of cloud services as it pertains to provision of computing, storage resources or electronic communications systems using cloud computing technologies
- supply of software and updates to it, including electronic copies, provision of access to them, as well as remote maintenance of software and electronic equipment
- provision of advertising services on the Internet, mobile apps and other electronic resources, providing advertising space.

At the same time, the following transactions will not be considered electronic services:

- supply of goods and/or other services other than electronic, which include electronic services, if the cost of the latter is included in the total cost of such goods or services
- supply of distance learning services via the Internet, if the Internet is used exclusively as a means of communication between the teacher and the listener
- supply of copies of works in the field of science, technology, art on material media
- supply of consulting services by e-mail
- supply of internet access services.

**Electronic services: place of supply**

As a general rule, the place of supply for electronic services is considered to be the location of the services' recipient.

For individuals registered as private entrepreneurs, the place of supply of electronic services is considered to be the place of their registration as business entities.

If the recipient of electronic services is an individual not registered as a business entity, the place of supply of services is the actual location of such an individual. At that, the Law establishes rules for determining the actual location for various means of communication through which electronic services can be provided:

- fixed connection: location of the telecommunications provider, which services were used by an individual when receiving services
- mobile connection: the country identified by the mobile country code of the SIM card used when receiving such services
- other means of connection, including through access cards: the country in which the following other means of communication are located, or to which the access card is sent for its use.

Additional indicators of an Individual's location are his/her payment address, bank details and other commercially important information.

**VAT base and rate**

The tax base of VAT on supply of electronic services by a non-resident is the cost of such services. VAT is 20% of the tax base and shall be added to the cost of electronic services, except for VAT-exempted transactions. At that, a non-resident does not recognize input VAT (VAT credit) and does not draw up VAT invoices on supply of electronic services to Individuals.
VAT reporting and settlement

The base reporting period for non-residents registered as VAT payers is the quarter. A non-resident registered as a VAT payer shall prepare and submit a simplified tax return (in Ukrainian or English) within 40 calendar days following the last calendar day of the reporting (tax) period. A non-resident registered as a VAT payer is obliged to submit tax return even in the absence of taxable transactions.

The amount of VAT liability specified in the tax return shall be paid within 30 calendar days following the last day of the deadline for filing the tax return. VAT shall be paid in foreign currency (US dollar or Euro) to a foreign currency account opened for the State Treasury Service of Ukraine in an authorized bank.

Interaction with the tax authorities and responsibility

The Law stipulates that communication between non-residents registered as VAT payers with the tax authorities (filing declarations, complaints, receiving requests, etc.) will take place through a special electronic portal for non-residents.

The controlling authorities are granted with rights to conduct desk audits of non-residents’ simplified tax returns and send requests to non-residents for generalized information on supply of electronic services to individuals in the customs territory of Ukraine, the cost of the services provided and the timing of their payment.

The tax authorities will have the right to send special tax notifications to non-residents registered as VAT payers (if they fail to submit a tax return, non-payment of tax, etc.), as well as to non-residents who have not fulfilled the requirements for mandatory registration as a VAT payer (notification will be sent through the competent authority of a foreign state).

In case of non-compliance with the requirements for mandatory registration as a VAT payer, a tax fine will be applied to a non-resident in the amount of 30 minimum wages as of 1 January of the reporting year (ca. USD 6.6k in 2021).

The Law also establishes a significant number of procedural aspects regarding the registration of non-residents as VAT payers, cancellation of such registration, communication between a non-resident and the tax authorities, etc. For a detailed settlement of such aspects, it is envisaged to adopt subsidiary legislation.

Other changes

The Law provides the abolishment of the 20% tax on payments to non-residents for the production and/or distribution of advertisement, which is currently stipulated in para. 141.4.6 of the TCU. This clause enters into force on 1 January 2022.

The Law clarifies certain aspects of the administrative appeal procedure of decisions of the tax authority (in particular, regarding decisions taken against non-residents operating in Ukraine through branches, including permanent establishments).

The Law establishes that for documents drawn up in electronic form, the date of execution of the document certifying the fact of services’ supply by the taxpayer is considered to be the date specified in the document itself as the date of its preparation in accordance with the Law of Ukraine "On Accounting and Financial Reporting in Ukraine", regardless of the date of the electronic signature.

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We will continue to monitor the developments and will inform you about important changes in VAT on supply of electronic services to individuals.
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