The Private Wealth & Private Client Review

Fourth Edition

Editor
John Riches

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EDITOR'S PREFACE

There is no doubt that the twin recurring themes for 2015 at a global level in private wealth planning are those of transparency and regulation. The zeal of policy makers in imposing ever more complex and potentially confusing sets of rules on disclosure of beneficial ownership information seems unabated.

i Common reporting standard (CRS)

The centrepiece of cross-border automatic information exchange is CRS. This FATCA equivalent for the rest of the developed world is set to come into effect from 1 January 2016. At the last count just over 90 countries had committed to CRS. Its principal effects will be felt in two waves – among the so-called early adopters group the rules will take effect from 1 January 2016 and first information exchanges will apply in September 2017. For the second wave, there will be a year's delay.

What is interesting about CRS is that the OECD has taken a central role in producing coordinated guidance on its interpretation. The draft guidance initially published in July 2014 was somewhat sketchy in nature and we can expect, as we move towards the beginning of next year, revised and more detailed guidance on a number of key issues.

Deep concerns exist about the extent to which information exchange between tax authorities under CRS will remain secure in the hands of the 'home' countries of beneficial owners. While the 'normal' way of signing up to CRS is via the multilateral convention that provides for exchange with other signatory nations, there are indications that some jurisdictions (at this stage the Bahamas, Hong Kong and possibly Switzerland) may seek to adopt a more 'bilateral' approach implementing CRS. If this approach becomes more widespread, then the practical implementation of CRS could be significantly delayed by jurisdictions who negotiate treaties on a one-by-one basis with 90 other countries.

While CRS is often compared to FATCA, there are some material differences that emerge from closer scrutiny. Whatever the shortcomings of FATCA, the ability to issue a global intermediary identification number and to sponsor entities on a cross-

border basis somewhat lessens the bureaucratic excesses of its impact. What is distinctly unclear about CRS at this point is whether equivalent mechanics will emerge. As CRS is currently written as a series of bilateral treaties between jurisdictions with no domestic law 'anchor' (as is the case with FATCA) concerns are being expressed about the potential duplication for complex cross-border structures of reporting. In this context, the July 2014 introduction to CRS notes that the rules as to where a financial institution (FI) will be deemed resident differs between jurisdictions – in some cases this will be based on the place of incorporation whilst in others it may be based on the place of effective management.

There are concerns as to how non-financial entities (NFEs) will be dealt with under CRS. There is anecdotal evidence emerging already in the context of FATCA that financial institutions, driven by concerns about fines from regulators for NFEs and the related ownership structure are subjecting bank account applications for NFEs to additional enquiries that generate very significant costs and delay.

It is noteworthy that there has been a significant crossover from the anti-money laundering (AML) or terrorist financing regime coordinated by the Financial Action Task Force (FATF). This is expressly provided in the CRS model treaty that imports into CRS the FATF concept of beneficial ownership. In the CRS world, this is known as 'controlling persons'. By expressly linking the definition of controlling persons to that of beneficial ownership employed for FATF purposes, there is the prospect of the beneficial ownership definition evolving over time in accordance with principles adopted in that domain. It is noteworthy that, as well as looking to ultimate legal and beneficial ownership of an entity, these definitions also look to the capacity to exert influence and control in the absence of any formal legal entitlement. Thus the expanded definition is as follows.

Beneficial owner refers to the natural person who ultimately owns or controls a customer or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement.[1]

It is completely appreciated that, in a law enforcement context, criminals and terrorists do not typically advertise their involvement in ownership structures where they are liable to be detected by the appropriate agencies. Transporting this definition wholesale, however, into the world of tax information exchange where domestic tax authorities may draw unfair and adverse implications from an attribution of being a 'controlling person' is more questionable. It is not a complete response to this concern to say, in the final analysis, if someone has no ability to enjoy the benefit of assets held within a particular structure that they can demonstrate this – the potential costs and bureaucracy of an unwarranted tax audit that may arise from such a misunderstanding will be more difficult to quantify.

Another area of concern is the capacity for banks who have, in the past, misclassified or misunderstood information about ownership structures. If this information is simply

1 http://www.fatf-gafi.org/pages/glossary/a-c/ – The Recommendations were adopted by FATF on 16 February 2012. (emphasis added).

'copied over' from AML records for CRS purposes then there is scope for false and misleading information to be exchanged in circumstances where the 'beneficial owners' may be completely unaware of such mistakes or misclassifications.

What follows from this is an increased importance for professional advisers to actively engage with clients to discuss the implications of these changes. Taken together, the combined impact of these changes is likely to be seen in years to come as a 'paradigm shift' in international wealth structuring. It is therefore critically important that the advisory community equips itself fully to be able to assist in a pro-active manner.

ii Public registers of beneficial ownership

On 20 May 2015, the EU published the final version of its fourth anti-money laundering directive (4AMLD). This commits the EU Member States to providing a public register of beneficial ownership within the next two years. What is noteworthy about the terms of the regulation is the fundamental distinction that has been drawn between ownership information about 'legal persons' (including companies and foundations) on the one hand, and 'legal arrangements' (including trusts) on the other. There is an obligation for information on legal persons to be placed in the public domain while information relating to trusts and equivalent arrangements will be restricted so that it is only made available to competent authorities.

The acceptance in the drafting of these regulations that there is a legitimate distinction to be drawn between commercial entities that interact with third parties, primarily in the context of business arrangements, and private asset ownership structures that are primarily designed to hold wealth for families is an encouraging one.

It should not, however, be assumed that the emphasis on privacy that underpinned this particular distinction will necessarily be a permanent one. There is a very strong constituency within the EU that still argues that a public register of trusts should be introduced at some stage in the future.

Turning to the UK, 2016 will see the introduction of a public register of beneficial ownership for companies in the UK. This legislation, to a large extent, anticipates the impact of 4AMLD although it is not completely symmetrical. The centrepiece of UK domestic legislation is the public identification of persons with influence over UK companies, known as 'persons exercising significant control' (PSCs). There are significant penalties for non-compliance. In particular, in circumstances where a PSC does not respond to the request for information from a company, not only can that refusal generate potentially criminal sanctions, it can also result in any economic benefits deriving from the shares as well as the ability to vote being suspended.

While it is appreciated that there are reasons why sanctions need to be applied to encourage people to comply, the harsh economic penalties may be seen as totally disproportionate to non-compliance. It is interesting to note that the PSC concept analogous to that of the 'controlling persons' in the context of CRS. As with CRS, the most complex area here is the extent to which those being seen to exert 'influence' without formal legal entitlement may be classified as PSCs.

One further interesting issue that needs to be considered as matters move forward is whether the impact of the EU public register for corporate entities will result in a 'back door' trust register in many cases. One of the categories for disclosure of PSCs in

the UK register is 'ownership or influence via a trust'. In circumstances therefore where a trust holds a material interest in a company, this can result in not only the trustees and protectors of the trust, but also family members with important powers (such as hire and fire powers) being classified as PSCs and having their information placed on a public register. While this register will not give direct information about beneficiaries as such, in many cases it will provide a significant degree of transparency about family involvement. It seems likely that, over time, the EU will also look to 'export' a requirement for beneficial ownership information on public registered companies to be incorporated in many of the international finance centres. While IFCs have indicated that they are sceptical about the adoption of such registers in circumstances where there is not a common standard applied to all jurisdictions, it remains to be seen how long this stance can be maintained once 4AMLD is in full force.

iii Position of the United States

The United States stands out as having secured a position for itself in the context of cross-border disclosure that many feel is hypocritical. Specifically there is a carve out from CRS on the basis that the US has implemented FATCA. The constitutional position in the US where measures of this nature would tend to be introduced at a state rather than federal level also complicates the picture. In the absence of any comprehensive regime to regulate trustee and corporate service providers, the US appears to have achieved a competitive advantage in administering 'offshore' structures because it has exempted itself, in practical terms, from reciprocation on automatic information exchange. This is already leading to many considering the US as an alternative base from which to administer family structures in a more 'private' setting than is possible in IFCs once CRS take effect.

iv Global legal entity identifier system (GLEIs)[2]

A development flowing from the 2008 financial crisis is the introduction of GLEIs. In December 2014 a regulatory oversight committee relating to GLEIs introduced a task force to develop a proposal for collecting GLEIs information on the direct and ultimate parents of legal entities. The policy is to ensure financial intermediaries can track who they are dealing with as counterparties in investment transactions. The underlying policy that drives the creation of the GLEIs is to create transparency in financial markets. In the current phase 1 of the project, the information required to be collected is limited to 'business card information' about the entities concerned and will therefore be limited to a name, address and contact number. However, the 'level 2' data that is likely to be required will extend the reference data to relationships between entities. This could result in beneficial ownership information being required in due course. This proposal is likely to see some development in the course of the next six months but is yet another illustration of overlapping regimes for collecting beneficial ownership information that are likely to have a substantial effect on the operation of family wealth holding structures in the years ahead.

2 http://www.leiroc.org/.

v Conclusion

The challenges of keeping abreast of changes in the regulatory and transparency arena are significant. These issues look set to be a significant driver in wealth strategy in the next three to five years. Navigating these issues will increasingly become a required skill set for professional advisers.

John Riches
RMW Law LLP
London
September 2015

Chapter 38

UKRAINE

Alina Plyushch and Dmytro Riabikin[1]

I INTRODUCTION

The 2013–2014 Dignity Revolution ousted President Viktor Yanukovych and caused the country to choose the path of closer alignment with the European Union. The situation is complicated by the annexation of the Crimea by the Russian Federation and the continuing military standoff with pro-Russian separatist groups that have seized control of parts of the eastern Ukrainian regions of Donetsk and Luhansk. Coupled with the economic crisis, these events have had a substantial negative effect on the Ukrainian economy sending the country into deep recession.

On 27 June 2014 President Petro Poroshenko signed the Association Agreement with the EU. The Association Agreement was simultaneously ratified by the Verkhovna Rada (the parliament of Ukraine) and the European Parliament on 16 September 2014, however, the establishment of the deep and comprehensive free trade area (DCFTA) was moved to 31 December 2015.

Pursuant to the Association Agreement the Government of Ukraine is introducing legislation to harmonise Ukrainian legislation with that of the EU. Implementation of the Association Agreement creates new opportunities both for Ukrainian business in Europe and for the foreign investors in Ukraine.

Another substantial international instrument that influences Ukrainian legislative reforms is the Extended Fund Facility (EFF) between Ukraine and the International Monetary Fund (IMF), approved on 11 March 2015 by the IMF Executive Board, which suspended the previous stand-by arrangement. In accordance with the EFF Ukraine is obliged to implement number of fiscal, economic and legislative measures under the IMF supervision.

1 Alina Plyushch is a counsel and Dmytro Riabikin is an associate at Sayenko Kharenko.

In compliance with the EFF significant amendments were introduced to such areas as banking and energy sector regulation, anti-money laundering, combat against corruption, protection of investors and investments etc. These significant shifts generally correspond to recognised international standards (including those of the IMF, the European Union and the Financial Action Task Force) in said areas, nevertheless the pace of reforms and their practical implementation remain modest.

In recent years Ukrainian businessmen were substantially focused on the effective wealth protection and management mechanisms. Current Ukrainian business environment makes wealth preservation and protection a number one priority.

Ukrainian legislation does not provide for the effective regulatory framework aimed at the preservation and protection of private wealth. Thus wealthy Ukrainian individuals prefer to structure their private capital through cross-border holding and trust structures headquartered outside Ukraine.

The holding structures utilising trusts or foundations proved to be a reliable option to achieve these goals, secure succession and effectively manage created wealth.

II TAX

Taxation of individuals in Ukraine depends on the tax residence status, source and type of income.

i Tax residency

The Tax Code of Ukraine (the Tax Code) provides the following residency test to determine the individual's tax residency: (1) citizenship (all Ukrainian citizens are considered tax residents of Ukraine by default); (2) residence (permanent residence in Ukraine for a period exceeding 183 days); and (3) centre of vital interests (close economic and personal ties).

Registration of an individual as a sole trader in Ukraine is also sufficient to recognise this individual as a Ukrainian tax resident. In addition an individual may voluntarily accept to become a tax resident in Ukraine in accordance with the procedures set out in the Tax Code.

Despite all of the above tests, in practice the main criterion to determine the tax residency regularly applied by the Ukrainian tax authorities is the number of days spent by an individual in Ukraine in a calendar year.

For the purposes of the Tax Code any person who fails to qualify as a Ukrainian tax resident is considered to be a non-resident of Ukraine.

ii Source of income

Tax residents of Ukraine are taxed on their aggregate worldwide income. Non-residents are taxed on Ukrainian-sourced income only. Non-resident individuals are not eligible for certain deductions and exemptions available to residents for personal taxation purposes.

iii Types of taxable personal income

The Tax Code recognises both monetary and non-monetary personal income.

The Tax Code provides for the following taxable types of personal income (irrespective of residency): income from employment, interest and dividend income, gifts, inheritance, investment income, insurance payments, rental income, fringe benefits, amounts of received punitive damages and written off payment obligations to the third parties etc.

In addition the Tax Code specifically excludes certain types of income from the taxable basis of both residents and non-residents. Certain categories of low-income taxpayers are entitled to reduce their respective incomes by an amount of the 'social tax benefit'.

The Tax Code prescribes that if so provided by the respective international tax treaties, amount of taxes paid by a resident taxpayer outside of Ukraine may be used as credits against amount of taxes to be paid in Ukraine, provided that the taxpayer submits a written confirmation from the foreign tax authority acknowledging that such foreign taxes have in fact been paid. However the total amount of such foreign tax credits may not exceed the total amount of the personal income tax (PIT) due in Ukraine.

iv Rates

The Tax Code was significantly amended by the Verkhovna Rada on 28 December 2014 (the majority of such amendments became effective on 1 January 2015) as a part of the tax reforms announced by the government.

Starting from 1 January 2015 both residents and non-residents are taxable at the same tax rates of 15 per cent or 20 per cent which apply to the income from employment and some other related types of income. 15 per cent tax rate applies to monthly income not exceeding 10 minimum wages as of 1 January of the reporting (calendar) year (12,180 hryvnas for 2015). The monthly income exceeding this amount is taxable at the rate of 20 per cent.

The passive income which includes, *inter alia*, interest, investment profit, royalties and some types of dividends is taxed at a fixed rate of 20 per cent. The dividends received by an individual from Ukrainian companies that are subject to the corporate profit tax are taxed at the rate of 5 per cent.

In 2015 certain tax rules regarding royalties were eased. Henceforth residents paying royalties to non-residents may account as expenditure the amount that does not exceed 4 per cent of their net income plus profit from royalties in the calendar year. However, 100 per cent of royalties paid may be accounted as expenditure, if the tax payer may confirm that royalties are paid on the arms length basis. Though applicable accounting standards make it rather complicated to prove that the quantum of royalties is determined on the arms length basis.

Income derived from a disposal of real estate is taxed at the rate of either zero per cent or 5 per cent depending on (1) the type of property, (2) the frequency of disposals, and (3) the duration the title to such property was held by the seller.

v Gift and succession taxes

Gifts and inheritance are taxable income and both are subject to the PIT at the rates of zero per cent, 5 per cent or 15 per cent (20 per cent). The exact applicable rate depends on the residency status of the donator or the testator and on the degree of relation

between the donator or the testator and the recipient or the heir (varying from zero per cent for spouses and children to 20 per cent for inheritance or gifts received from or by non-residents).

Tax residents shall pay income tax on inheritance and gifts irrespective of the location of the acquired assets.

There is no wealth tax in Ukraine, however, amendments to the tax law introducing the wealth tax are currently being considered.

vi Assets tax

The amendments to the Tax Code effective as of 1 January 2015 have introduced consolidated assets tax, which consists of land tax, non-land real estate tax and transport tax. Before these amendments were introduced there were separate taxes on the land and on the residential real estate.

The land tax is payable by individuals holding title to or a right of permanent use of land plots in Ukraine irrespective of their tax residency. Particular land tax rates are determined by the municipal authorities and shall not exceed 12 per cent of the cadastral value of a land plot depending on the type of the land plot and the particular rights of its holder (i.e., either title to, or the right of permanent use). The Tax Code provides for a number of tax exemptions regarding land tax depending, *inter alia*, on the status of an individual, the type of a land plot, its square and purpose of its use.

Residential and non-residential real estate owned by an individual is subject to a non-land real estate tax. The tax rates are set forth by the municipal authorities but shall not exceed 2 per cent of the minimum wages as of 1 January of the reporting (calendar) year per square metre of the real estate owned by an individual. At the same time the Tax Code sets forth certain exemptions for the real estate tax (e.g., the minimum real estate square, which shall not be subject to the real estate tax).

Owners of luxury vehicles registered in Ukraine irrespective of their residency are subject to the transport tax in amount of 25,000 hryvnas per each vehicle with the following qualifications: the vehicle is used by its owner for less than five years, and such vehicle's engine capacity exceeds 3,000 cubic centimetres.

vii Military duty

In view of the current political situation in Ukraine, the Verkhovna Rada has introduced a military duty. In 2015 military duty is levied on the Ukrainian-sourced income of non-residents and on the worldwide income of the tax residents of Ukraine at the rate of 1.5 per cent.

viii Issues relating to cross-border structuring

Ukraine has a wide network of the double taxation treaties with approximately 70 countries. On 15 July 2015 the Verkhovna Rada passed a law ratifying the double taxation treaty with Ireland, which enters into force on 16 August 2015. Meanwhile the double taxation treaties with such countries as Malta and Luxembourg are still pending their ratification. The majority of the double taxation treaties entered into by Ukraine are based on the OECD model convention.

Currently while considering trans-border structuring options Ukrainian private business is focused on such jurisdictions as the Netherlands, Estonia, Hungary, Slovakia and Latvia due to the favourable provisions of the respective double taxation treaties between Ukraine and these countries. While Cyprus remains to be one of the most popular and attractive cross-border structuring option for the majority of Ukrainian businessmen in tax planning and private wealth protection and preservation, the interest in structuring through the Netherlands, Estonia, Hungary, Malta, Luxembourg and other jurisdictions with favourable tax regimes for holding, financial and operational companies will continue to grow for the observable future.

As a part of the tax reform the transfer pricing rules set in the Tax Code were significantly amended (amendments effective as of 1 January 2015), in particular with regard to the list of transactions that are subject to the transfer pricing regulation (the New TP Rules). The New TP Rules are based on the OECD Transfer Pricing Guidelines. These regulations require that prices for goods and services in certain transactions shall be set on an arm's-length basis.

The New TP Rules apply primarily to cross-border transactions with related foreign entities. However, they may also apply to transactions between unrelated parties (e.g., cross-border transactions involving counterparties from certain 'low-tax' jurisdictions). A list of such jurisdictions is established and updated by the government (in 2015 three jurisdictions – Hong Kong, Turkmenistan and Niue – were added to the revised list).

The above transactions are subject to the New TP Rules provided that the following criteria are met: the total taxable income of the respective Ukrainian taxpayer or its related parties exceeds 20 million hryvnas in the relevant calendar year; and the volume of such transactions with any particular counterparty exceeds 1 million hryvnas (exclusive of VAT) or 3 per cent of total taxable income of the respective Ukrainian taxpayer for the relevant calendar year (each such transaction a 'controlled transaction'). Ukrainian taxpayers are required to report all controlled transactions they were party to the tax authorities on an annual basis.

Based on such reporting as well as on their own monitoring and tax audits Ukrainian tax authorities can make transfer pricing adjustments and impose additional tax liabilities in respect to the controlled transaction if the terms and conditions of a particular controlled transaction are not an arm's-length basis.

The arm's-length price in respect of a controlled transaction may be established through application of various methods, including comparable uncontrolled price, resale price, cost plus, net profit and profit distribution methods.

III SUCCESSION

Rules governing succession are incorporated in the Sixth Book (Chapter) of the Civil Code of Ukraine (the Civil Code). Conflict of law issues arising out of and connected with succession are set forth in the Law on Private International Law. Useful guidelines on the application of the succession legislation are outlined in the Letter of the High Special Court of Ukraine on Civil and Criminal Cases on court practice in succession cases dated 16 May 2013.

Following Roman civil law traditions succession in Ukraine is regulated either by way of a testament or pursuant to provisions of the Civil Code (succession by law).

A testator's estate is defined as all the testator's rights and liabilities remaining in force after his or her death.

The death of the testator triggers probation. Within six months after the commencement of the probation the heirs may either execute or renounce their rights to succession.

Transfer of title to heirs is effected on the basis of a certificate of inheritance issued by a notary upon expiration of six months probation period. Issuance of a certificate is mandatory for immoveable property while for moveable property it is optional (though highly recommended).

Under amendments dated 20 October 2014 (to be effective from 1 January 2016) acceptance or renunciation of inheritance may be conducted by the authorised officer of municipal government body and if there are no notaries in such area such officers may issue certificates of inheritance.

Protection of the testator's estate, distribution of his or her shares, execution of the last will is performed by a notary and, when applicable, by an executor of the will appointed by the testator.

i Intestacy rules

Inheritance by law arises if a testator leaves no valid will and testament. Inheritance by law rules will also apply if the testator has left a will but it was successfully challenged by heirs or if inheritance was renounced by heirs.

There are several lines of priority of succession. The testator's estate is distributed among the heirs of each priority line (i.e., the heirs of each priority line exclude the members of the next lines). This order of succession may be changed upon written and notarized agreement between the heirs when such agreement does not infringe rights of the heirs that are not parties thereto.

The principle of representation applies (i.e., in case of the death of an heir of the first priority line (e.g., the testator's son) his or her heirs will have the right to their share of the inheritance).

The Civil Code intestacy rules provide that only individuals may inherit by law. The right to succession may be executed by an heir upon provision of evidence of his or her relations with the testator (e.g., birth or marriage certificate). The heirs of the same priority line inherit the testator's estate in equal shares; however, they may enter into a separate agreement and decide upon distribution of the testator's estate among them. Under the Civil Code there are following priority lines:

First priority	Testator's children (born both in and out of marriage), spouse and parents
Second priority	Testator's brothers and sisters and both paternal and maternal grandparents
Third priority	Testator's aunt and uncle
Fourth priority	Individuals who lived as a part of testator's family for at least five years before his or her death
Fifth priority	Other relatives of the testator up to the sixth degree of kinship

ii Inheritance by will

The Civil Code sets out strict requirements to the form of the will. It shall be made by a testator in writing with a statement of the date and place of notarisation. The testator may define as the heirs either individuals or legal persons. Only adult persons of full legal capacity may execute a will (they must be 18 years old (or in certain cases 16) or over and with full mental capacity).

A testator may set out in a will any additional bequests in favour of any designated person (e.g., right to abide in the inherited real property). The testator may also determine certain preconditions or conditions for his or her heirs to satisfy in order to receive the right to inheritance (e.g., residence in certain place, certain age etc.). However, such preconditions must not contradict the law or principles of public morality.

A document executed in breach of will execution rules set out in the Civil Code or by a person lacking full legal capacity is deemed void *ab initio*.

A will is deemed void when there is evidence that the testator has executed the purported will either by coercion or as a result of fraud. Upon claim of the interested person such will may be declared void by the judgement of the court.

Spouses may draft a combined will. Apart from the will a testator may also enter into a succession agreement under which acquirer obliges to undertake certain actions prescribed by alienator (testator) in return for ownership rights to the testator's estate.

iii Mandatory inheritance

Testator's right to choose heirs is limited by provisions of Section 1241 of the Civil Code, which guarantees that underage or disabled children, spouses and parents shall in any case inherit at least half of the portion they would have received in the absence of the last will. Under Ukrainian law the definition of a 'disabled person' covers both persons with disabilities and retired persons.

iv Conflict of law issues

As a general rule succession is governed by the law of the country of the last residence of the testator (i.e., if a citizen of Romania resides and dies in Ukraine the applicable law is that of Ukraine). However, if a testator executes a will he or she can choose his *lex patriae* (e.g., in the case of a Hungarian testator – the law of Hungary).

There are, however, certain overriding provisions of *lex specialis*. The form of the act shall correspond to the requirements of the law of a place (country) of the testator's death. However, the will may not be declared void on the basis of error in form if it corresponds to the law of the country where the testator's immoveable property is situated, the *lex patriae*, the law of the country of the last residence or the law of the country where the will was executed, whichever is applicable.

Transfer of title to immoveable property shall be governed by the law of the state where such immoveable property is situated.

v Matrimonial rules

In 2014–2015 no amendments were made to the Family Code of Ukraine (the Family Code), the act governing matrimonial relations in Ukraine. Same-sex marriages are not

recognised by the Family Code and their official recognition is unlikely in Ukraine in the foreseeable future.

The Family Code provides for tenancy-in-common of the spouses' property with certain exclusions (e.g., personal belongings, property acquired before the marriage, etc.). This regime can be changed by way of a prenuptial agreement. Prenuptial, maintenance and alimony agreements shall be executed in writing and notarised. However, there is no developed case law in Ukraine regarding such agreements. Difficulties may arise in the case of foreign spouses and with conflict of law issues.

IV WEALTH STRUCTURING AND REGULATION

i General overview of private wealth regulation

None of the forms of legal entities provided by Ukrainian corporate legislation may be viewed as specifically designed for private wealth management purposes. The trusts and foundations are generally not recognised in Ukraine, though their definitions sometimes appear in the new legislation.

2014–2015 was marked by significant developments in the legislation aimed at combating money laundering and establishing economic and financial transparency (e.g., in 2014 the definitions of the 'beneficial owner' and the 'politically exposed person' were adopted as described below). Substantial changes were introduced to the regulatory regime of the banking sector.

ii Beneficial owners' disclosure requirements

Following FATF Recommendations 24 and 25 in late October 2014 the Verkhovna Rada introduced new requirements to the disclosure of the ultimate beneficial owners (UBO) of Ukrainian legal entities.

The Law on Amendments to Certain Laws of Ukraine on Establishing Ultimate Beneficial Owners of Legal Entities and Political Exposed Persons provides that all legal entities in Ukraine shall file with the State Registry of Legal Entities and Private Entrepreneurs of Ukraine (the State Registry) information on their: ownership structure; and the UBO by 25 May 2015 (further prolonged to 25 September 2015). The filing requirements do not cover legal entities whose members are exclusively individuals.

Upon filing with the State Registry, the UBOs' personal data (including full name and place of residence) is publicly available on the webpage of the State Registry.

The definition of the UBO included into the AML Law (as defined below) covers both shareholding and dominant control tests endorsed by the FATF in the 2014's Guidance on Transparency and Beneficial Ownership. Moreover, nominee shareholders may not be registered as the UBOs of Ukrainian legal entities.

Failure to file information on the UBO will lead to fines imposed on the management of Ukrainian legal entities (up to 8,500 hryvnas).

iii New requirements of the National Bank of Ukraine

In 2014–2015 the National Bank of Ukraine (NBU) under the IMF supervision substantially amended legislative requirements to Ukrainian banks' owners and ownership structures, which aim to secure transparency and financial stability. New

provisions primarily amended procedures for obtaining the NBU's approval for acquiring significant interest in Ukrainian banks. Thresholds for 'significant interest' are set at 10 per cent, 25 per cent, 50 per cent and 75 per cent and the NBU's approval is required when either of these thresholds is reached.

By Regulation No. 328 the NBU introduced the definition of 'trust' (discretionary trust) and prescribed that any bank ownership structure that includes discretionary trust arrangements is viewed by the NBU as non-transparent (as it restricts the NBU's ability to establish the ultimate owner of the bank). If the bank's structure is considered 'non-transparent' it may lead to materially adverse consequences (e.g., the NBU may refuse to grant a refinancing loan or otherwise restrict such bank's operations). Furthermore business reputation of the managers of such bank may be seriously affected. In the worst-case scenario the NBU may designate such bank as a 'problematic' one.

The NBU enhanced requirements to financial standing of the UBOs. Under the new rules the UBO's income should be sufficient to ensure further capitalisation of the bank. In setting out the UBO income sufficiency test the NBU linked the UBO's income to the bank's regulatory capital or its share capital if it exceeds the regulatory capital.

If a bank's shareholding structure does not reveal a clear link with a particular UBO, the NBU will most likely suspect that such bank has nominee shareholders acting in the interests of a real UBO. In such case, the NBU will be able:

a to apply the so-called 'informal ownership concept' in case the lack of information on the formal ownership in a bank. As a result the NBU will be entitled to recognise a person having a significant or decisive influence over the bank's management and activity as an owner of a significant interest in such bank. To the moment the NBU has already tested the informal ownership concept on several occasions. In particular the NBU identified and imposed sanctions on several informal owners of a significant interest in Ukrainian banks. Furthermore, the NBU is planning to dramatically increase fines applicable to informal owners of a significant interest in a banks, who did not obtain the respective NBU approval; or

b to check the financial standing of 10 largest 'ultimate key stakeholders' – persons holding at least a 2 per cent shareholding in a legal entity in the bank's ownership chain and that do not themselves have key stakeholders (e.g., individuals or foreign public listed companies). If at least two ultimate key stakeholders holding more than a 5 per cent shareholding in a bank or one person holding ultimately at least a 10 per cent stake fail to prove sufficient financial standing the NBU may designate the ownership structure of a bank as 'non-transparent'.

The formula for calculation of indirect ownership in a bank should provide the NBU with additional instruments for identifying indirect owners of a significant interest in a bank. The NBU will use the formula in addition to the criterion of control.

The NBU appreciated the fact that some private investment vehicles, such as limited partnerships, may find it difficult (if possible at all) to provide all documents and comply with formal requirements commonly applied by the NBU to the acquirers of a significant interest in a Ukrainian bank. Therefore if private investment vehicles meet the criteria envisaged by the NBU's regulations the NBU may exempt such vehicles from the obligation to comply with all formal requirements.

iv Anti-money laundering regime

On 14 October 2014 the Ukrainian parliament adopted the Law on Prevention and Counteraction to Legalisation (Money Laundering) of the Proceeds from Crime or Terrorism Financing, as well as Financing of the Proliferation of Weapons of Mass Destruction (the AML Law), which is the primary legislative act in the sphere of anti-money laundering in Ukraine. Another key legislative act in this sphere is the Criminal Code of Ukraine (the Criminal Code).

In line with the EFF the AML Law is aimed at compliance with the principal FATF recommendations (including Forty Recommendations) on combating money laundering and terrorist financing.

Ukrainian anti-money laundering regime includes a two-level strict monitoring system over the financial operations performed by residents and non-residents of Ukraine. Initial financial monitoring (identification of a client, details of and grounds for particular financial operation, etc.) of financial operations is conducted by intermediaries including: banks, insurance (and reinsurance) companies, other financial institutions, stock and commodities exchanges, professional members of the security market (e.g., brokers, dealers), notaries, auditors and individuals rendering accounting services, attorneys at law and other persons providing legal services, etc (the initial financial monitoring performers).

The AML Law introduced numerous amendments to the previous anti-money laundering regime and, *inter alia*:

a provides for outsourcing of client identification or verification to a third party;

b authorises the initial financial monitoring performers to require a client to provide its ownership structure in order to enable them to determine beneficial owners of the client;

c introduces financial monitoring with respect to national or foreign politically exposed persons and officials of international organizations, establishes a high level risk for operations involving (or carried out in the interests of) politically exposed persons or officials of international organisations and provides for additional measures of financial monitoring for clients with a high level of risk; and

d clarifies the legal basis for termination of relationships with a client by the initial financial monitoring performers in case the identification or verification of a client is not possible.

The AML Law also provides for the formation of a national analytical database that may be used by the law enforcement agencies of Ukraine and other countries for the purposes of identification, examination and investigation of crimes related to money laundering and other illegal financial transactions.

Ukrainian anti-money laundering legislation establishes a system of the state bodies supervising observance of the financial monitoring requirements by the initial financial monitoring performers. The major authority vested with the general supervision of the financial monitoring system function is the State Service for Financial Monitoring of Ukraine (the Service). The Service *inter alia* adopts standards and recommendations as to the conduct of financial monitoring and keeps updated the list of persons connected with terrorist activities and targets of international sanctions.

The Criminal Code provides for a criminal liability for laundering of the proceeds of a crime. This leads to an imprisonment of up to 15 years combined with confiscation of the proceeds of a crime and property of the liable person as well as deprivation of the right to perform certain activities or hold certain positions for up to three years.

V CONCLUSIONS AND OUTLOOK

Ukrainian legislation is going through a reform period with the aim of becoming compliant with international and EU standards. Substantial changes are already visible though the climate for private wealth management and protection in Ukraine is still not friendly enough.

There is a growing need to introduce these structures at the owners' level. The age of the first generation of Ukrainian businessmen is also pushing them to look into restructuring of their businesses in order to secure the interests of their children for years to come.

A reliable and effective solution to achieve these goals is the creation of a cross-border structure with a trust or foundation on the top. Such structuring provides for a transparent and reliable ownership and control system for the business, helps to protect the interests of the beneficiaries, and facilitates optimisation of the group taxation. However, Ukrainian legislation now emphasises transparency as a major requirement for all such structures and it is always important to consider that the UBOs of such structures shall be disclosed to Ukrainian authorities and that such information will be publicly available.

The Ukrainian tax system is still evolving and developing rapidly. In times of political and financial hardships the government views taxes as a primary source for budget income. This is confirmed by the new taxes introduced in 2014–2015 and the increase in tax rates. On the other hand, in course of the general fight against cronyism and corruption, the government aims to reform Ukrainian tax authorities and find solutions favourable both to business (e.g., the tax amnesty proposal in 2014) and to the state budget. From the cross-border perspective important regulations to look at are the transfer-pricing rules. One should also consider the wide network of Ukrainian double taxation treaties.

Ukrainian law covers the main aspects of succession and matrimonial relations and provides for the possibility to enter into agreements in order to structure such relations and define specific regulation for specific cases. Protection of a testator's estate is vested in notaries securing it from bad faith heirs. Adopted mainly at the beginning of the 2000s, succession and matrimonial legislation has not seen major changes in the recent years. No further updates or amendments have been announced by the new Ukrainian government at this stage.

The new AML Law and the Criminal Code serve as the main sources of the Ukrainian anti-money laundering regime. In particular, the AML Law outlined the financial monitoring procedures in more detail. In line with that the state anti-money laundering compliance supervision authorities have adopted regulations, implementing

fines for non-compliance with the legislative requirements. This is aimed to ensure effective risk assessment and control to be performed by the initial financial monitoring performers and stricter KYC demands. Persons willing to acquire Ukrainian banks will henceforth face stricter compliance requirements. These changes generally correspond to FATF standards (Ukraine is an observer of the FATF).

Appendix 1

ABOUT THE AUTHORS

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Alina Plyushch is a counsel with Sayenko Kharenko specialising in corporate law, M&A, corporate finance, capital markets and private wealth management.

Alina has over 15 years of professional experience in advising clients on corporate restructuring, share and asset sales, joint ventures, private placement and capital markets transactions.

Ms Plyushch is one of the leading specialists in Ukraine in the private wealth management area and has extensive experience in advising on protection of the beneficial owners' interests both in Ukraine and abroad, including corporate restructurings, incorporation of trusts, foundations and segregated portfolio companies.

Alina Plyushch is listed among world's best Private Client lawyers by the independent review *Who's Who Legal: Private Client 2015*.

Alina earned her graduate diploma in law and postgraduate diploma in legal practice from BPP University Law School (London) and law degree *summa cum laude* from the Academy of Advocacy of Ukraine.

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Dmytro Riabikin is an associate at Sayenko Kharenko specialising in private wealth management, M&A, corporate law and securities market.

Dmytro has a six years' experience of advising clients on various private wealth management issues, including protection of interests of the beneficial owners of Ukrainian and foreign businesses by means of corporate restructurings and setting up trusts.

Dmytro earned his master degree *summa cum laude* in private international law from the Institute of International Relations of Taras Shevchenko National University of Kiev. Currently Dmytro is a postgraduate student of the Department of Private

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