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PREFACE

Dear Friends,

We are all nearing the end of a turbulent period, and hope that with appropriate measures we can pick-up our normal life again. Together, as a family, we have managed to continue our dedicated services and supported our business partners with their sustainable growth in Turkey as well in the countries where we are currently present.

Our mission is to proceed with devoted work and provide comfort in the peace of minds of our business partners when they intend to grow outside their own country. In line with the aforesaid, we aim to also open our offices in New York as well in Johannesburg by the end of this year.

With our trusted name NAZALI® and our dedicated professionals, we remain ascertaining the sustainable growth of the business activities of our business partners outside their homeland as a one-stop-shop service provider.

After the successful release of the first edition of NAZALI® GLOBAL MAGAZINE and positive feedback from our business partners as well our peers in the market, we decided also to release the second edition of NAZALI® GLOBAL MAGAZINE as well.

In this edition we also would like to take the opportunity to introduce our UK office to you as well, under the outspoken leadership of Mr. Ersin Nazali.

Like the first edition, the second edition of NAZALI® GLOBAL MAGAZINE consists of interesting articles per jurisdiction with a primary focus on legal and tax topics.

We hope again for an enjoyable reading and look forward to your feedback and/or questions.

Looking forward to meet you again in our next edition of NAZALI® GLOBAL MAGAZINE

Sincerely regards,
NAZALI GLOBAL

UNITED KINGDOM

ABOUT NAZALI UNITED KINGDOM

Our London office started providing their professional services in June 2019 with a group of qualified and experienced individuals offering broad knowledge and services on Accounting, Tax and Legal, Compliance and Corporate Governance for clients locally and internationally.

NAZALI UK is headed by the Managing Partner of the company Mr Ersin Nazali. He has a wide range of knowledge in several tax areas such as international tax, tax inspections, tax litigation, transfer pricing and tax free re-structing of companies.

Please feel free to contact Mr. Ersin Nazalı, through:

Ersin NAZALI

Ersin Nazalı, co-founder and managing partner of NAZALI, is a tax expert and has considerable knowledge in several tax and corporate law areas, especially tax-customs disputes, customs litigation, transfer pricing, tax inspections and restructuring of multinationals. Ersin Nazalı has been listed as a leading tax advisor and attorney in Turkey by Legal 500 (2013, 2014 and 2015) and International Tax Review (2014, 2015 and 2016). Ersin Nazalı has published more than 80 articles in several tax journals and 5 books (Taxation of Merger-Acquisition and Spin off, International Taxation, Permanent Establishment, Transfer Pricing, Tax-Civil-Criminal Liabilities of Company Directors).

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CURRENT NEWS ABOUT UNITED KINGDOM

» Corporation tax rate in the UK:

Corporation tax rate for small profit 19% (profit up to 50k) it will taper, 25% in 2023. In order to support the recovery, the increase will not take effect until 2023. Businesses with profits of £50,000 or less, will continue to be taxed at 19% and taper above £50,000 will be introduced so that only businesses with profits greater than £250,000 will be taxed at the full 25% rate.

» Extension of loss carried back:

The UK Government proposes to introduce legislation in Finance Bill 2021 to provide a temporary extension to the loss carry back rules for trading losses of both corporate and unincorporated businesses (for accounting periods ending between 1 April 2020 and 31 March 2022). This temporary extension of trading loss c/b from one year to three years, to further support the cashflow of businesses, the government is extending the loss carry back against trading income subject to a cap of £2m.

» Capital Allowance Super-deduction:

In the UK, Finance bill 2021 government introduce super-deduction on capital allowance, which essentially is a state subsidy for the private sector investment in plant and machinery, an enhanced temporary 130% first-year allowance for main rate assets, and a 50% first-year allowance for special rate assets. An investment-led recovery beginning April 2021, the new super-deduction will cut companies' tax bill by 0.25p for every pound they invest in new equipment. This is worth around £25 billion to UK companies over the two-year period the super-deduction will be in full effect.

» Capital Gains Tax return and payment:

From 6 April 2020, anyone making a taxable gain from selling a UK residential property must submit a residential property capital gains return within the 30-day window from the date of completion and pay any CGT owed. For the non-UK resident persons, NRCGT will apply as of 6 April 2015 due to any disposal of residential property in the UK. There will require a rebasing of residential property on 5 April 2015.

» UK property held by non-UK resident's company:

Changes from 6 April 2020, non-UK resident companies that carry on a UK property rental business or have other UK property income will be liable to corporation tax instead of income tax.

Changes from 6 April 2019, UK property gains released by non-UK resident companies are subject to corporation tax instead of CGT. Non-resident companies no longer be required to complete NRCGT returns, as they are not required under Corporation Tax. The normal Corporation Tax filing and quarterly payment rules apply. However, by concession where there are 4 or more disposals, HMRC accept a 12-month accounting period.

» VAT rates reduce for hospitality business:

UK government will not increase VAT rate on finance bill 2021. For hospitality business reduce VAT rate 5% will be continued until the end of September 2021. New interim rate of 12.5% will apply a further six months until 31 March 2022.

» VAT Reverse Charge for Construction Industry:

VAT reverse charges for building and construction services come into force on 1 March 2021 (it has been delayed, it was due to be applied from the 1st of October 2020), in order to tackle fraud in the construction industry. The reverse charge will apply to individuals or businesses registered for VAT in the UK, this means the customer receiving the service will now be liable to account for VAT and must pay the VAT due to HMRC instead of paying the supplier. The VAT cash amount will no longer flow between businesses and will have to be registered and the invoice must state the reverse charge applied.

WHOLLY AND EXCLUSIVELY DEDUCTIBLE EXPENSES FOR A LIMITED COMPANY

Miss Gizem Dogan
Accounts & Tax Assistant

ABSTRACT

In this article, there will be information on many reasons and benefits on why investors should invest in the UK and why it will benefit their businesses.

Key Words: Expenses, Limited Company, Investors, UK, Deductible, Benefits.

INTRODUCTION

There are several allowable expenses that do not need to be questioned if it is related to business and this expenditure are wholly and exclusively related to business. These are rent, accountancy fees, advertising and PR, software costs, directors' salaries, employer's national insurance (NI), purchase of equipments, pensions, postage, stationery and printing expenses, interest on business loans, telephone and internet expenses as well as wages and salaries. Expenses for the above mentioned and any other expenses will be eligible for tax relief if they are wholly and exclusively for the purpose of running the business. On the other hand, there are a few expenses that are not so straight forward. These are explained in the following part of this article.

1. ENTERTAINMENT AND GIFT[1]

The general rule is that expenditure on entertainment and gifts is not deductible. There is no deduction for UK and overseas customers entertaining for income tax and corporation tax purposes. Entertaining for and gift to employee are normally deductible. Gift to customers that are not costing more than £50 per person yearly are allowable if it carries conspicuous advertisement for the business and are not food, drink, tobacco or vouchers exchangeable for goods. Gift to charities may also be deductible if wholly and exclusively for the business. Entertainment expenses are a mixture of allowable and non-allowable costs. Staff entertainment[2] is an eligible business expense which is limited to yearly £150 per staff. The staff should be on the payroll to claim for tax relief. On the other hand, ex-employees or subcontractors invited for the entertainment are excluded and their share of the staff entertainment expenses is not deductible.

2. CAPITAL EXPENDITURE

In principle capital expenditures are not deductible, which also applies for its depreciation and amortization as well. However, there are several expenses within a company that can claim capital allowance to reduce the corporation tax bill. The most common types are plants and machinery used in the office to carry out business activities properly These can be claimed through capital allowance, whereas in the first year 100% can be claimed under the Annual Investment Allowance (AIA). The government is currently allowing expenses up to £1m.

The capital allowance main rate is 18% and in certain circumstances a special rate is 6% is applicable.

3. STAFF TRAINING AND WELFARE EXPENSES[3]

Staff training and welfare expenses also have their exemptions. New staff training and new skill courses will not be classified as a deductible expense, as it is not considered as helping the company to develop. However, if the staff decides to take on a course to widen their knowledge to add value for business growth and which would benefit the business, then this would be deemed as a deductible expense[4]. Expenses for training would need to be a necessary knowledge for the purpose of the business, which is also known as the Continuing Professional Development (CPD).

4. MOTOR AND TRAVEL EXPENSES[5]

Motor expenses also has expenses where some elements are deductible, and some are not. For example, if a car is purchased under the business name and is exclusively used for business purposes this will mean that motor expenses such as fuel, car insurance and parking fees will be allowable and deductible as a capital allowance. On the other hand, if the car is owned by the company director and is used for business purposes then the mileage allowance can be claimed up to 45p per mile within the first 10,000 business miles and 25p per mile over 10,000 miles[6]. The expenses for motor will need to be divided in this case. Another expense that employers cannot claim for will be parking fines and travelling between home and work. Travel expenses such as train, bus and taxi fares, hotel rooms and meals for business trips are deemed as a deductible expense. All expenses during a business trip/meeting will be eligible for a claim.

5. LEGAL AND PROFESSIONAL EXPENSES

Legal and professional expenses relating to capital or non-trade items, which are not deductible. These include expenses incurred in acquiring new capital assets or legal rights, share issue costs or expenses for drawing-up partnership agreement.

Legal and professional expenses directly related to trading activities are deductible. These are defending or protecting title of fixed assets, renewal of short lease, which is less than 50 years, debt collection cost and accountancy fees.

6. PARKING FINES

For the company tax purposes, parking fines are allowable expenses for employees using their employer's car or business vehicle on business trips however parking fines are not allowable if it is for the Director or proprietor.

7. WEBSITE COST[7]

The treatment of website expenses depends on the function that the website performs. If the function is solely to advertise or promote the business, then the website cost can be treated as deductible expenses. On the other hand, if the website enables sales to be generated or payments received then the website cost is capital expenditure and not deductible from trading profit[8]. However, this capital expenditure will qualify for capital allowances at main rate 18%.

CONCLUSION

The UK benefits such as deductible expenses enable businesses/limited companies to have relief on necessary payments they make for their business. Having benefits as such, gives businesses the flexibility to claim back and pay less tax which would increase their profit.

1 *https://perrysaccountants.co.uk/news/is-client-entertainment-tax-deductible*

2 *https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_date/file/967202/super_deduction_factsheet.pdf*

3 *https://wmtllp.com/2017/08/staff-welfare/*

4 *https://www.gov.uk/expenses-and-benefits-training-payments/what-to-report-and-pay*

5 *https://www.gov.uk/expenses-if-youre-self-employed/travel*

6 *https://www.gov.uk/simpler-income-tax-simplified-expenses/vehicles-*

7 *ATT – Corporation textbook-BPP learning media*

8 *ACCA-P6 Study Text-2016-BPP learning media*

BUSINESS ASSET DISPOSAL RELIEF AND INVESTORS RELIEF IN THE UNITED KINGDOM

Mr. Oliur Rahman
Director

ABSTRACT

UK government is always encouraging entrepreneurs and investors within the UK tax systems. Business Assets Disposal Relief and the Investor Relief is one of the attractive reliefs in the UK.

Key Words: UK, Tax Relief, Business Asset, Material Disposal, Investor Relief, Shared Rights, Conditions, Associate Disposal, Anti-Avoidance Relief.

INTRODUCTION

This article explains how Business Assets Disposal Relief apply and which disposal of business assets will qualify for the relief. Also, it explains when the Investor Relief applies.

1. BUSINESS ASSETS DISPOSAL RELIEF[1]

Business Assets Disposal Relief is a Capital Gain Tax (CGT) relief. Before 2020/21 the relief was known as Entrepreneurs Relief (ER). The relief is applicable when there is:

- a material disposal of business or business assets, which means the whole or part of a sole trader or partnership business.
- a company's director or employee selling shares or securities in their personal trading company.
- a disposal of asset used in a business at the time the business ceased, this asset must be sold within 3 years of the cessation; or
- an associate disposal with a material disposal.

Generally, Business Assets Disposal Relief is available to sole traders and partners selling the whole or part of their businesses[2].

Company directors and employees who dispose of their shares or securities in their personal trading company where they work as well as company directors and employees who acquired share under the Enterprise Management Incentive (EMI) shares the option scheme (EMI option holders do not need to satisfy 5% condition).

1.1.THE RELIEF

Business Assets Disposal Relief reduces the rate of CGT on qualifying assets to 10% regardless of taxpayer marginal rate.

Capital gains are eligible for relief up to £1 million per individual, this is a maximum lifetime relief. (Before the 11th of March 2020, the lifetime limit was £10 million). If anyone previously claimed their right of the relief based on the accumulated total gain of £1 million or more, then this individual cannot claim any further relief.

1.2. THE CONDITIONS

a. a material disposal of business or business assets.

b. a disposal of asset used in a business at the time the business ceased, must be sold within 3 years of the cessation.

c. a taxpayer must hold shares of at least 2 years prior to the disposal. (If the share transaction takes place as a company buyback of shares, Business Assets Disposal relief may be applicable. But qualifying shares will need to be held for at least five years and there are other qualifications to satisfy when considering a company buyback of shares.)

d. a taxpayer must work for the company (full-time or part-time employee or director)

e. a disposal of share or security in a personal trading company (or holding company of a trading group). Trading company is a company carrying on trading activities, where non-trading activity must not be substantial that is more than 20% in relation to the turnover, the assets, and the proportion of time/ expenses.

A company is an individual's 'personal company' if the 5% test is satisfied in combination with test 2 or test 3.

1.3. SHARE RIGHTS[3]

Test-1: At least 5% of the ordinary share capital of the company is held by the individual,

At least 5% of the voting rights in the company are exercisable by the individual

and

1.4. ECONOMIC BENEFICIAL RIGHTS[4]

Test-2: The individual will either have a right to 5% of the company's distributable profits and 5% of the assets available to equity holders on a winding up.

OR

Test-3: The individual would be entitled to at least 5% of the proceeds of a disposal of whole of the ordinary share capital of the company been sold on the day of the disposal (a hypothetical sale of all the company's ordinary share capital i.e., a sale of the business on that day).

2. ASSOCIATED DISPOSAL AND CONDITIONS[5]

Associated disposal also qualifies for Business Asset Disposal Relief where:

1. a taxpayer makes a material disposal of a business or share/securities in a company.
2. as part of the withdrawal from the business, an individual makes a disposal of a assets which had been used in that business.
3. the assets had been used in that business for at least 2 years and owned by the individual for 3 years prior to the disposal.
4. the disposal of at least 5% shareholding in a company or a 5% share in the partnership. It may be less than 5% interest where the disposal is of the whole of the individual's partnership interest, but individual must own 5% or more for 3 years of the 8 years prior to the disposal.

Associated disposal does not apply for sole traders. Also, Business Assets Disposal Relief on an associated disposal is restricted if the asset had **not been used** in the business through its period of ownership or **non-business use** or **rent charges** for use of assets. If there is no rent charged, then full relief is available. If the full rent is charged, then no relief is available. If the rent charged is below commercial rate, then some relief will be available. (Rent restriction only applies for period after 5 April 2008)[6].

Disposal of a single asset used in a business does not qualify for Business Assets Disposal Relief. It does not apply to the disposal of investment or non-business assets. Also, it does not apply to any disposals by companies.

1 https://www,gov.uk/business-asset-disposal-relief
2 https://www.gov.uk/government/publications/investors-relief-2020-hs308/hs308-investors-relief-2020
3 Entrepreneurs' relief – 02 May 2019. https://www.bdo.co.uk/en-gb/insights/tax/private-client/entreprenursrelief
4 Entrepreneurs' relief – 02 May 2019. https://www.bdo.co.uk/en-gb/insights/tax/private-client/entreprenursrelief
5 Tolley – CTA – Advance technical individuals – capital gain tax – FA2020
6 Entrepreneurs' relief – 02 May 2019. https://www.bdo.co.uk/en-gb/insights/tax/private-client/entreprenurs-relief

2.1. CLAIMING THE RELIEF

Business Assets Disposal Relief needs to be claimed and reported to HMRC on the personal self-assessment tax return for the year in which the gain arises. It must be claimed on or before the 1st anniversary of 31 January following the tax year of the qualifying disposal.

3. INVESTOR'S RELIEF[7]

Investor Relief will apply where an individual makes a disposal of qualifying shares in a trading company (or holding company of a trading group), If the claim for relief is made, the gain will be taxed at 10% (TCGA1992, S.169). The gain qualifying for relief is subject to lifetime limit of £10 million per individual.

3.1. CONDITIONS

1. Shares must be issued on or after 17 March 2016.
2. Shares must be a trading company (or holding company of a trading group).
3. Must be an unlisted company when they are issued.
4. The individual cannot be a relevant employee or director (relief available if become unremunerated director following the purchase and employee 180 days after the share issue).
5. Shares must be held continuously for at least 3 years.

3.2. CLAIMING THE RELIEF.

Must be claimed and reported to HMRC on the personal self-assessment tax return for the year in which the gain arises. It must be claimed on or before the 1st anniversary of 31 January following the tax year of the qualifying disposal.

3.3. ANTI-AVOIDANCE RULE

Close company director/shareholder can manipulate how they extract value from company. So, HMRC may apply the Transactions in Securities and Targeted Anti-Avoidance Rule (TAAR) to counteract an income tax advantage for a shareholder/director in certain circumstances & 'phoenixing' arrangement.

CONCLUSION

Business Asset Disposal Relief and Investors Relief is a final reward for entrepreneur and investors who will be doing business and invest in the UK.

7 *https://www.gov.uk/government/publications/investors-relief-2020-hs308/hs308-investors-relief-2020*

NETHERLANDS

ABOUT NAZALI NETHERLANDS

As part of NAZALI, our Amsterdam office has become active in the Netherlands since October 2020.

With its professional team, NAZALI Netherlands (through its Amsterdam office) offers a comprehensive blend of services in the field of, amongst others: Tax, Legal, Accounting, Compliance, Corporate Governance, Customs and Immigration.

The Dutch team exists of professionals having the right knowledge and experience in their field of scope, knowing the Dutch legislation as well its applicability in the daily business activities. This assures the client always being compliant with the legislation, but secures the client also being pre-informed on developments in the Netherlands.

NAZALI Netherlands is committed to provide services through its professionals from different disciplines and in close collaboration with NAZALI professionals in other jurisdictions. As one devoted team, under one roof, to maximise the exploitation of opportunities and chances for its Clients. This sets NAZALI apart from all other service providers.

NAZALI Netherlands is headed by Mr. Talip Sığırcıkoğlu as Partner and Managing Director. He gained broad experience in legal and finance services, but also has strong developed skills in the field of coordinating processes, management, coaching as well in business development. Talip Sığırcıkoğlu is specialized in guiding foreign companies who want to establish in the Netherlands and safeguards their legal goodstanding.

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CURRENT NEWS ABOUT NETHERLANDS

- As of July 1, 2021, the VAT rules for e-commerce will change. Much more often, entrepreneurs will owe VAT in the country where the private customer (B2C) is located. Significant changes are also on the horizon for digital platforms.
- Booking.com is suspected of tax fraud in Italy. The company allegedly failed to remit €153 million in VAT between 2013 and 2019. This stems from that the company abused VAT regulations. The result was that no VAT was paid at all, neither in Italy nor in the Netherlands, where its headquarters are located.
- The Netherlands still does not have its anti-money laundering legislation in order. The European Commission wants the government to apply the new EU rules in national legislation within two months, otherwise it will consider going to the European courts.
- Russia has unilaterally terminated the tax treaty with the Netherlands. That is what outgoing State Secretary Hans Vijlbrief reported. Russia has put a demand on the table that the Netherlands finds "unacceptable". There was no room for negotiations, according to Vijlbrief. He does want to continue talks with the country.
- In the Netherlands, the first opening of the Stimulation Scheme for Sustainable Energy Production and Climate Transition (SDE++) took place in November of 2020. Nearly 3,500 sustainable projects will receive a subsidy of up to € 4.6 billion from the SDE++ 2020.
- The Dutch government stimulates innovation by lowering the threshold for companies to invest in research and development through the WSBO arrangement. In 2020, approx. 20,000 Dutch companies made use of the WBSO arrangement for more than 135,000 R&D projects for a total amount of 1.2 billion euros. The Netherlands has made a one-off extra 157 million euros available for the WBSO for 2021.
- The Dutch cabinet is starting a pilot in the form of a residence arrangement that will make it easier for innovative start-ups to recruit top talents from abroad. This new pilot has started on 1 June 2021.
- The Netherlands is building a House of Quantum on the TU Delft campus. The House of Quantum will be the national headquarters of this quantum campus and will be further developed in close cooperation with the ASR Dutch Science Park Fund, which invests in commercially exploitable real estate located in Dutch science parks. Construction of the House of Quantum will be completed in 2024.
- Neste invests 190 million euros in the Netherlands to produce sustainable aviation fuel. The renewable products refinery in Rotterdam will be able to produce 500 kilotons of SAF per year.
- Singapore-based firm Legend Logistics Group establishes its first European Office in the Netherlands because the Netherlands is an important logistics hotspot in Europe, and has a high concentration of logistics service providers, offering excellent and efficient and access to markets. Legend Netherlands provides comprehensive logistics solutions for bulk liquid products tailored to its customers' requirements and specifications.
- The classification tax rules for the Dutch new entity as per 1/1/2022, the rules include the withdrawal of the 'unanimous consent requirement' for tax-transparency classification of Dutch CV and foreign limited partnerships, classifying these entities as tax-transparent by default. Dutch FGR's (Fund for Joint Account/Fondsen voor Gemene Rekening) in principle also become tax transparent, with an option of electing for a non-transparent tax status in certain situations. The rules were announced by the Dutch Ministry of Finance on 29 March 2021 aligning the rules with global standards.
- According to the Dutch (junior) finance minister Hans Vijlbrief, the G7's new proposals are in line with many Netherland tax measures. The aims are to reduce the incentives for large companies to move their profits to tax havens and ensure they pay more tax, also to back a minimum global corporate tax rate of at least 15%. The Netherlands cabinet has made major changes in eliminating tax evasion, and points to new rules covering interest and royalties and more changes that are being made in 2024.
- The EORI number (Economic Operators Registration and Identification) represents a unique code that is associated with each economic operator. This number is required for all Dutch companies that are involved in trading activities at the level of the European Union (EU). The term economic operator, as it is called under the EORI number application form, refers to both natural persons and legal entities involved in trading activities on the territory of the European Union, the EORI registration must be completed in the country in which the economic operator is a tax resident (tax residency is a concept applicable to both individuals and companies).

DIRECTORS' LIABILITY

Mrs. Demet Karatay Yeşilöz
Legal Consultant and Director Holland Desk

ABSTRACT

The directors' liability is regulated in the Dutch Civil Code. The directors' liability can play a role in different situations. First of all, liability can arise in the founding phase of the company. In addition, the director has responsibilities towards the company and must therefore perform his duties properly. In case the director performs his duties improperly towards the company this can lead to the liability of the director, which is also referred to as the internal directors' liability. There may also be personal liability of the director towards third parties in special cases. This is also referred to as the external directors' liability. Finally, the director can be held liable for improper performance by the curator in the event of bankruptcy. In this article the liability of the director will be further elaborated.

Key Words: Directors' Liability, Internal Liability, External Liability, Liability of (Foreign) Legal Person, Improper Management, Unlawful Act, Company in Formation, Bankruptcy.

INTRODUCTION

Directors take certain risks in the performance of their duties and also have a certain degree of discretion. The main rule is that the limited liability company itself is responsible for the debts that are incurred. Directors' liability is therefore an exception to the main rule that the company is liable for the debts. The different types of directors' liability will be explained in this document. First of all, the liability of the director towards the company will be discussed, also referred to as internal directors' liability. Subsequently, the directors' liability of a legal person as director will be further explained. Thereafter, the external directors' liability will be further elaborated. Finally, directors' liability in the event of bankruptcy will be further explained.

1.TYPES OF DIRECTORS' LIABILITY

1.1. Liability of director at company in formation

If an intended director of a company (or others who act on behalf of the company to be incorporated), before the incorporation of the company, enters into obligations such as renting an office space, buying PCs, office furniture, etc., then this person acts on the basis of articles 2:93 paragraph 2 and 2: 203 paragraph 2 of the Dutch Civil Code (hereinafter referred to as "DCC") on behalf of the company in formation and is ''jointly and severally bound '' to the legal act performed until the company has ratified the legal act. In practice, it is only directors of a company who perform legal acts on behalf of a company in formation. The moment of the declaration of liability is of crucial importance. Ratification of a legal act of a company in formation can take place explicitly or tacitly. From that moment on, the company is bound by the agreement. If a company does not comply with the agreement despite the ratification, then there may be personal liability if the director knew or could reasonably have known when entering into the agreement that the company would not be able to fulfill its obligations. The knowledge that the company would not be able to fulfill its obligations is presumed to be present if the company is declared bankrupt within one year of its incorporation.

1.2. Internal directors' liability

The main rule is that the limited liability company itself is liable for debts of the company. The liability of the director towards the company is referred to as internal liability. According to the explanatory memorandum, the liability of directors should not be assumed too quickly. It is inherent in the work of directors that they take certain risks in the management of a company and have a certain degree of discretion in making decisions. The internal directors' liability will be further elaborated below. First of all, the liability of the director as natural person is discussed. After that, the liability of the legal person as director is further elaborated. Finally, the liability of foreign legal person will be further explained.

a. Liability of director (natural person)

According to Article 2:9 paragraph 1 of the DCC each Director is responsible towards the legal person for a proper performance of the tasks assigned to him. Due to paragraph 2 of this article each Director is responsible for the general conduct of affairs. He is liable for the full consequences of an improper performance of duties, unless, also in regard of the tasks assigned to the other Directors, he is not gravely to blame for it and he neither has been negligent in taking measures to avert the consequences of that improper performance of duties.

The starting point is the so-called collegiality principle. This means that directors are collectively responsible and jointly and severally liable for the improper performance of duties by the board, except for the possibility of justification (exculpation).

The obligation to provide information and the burden of proof is vested in the legal person. The legal person must prove that there is an undeniable shortcoming by the board that creates serious culpability. Once this has been established, this shortcoming can be attributed to all directors, unless an individual director demonstrates that he cannot be seriously blamed and that he has not been negligent in taking measures to remedy the consequences of the shortcoming. The obligation to provide information and the burden of proof for the lack of personal culpability rests explicitly on the individual director.

The Staleman/Van de Ven case contains the interpretation of art. 2: 9 of the DCC and the scope of the discharge granted by the general meeting of shareholders. The following legal questions have been raised in this case:

1. When can a director be seriously blamed in the sense of art. 2: 9 of the DCC?

2. To what extent can directors appeal to a discharge granted to them as directors by the general meeting of shareholders?

Regarding to the first legal question Supreme Court considered that for a serious accusation all the circumstances of the case should be assessed. The circumstances to be taken into account include the nature of the activities carried out by the legal person, the risks generally arising therefrom, the division of tasks within the board, any guidelines applicable to the board, the information that the director had or belonged to at the time of the decisions or conduct accused of against him, as well as the insight and care that may be expected of a director who is calculated for his task and who fulfills it meticulously.

In respect to the second legal question regarding the scope of a discharge, the Supreme Court notes that a discharge should not be interpreted too broadly so that it would also extend to information available to an individual shareholder on other grounds - outside the context of the general meeting of shareholders or to information that is not apparent from the annual accounts or has not otherwise been disclosed to the general meeting of shareholders before the latter adopted the annual accounts [1].

When a company's creditor is disadvantaged by the unpaid and unrecoverable claim, the following will be considered when assessing the presence of grounds for director's liability:

i. whether the director acted on behalf of the company or,

ii. caused or permitted the company to fail to comply with its legal or contractual obligations.

It may generally only be assumed that the director has acted unlawfully towards the creditor of the company where he,

1 *In the Staleman / Van de Ven judgment of the Dutch Supreme Court of January 10, 1997, NJ 1997/360.*

also in view of his obligation to perform a proper task as referred to in art. 2: 9 of the DCC, a sufficiently serious reproach can be made.[2]

Regarding under (i) is that the personal liability of the director of the company can be assumed if he knew or should reasonably understand, when entering into commitments on behalf of the company, that the company would not be able to fulfill its obligations and would not offer any recourse, except in circumstances to be invoked by the director on the basis of which the conclusion is justified that he cannot be personally blamed for the disadvantage. As pointed out under (ii), the director concerned may be held liable for damage of the creditor if his actions or omissions as a director are so negligent in the circumstances with respect to the creditor that he can be personally blamed for this. Such a serious reproach may in any case be the case if it is established that the director knew or should reasonably have understood that the conduct of the company brought about or permitted by him would result in the company's failure to comply with its obligations and nor would it offer any recourse for the resulting damage.[3]

The grounds for directors' liability according to Article 2:9 of the DCC can be e.g.:

- Withdrawing funds from the company for private purposes.
- Committing criminal offenses and / or fraudulent acts.
- Taking unnecessarily large and irresponsible financial risks.
- Failure to take out the usual insurance policies for business operations.
- Failure to comply with the notification of inability to pay to the UWV, the pension fund or the tax authorities.

b. Liability of legal person as director

Pursuant to Article 2:11 of the DCC, the liability of a legal person as a director of another legal person also rests jointly and severally on anyone who is a director thereof at the time the liability of the legal person arises. The regulation therefore pertains to each direct director of the legal person. If one director is liable, pursuant to art. 2:11 of the DCC, then also the legal person as its other directors can be held liable on the basis of art. 2:11 of the DCC.

According to the explanatory memorandum, Article 2:11 of the DCC relates to the liability of a legal person director arising from the law[4]. By appointing a legal person instead of a natural person as director of a legal person, one could avoid directors' liability. Article 2:11 of the DCC aims to prevent the avoidance of liability by means of these types of constructions.[5]

Art. 2:11 of the DCC applies in all cases in which a legal person in its capacity as director is liable under the law, so also under art. 6: 162 of the DCC. The creditor does not have to argue or prove the serious personal culpability of the director. However, the director of that legal person can be a director on the basis of art. 2:11 of the DCC to prevent liability by stating, and if necessary proving, that he personally cannot be seriously blamed for the conduct on which the liability of the legal person-director is based[6].

c. Liability of foreign legal person as director

The liability of Dutch legal person has been elaborated above. How about the foreign legal person who is acting as director to a Dutch legal person? Does Article 2:11 of the DCC also applies to the foreign legal persons? The following two cases have dealt with these questions.

In the case D Group Europe N.V. against bankruptcy curator mr. Schreurs. D Group Europe N.V. ("D Group") is a public limited company established in Belgium and incorporated under Belgian law and was a director and sole shareholder of the Dutch company D Freight Group B.V. ("D Freight"). On March 2, 2009, D Freight was granted a temporary suspension of payments with the appointment of the curator as administrator. On March 16, 1999, the suspension of payments was withdrawn and D Freight was declared bankrupt. The central question in this judgment was whether an indirect director, established abroad, of a Dutch bankrupt company on the basis of art. 2:11 jo. 248 paragraph 1 of the DCC could be held liable for the deficit in the bankruptcy. The Supreme Court considered in this case that:

"pursuant to the provisions of article 3, under e of the Corporations Conflict Law Act, the law applicable to the corporation governs, among other things, the question of who is liable in addition to the corporation by virtue of a certain capacity, such as that of director. This means that Dutch law as the incorporation right of D Freight also governs the liability of D Group as director of this company and that art. 2:11 of the DCC applies within this corporate relationship. This is without prejudice, as the Court of Appeal legal consideration under 11.7.5 has considered that the corporate relationships between D Group and its director (s) are governed by Belgian law as the incorporation law of D Group[7]."

In another case the Van der Meer q.q. / Pieper case the Supreme Court considered that based on Article 2:11 of the DCC the director can only be held liable if the liable legal person-director managed by it is a Dutch legal person and that Article 2:11 of the DCC cannot be applied to the foreign legal person, because the foreign legal person is determined by international private law. Application of this law leads to the conclusion that Pieper's liability must be assessed under Swiss law. As a result, Pieper could not be held liable on the basis of Article 2:11 of the DCC[8].

In view of these cases, it can be stated that Article 2:11 of the DCC does not apply to a foreign legal person acting as a director.

2. EXTERNAL DIRECTORS' LIABILITY

a. On the basis of tortious act (unlawful act) in accordance with article 6: 162 of the DCC

External directors' liability is the liability of a director towards a third party and is based on tort (unlawful act) conform Article 6: 162 DCC.

If a company fails to comply with an obligation or commits an unlawful act, the starting point is that the company alone is liable for damage resulting therefrom. In special circumstances, however, in addition to the liability of that company, there is also room for liability of a director of the company. In order to assume such liability, it is required that director can be personally blamed for the damage. Thus, for the assumption of liability of a director in addition to the company, higher requirements apply than is generally the case. A high threshold for liability of a director towards a third party is justified by the fact that with regard to the other party primarily the actions of the company are involved and by the social interest that directors are prevented from having their actions undesirably determined by defensive considerations.

Whether the director can be made personally reproach for the damage as a result of his actions depends on the nature and severity of the norm violation and the circumstances of the case.

If a person acts in his capacity as director, the director has generally only acted unlawfully towards a third party if he is personally responsible for serious reproach. This means that the director acts negligently towards the creditor in the given circumstances and can be personally blamed for this act. For example a director who has entered into an obligation on behalf of the company and the claim of the creditor remains unpaid and proves irrecoverable, the director may be held personally liable if he knew or should reasonably have understood when entering into that obligation that the company could not meet the obligations and would not offer any recourse, except in circumstances to be invoked by the director on the basis of which the conclusion is justified

2 *Judgment of the Supreme Court of February 18, 2000, No. C98 / 208, NJ 2000, 295*

3 *ECLI:NL:HR:2006:AZ0758, Judgment of the Supreme Court of 08-12-2006.*

4 *Kamerstukken I, 1985/1986, 16 631, nr. 27b, p. 22.*

5 *Kamerstukken, 16 631, nr. 27b, p. 22.*

6 *ECLI:NL:HR:2017:275, Judgment of the Supreme Court of 17 February 2017, case Kampschöer/Le Roux Fruit Exporters legal consideration under 3.4.2-3.4.3.*

7 *ECLI:NL:HR:2011:BP1408, Judgment of the Supreme Court of 18 March 2011, legal consideration under 4.1.3.*

8 *ECLI:NL:HR:2013:CA3958, Judgment of the Supreme Court of 21 June 2013, legal consideration under 3.4.*

that he cannot be personally blamed for the loss[9]. This is also called the Beklamel criterion. The "Beklamel criterion" implies the requirement that the director knew or should have understood when entering into the commitment that the company's creditor would suffer damage as a result of his actions[10].

There may also be serious personal reproach if the director has caused or permitted the company to fail to comply with its legal or contractual obligations. The director is acting unlawfully towards the company's creditor when, partly in view of his obligation to perform a proper task as referred to in Article 2:9 of the DCC, he can be personally blamed for a serious reproach.

Some examples for which a director can be held liable are:

- Entering into obligations, knowing that the company will not be able to fulfill them;
- Acting contrary to the statutory object of the company;
- Selective payments to affiliated companies and individuals;
- Continuation of the company-run business after the moment of actual insolvency;
- Failure to keep records;
- Not filing or filing the annual accounts too late at the Dutch Chamber of Commerce;
- Fail to prepare the annual accounts on time;
- Giving a misleading representation of the position of the legal entity in the annual report;
- Unjustified personal enrichment at the expense of the legal person.

b. External liability of directors in case of bankruptcy

External directors' liability can be based on manifestly improper management (article 2: 248/138 of the DCC) and on a claim from torts (article 6: 162 of the DCC). First, the possibility of redress for manifestly improper management is discussed. Subsequently, the claim from an unlawful act is discussed.

1. CLAIM BASED ON IMPROPER MANAGEMENT (ARTICLE 2: 248/138 DCC)

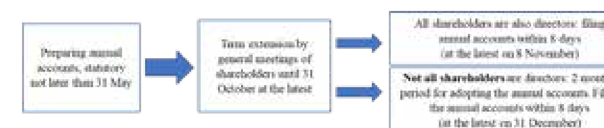
Article 2: 138 (in case of public limited liable company) and Article 2:248 (in case of private limited liable company) of the DCC deal with the event that a company has gone bankrupt and creditors are left with an enormous unpaid claim and the company can no longer be held liable. Pursuant to article 2: 138/2:248 paragraph 1 of the DCC, in the event of bankruptcy of the company:

"each director is jointly and severally liable towards the estate for the amount of the debts, insofar as these cannot be met by liquidation of the other assets, if the management clearly fulfills its tasks improperly and it is likely that this is a major cause of the bankruptcy."

In the event of bankruptcy, the curator can appeal to improper management and the resulting directors' liability. That directors' liability applies if the board has clearly performed its duties improperly and it is plausible that this is an important cause of the bankruptcy. In the Panmo case, the question was raised of when there was manifestly improper performance in the sense of Article 2: 248/138 of the DCC. The Supreme Court stated that improper management within the meaning of Article 36 paragraph 3 of the IW 1990 (Collection Law) and Article 2: 138 and 2:248 of the DCC can only be spoken if no reasonable thinking director - under the same circumstances - would have acted in this way[11].

Pursuant to paragraph 2 of Article 2:138/248 of the DCC if the board has not fulfilled its obligations under Articles 2:10 or 2:394, it is considered as not performing its duties improperly and it is suspected that improper performance of its duties is an important cause of the bankruptcy. Article 2:10 of the DCC refers to accounting and Article 2:394 of the DCC refers to the obligation to publish the annual account of the company. This means that in case the accounting obligation has not been met properly or the obligation to publish the annual account has not been fulfilled than pursuant to Articles 2:138 or 2:248 paragraph 2 of the DCC it is considered as improper performance of its duties and is also considered as an important cause of the bankruptcy. However, if the director set an external cause for of the bankruptcy, and the director is accused by the curator of having failed to prevent the occurrence of that cause, it is allowed that the director states facts and circumstances and, if necessary, demonstrate plausible evidence that shows that this failure does not result in improper performance of duties. If he succeeds in doing so, it will be up to the curator to demonstrate, on the basis of article 2: 248 paragraph 1 of the DCC, that the manifestly improper performance of duties was nevertheless also an important cause of the bankruptcy[12].

After closing the financial year, it is important to file the annual accounts on time with the Chamber of Commerce. When must the annual accounts at the latest? For the deadlines, see the timeline shown below.



2. CLAIM BASED ON TORT (UNLAWFUL ACT) (ARTICLE 6: 162 OF THE DCC)

If there are no other remedies, there may be a possibility to establish directors' liability based on tort. Article 6:162 of the DCC is the general basis for claims for damages that arise from torts. On the basis of Article 6:162 (1) of the DCC:

"a person who commits a tort towards another which can be imputed to him, must repair the damage which the other person suffers as a consequence thereof."

In order to assume liability based on tort, it is required that director can be personally blamed for the damage. Higher requirements apply for the personal liability of the director than is generally the case. The tortious act has been in detail elaborated above. See for further explanation under point A.

External directors 'liability on the basis of improper management can only be invoked by the curator, but directors' liability on the basis of tort (unlawful act) can be invoked by an individual creditor.

CONCLUSION

The main rule is that the company itself is responsible for the debts that incur. Directors' liability is therefore an exception to the main rule that the company is liable for the debts. There are different types of liability of the director. First of all, if an intended director of a company enters into obligations before the incorporation of the company, then the director or person acting on behalf of the company in formation is liable for the legal acts when the company does not ratify these legal acts afterwards. For the incorporated company, the liability of the director as natural person towards the company, also known as internal liability, is based on Article 2:9 of the DCC. The director can be personally liable for improper performance of his duties if he knew or should reasonably understand, when entering into commitments on behalf of the company or caused or permitted the company to fail to comply with its legal or contractual obligations. Legal person acting as director on behalf of the company can also be liable jointly and severally on anyone who is a director thereof at the time according to Article 2:11 of the DCC. However, this cannot be stated in case of a foreign legal person acting as director on behalf of the Dutch legal person. In case of external directors' liability, a third party can appeal tortious acts in accordance with Article 6:612 of the DCC. However, higher requirements apply and the personal liability of the director must be proved. In the event of bankruptcy, the curator can apply its claim based on improper management in accordance with Article 2:138/248 of the DCC. There is improper management if no reasonable thinking director - under the same circumstances - would have acted in this way. When the administration is kept improperly or the annual account is not filed on time than it is considered as improper performance of its duties and is also considered as an important cause of the bankruptcy. Finally, when there are no other options curator can apply for tortious act according to Article 6:162 of the DCC.

9 *ECLI:NL:HR:1989:AB9521, NJ 1990/286, Judgment of the Supreme Court of 6 October 1989, case Beklamel.*

10 *See also ECLI:NL:HR: 2014:2627, Judgment of the Supreme Court of 5 September 2014, case September.*

11 *ECLI:NL:HR:2001:AB2053, Judgment of the Supreme Court of 8 June 2001, case Panmo, under 3.7.*

12 *ECLI:NL:PHR:2007:BA6773, Judgment of the Supreme Court of 30 November 2007, the blue tomato case, under 3.4.*

THE SOLID DUTCH CORPORATE STRUCTURE AND THE HISTORICAL BACKGROUND

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ABSTRACT

The Netherlands has a solid corporate structure and legislation framework when it comes to setting up the company organization and the corporate governance. This is all thanks to the history of the Netherlands, which goes back to the period of the Dutch East Indies Company (VOC; Verenigde Oost-Indische Compagnie) in early 17th century. From back then the Dutch had already realized the importance of creating a corporate structure for a company.

The Netherlands today, with the worldwide COVID-19 pandemic has proven to stay a relatively stable country. The recent survey from US News and the earlier survey from CEO Worldwide Magazine, the Netherlands is one of the most stable countries in terms of financial, economic, and social climate.*

Key Words: Dutch Corporate Structure, Corporate Governance Regimes under Dutch Law, Dutch Trading and Finance History, VOC, First Listed Public Company in the world.

INTRODUCTION

In general, a corporate structure is the organization of different business units or departments within a company. Each department has a specific function and collaborates constantly with the other departments to contribute and to achieve the overall values, mission, and goals of the company. In the interest of the stockholders to be well looked-after, many companies create a separation between management and the ownership in a company. Clear structure can grow a start-up business into an international company that can be traded around the world. A well-defined structure helps a business to shape its goals and attract investors who easily understand how a company plans to generate revenues and profits. The standard of corporate structure includes the Board of directors, who control and manage the business; the Corporate officers, who run operations and the Shareholders, who own the business.[1]

1. CORPORATE STRUCTURE IN THE NETHERLANDS

In the Netherlands, the structure of the company is regulated in the Dutch Civil Code, Book 2. The business structures with a legal form in the Netherlands are:[2]

- Associations (“Verenigingen”);
- Cooperatives (“Coöperatie”’);
- Mutual Insurance Societies (“Onderlinge waarborgmaatschappijen”);
- Open Corporations (“Naamloze Vennootschappen”/ N.V.), public limited companies with free tradable shares.
- Closed Corporations (“Besloten Vennootschappen” / B.V.), private limited companies with restricted tradable shares.
- Foundations (“Stichtingen”).

1 Corporate Structure: Understanding it’s Basics https://eqvista.com/business-structure/corporate-structure

2 Dutch Civil Code, Book 2 article 3.

* These Are The World’s 10 Most Economically Stable Countries In 2019 > CEOWORLD magazine; The 10 Most Economically Stable Countries, Ranked by Perception | Best Countries | US News

The common use of the legal forms in the Netherlands are B.V. and N.V., regardless of the company’s legal form, the following regimes rule the governance structure of the Dutch companies and provide alternative governance models in the Netherlands.[3]

1. Common regime (“Gewoon Model”). Applicable mainly for small and medium-sized companies;
2. Structure regime (“Structuurmodel”); This regime is applicable to companies that meet criteria related to the number of employees and the amount of subscribed capital;
3. Mitigated structure regime (“Verzwakt Structuurmodel”);
4. Exempted regime (“Vrijgesteld Model”).

The Common regime gives small and medium-sized companies a choice between a governance structure with only a management board entirely composed of managing directors, and a two-tier board model with an executive management board and an additional supervisory board.[4] In this regime, the shareholder’s meeting has extensive powers to govern companies.

Regulations on the corporate governance system of large companies have been expanded through the Structure regime. Companies with the Structure regime are obliged to adopt a two-tier board structure. Under this regime, a substantial part of the control of the shareholder’s meeting changes to the mandatory supervisory board. Exception applies for multinational companies and companies that are part of a foreign holding structure, they may choose the mitigated regime and the exempted regime.[5]

The Mitigated regime applies to multinational companies, where the holding, parent company employs most of the employees in foreign country or outside the Netherlands. The Mitigated regime is of great importance to foreign companies and/or multinationals that seek full control over subsidiaries incorporated in the Netherlands. The mitigated form of the Structure regime is applicable to companies when at least fifty percent of a corporation’s shares are held by a holding or a joint venture (a group of parent companies).[6]

In this regime the supervisory board has less extensive powers, the supervisory board does not have the formal rights to appoint and to dismiss members of the management board and to adopt the annual accounts. These rights belong to the shareholders’ meeting. However, an independent supervisory board is still mandatory under this regime and the co-optation system is still in place. In addition, the supervisory board remains in the formal position to approve management decisions. The Civil Code provides these rules to secure an independent supervisory board that not only protects the rights of shareholders, but those of employees and other stakeholders as well.[7]

The Dutch Civil Code also provides rules that exempt companies from the structure and the Mitigated structure regimes, that is the Exempted regime or “vrijgesteld structuurregime”. This applies to companies which are dependant of a holding, parent company or group that is already subject to the Structure regime or the Mitigated structure regime. Although these dependant companies may meet the three cumulative criteria of structure companies, the formation of a supervisory board in these dependent companies is not mandatory. If a supervisory board is formed, the general meeting of shareholders appoints and dismisses supervisory directors. The general meeting of shareholders has also the formal right to appoint and dismiss managing directors and to approve certain decisions. Companies can be also exempted from the rules of the Mitigated and Structure regimes when it is a mere holding company belonging to an international group of companies; if most of the employees

3 Developmentwork.net; 8.2 Corporate Governance in the Netherlands, http://developmentwork.net/chapter-8-two-tier-board-attributes-netherlands/251-82-corporate-governance-in-the-netherlands-

4 Dutch Civil Code, Book 2 article 152: Book 2 article 262.

5 Developmentwork.net; 8.2 Corporate Governance in the Netherlands.

6 Dutch Civil Code, Book 2 article 155: Book 2 article 265.

7 Developmentwork.net; 8.2 Corporate Governance in the Netherlands.

of the entire group are employed outside the Netherlands, and/or acts exclusively as a service provider, managing and/or financing the group companies or subsidiaries.[8]

Due to its flexibility, the Dutch Civil Code provides companies that operate under the rules of the Mitigated and Exempted regimes, to have possibility to practically follow board practices that are common to large corporations in the US and the UK. In these two regimes, the supervisory board has less extensive powers, while the formal rights to appoint and to nominate managing directors are granted to the general meeting of shareholders.

2. THE TWO-TIER STRUCTURE

As mentioned earlier, under Dutch Law, the mandatory application of the statutory two-tier structure is for companies subject to the Structure regime, which meet to the following legal criteria:[9]

1. For a period of three consecutive years, the company's issued capital and reserves amount to not less than €16 million.

2. The company has a works council instituted pursuant to a statutory requirement.

3. The employment number reaches at least 100 employees in the Netherlands.

The two-tier structure consists of a management board of directors or governors and a separate supervisory board, who supervise and advise the management board and oversee the company business operation. This is the classical Dutch board system which has been existed since early 17th century in the Dutch history.[10] The first listed company in the world, the Dutch East Indies Company (the VOC) introduced a form of a supervisory board to improve the company's governance not only to accommodate the shareholder interest but also to protect the interest of the company itself.[11]

3.DUTCH EAST INDIES COMPANY

In 1602, the Dutch government supported the creation of a single "United East Indies Company" or Dutch East Indies Company or in Dutch, '*Verenigde Oost-Indische Compagnie*', the VOC. This company was granted a trading monopoly over Asia, what started-off as a spice trader, which later expanded to become the greatest shipping and trading company in the world during the 17th and 18th centuries.[12] The VOC was the first company to operate globally in different continents such as Europe, Asia, and Africa, and the first company in history to raise funds by offering its shares to the public, the world's first recorded IPO (Initial Public Offering). This became a key event in financial history, where a listed public company for the first time ever was formally created.[13]

With the establishment of its administration centre (2nd headquarter) on the island of Java, Indonesia, in the city of Batavia (present-day Jakarta), the VOC played an innovative role in corporate organization, helped to establish important links between European and Asian regional economies and strengthened economic integration in Asia.[14] The VOC was an early pioneering model of the multinational/transnational corporation.

4. CLASS OF SHARES AND GOVERNANCE ISSUES

The VOC had two types of shareholders: the participations, who could be seen as non-managing members, and the Governors, "*bewindhebbers*" who acted as managing directors. This was the usual set-up for Dutch joint-stock companies at the time. The innovation in the case of the VOC was that the liability of not just the participations but also of the Governors were limited to the paid-in capital. The VOC therefore was a limited liability company or a public limited company since the shares were publicly traded. Also, the capital would be permanent during the lifetime of the company. Consequently, investors that wished to liquidate their interest in the interim could only do this by selling their shares to others on the Amsterdam Stock Exchange.

The seventeenth-century Dutch businessmen, especially the VOC investors, were possibly the history's first recorded investors to seriously consider the corporate governance's problems. This was started already in 1609 when a sizeable investor complained about the poor corporate governance of the VOC. In 1622, the history's first recorded shareholder revolt also happened among the VOC investors who complained that there was no proper administration, the company account books had been "smeared with bacon" so that they might be "eaten by dogs."

The investors demanded a proper financial audit. They complained about management self-enrichment and secrecy. A form of a supervisory board was introduced in 1623 following shareholder pressure (i) to improve the company's governance and (ii) to protect the shareholder's as well the company's interest. Hereby the company's interest was separated from the shareholder's interest, where the latter gaining profits or capital returns.[15]

CONCLUSION

The strong background of the business and financial history, which existed already in the early 17th century (VOC), makes the Netherlands own solid corporate structures due to a legislation framework for corporations to comply with. Having a proper corporate governance is important for companies as it would give a direction how to operate business complying with legal framework and regulations, which lead to business growth. The stable framework in terms of financial, economic, and social climate in the Netherlands attract investors. This solid structure gives the investor confidence to make decisions, both medium and long term for the growth of the business.

8 *Dutch Civil Code, Book 2 article 153; Book 2 article 263.*

9 *Dutch Civil Code, Book 2 article 154.*

10 *J. van Bekkum, J.B.S. Hijink, M.C. Schouten & J.W. Winter Corporate Governance in the Netherlands, EJCL, December 2010.*

11 *Kamerstuk 28179, nr. 3 | Overheid.nl > Officiële bekendmakingen (officielebekendmakingen.nl)*

12 *F.S. Gaastra (1986), Dutch East India Company; expansion and decline.*

13 *Lodewijk Petram, The World's First Stock Exchange (New York: Columbia University Press 2014).*

14 *J. Nijman, The VOC and the expansion of the world-system 1602–1799, Elsevier, May 1994.*

15 *Kamerstuk 28179, nr. 3 | Overheid.nl > Officiële bekendmakingen (officielebekendmakingen.nl)*

HYBRID MISMATCHES DUE TO THE DIFFERENT QUALIFICATIONS OF CRYPTOCURRENCIES

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ABSTRACT

Within the EU, hybrid mismatches can be neutralized by the legislation of ATAD2 for hybrid entities, hybrid financial instruments and hybrid permanent establishments. With regards to hybrid financial instruments, the lack of guidance for the categorization and classification of cryptocurrencies and the unclear equation of cryptocurrencies to certain financial instruments can cause a whole new batch of hybrid mismatches. To recognize these hybrid mismatches is of importance due to the rise of popularity in the usage of cryptocurrencies worldwide.

Key Words: Hybrid Mismatch, Cryptocurrencies, Tokens, ATAD2, OECD.

INTRODUCTION

As the popularity of cryptocurrencies is steady growing, we can ask ourselves what the reasons are of the recent surges. Another important question to ask is how are consumers and companies are going to use cryptocurrencies? And what are going to be the tax implications in this? Some states have taken the liberty to tax cryptocurrencies according to their own views. But this may prove to be problematic in the long run. Because of the different fiscal treatment of cryptocurrencies, these discrepancies can result in hybrid mismatches.

As explained in a previous article[1] an important aspect for correctly treating cryptocurrencies tax-wise is the qualification of the different subcategories of cryptocurrencies. This qualification may differ per state, which can result in that some cryptocurrencies may have a hybrid character. Having stated this, it is important to see to what extent ATAD2 can be applied to cryptocurrencies that may result in hybrid mismatches if treated as financial instruments.

First, I will briefly discuss the different subcategories of cryptocurrencies. For the purpose of this article I will subcategorize cryptocurrencies in three categories as categorized by the OECD: payment tokens, security tokens and utility tokens. I will also discuss a fourth sub-category: debt tokens.

Secondly, I will explain the implications that may arise with regards to hybrid mismatches due to the different approach of different countries that tax cryptocurrencies. I will show this by way of an example. In which the example will show how said hybrid mismatches and how current ATAD2 regulation can neutralize the tax benefits that arise from hybrid mismatches.

1. CATEGORIES OF CRYPTOCURRENCIES

Cryptocurrencies can in principle be subcategorized in coins and tokens. Coins are cryptocurrencies that run on their own blockchain and tokens are cryptocurrencies that run on a third party blockchain[2]. But the terminology of coins and tokens is also hybrid in the sense that when speaking of a coin, one usually means a Payment token like Bitcoin (although because of the increasing value of Bitcoin it can also be seen as an asset). The OECD has categorized[3] cryptocurrencies in three categories; payment tokens, security tokens and utility tokens. These tokens can be summarized as followed;

1.1. Payment Token

A token can be categorized as a payment token if it has the following characteristics according to the OECD:

- The token is intended to operate most similarly to traditional, fiat currencies[4];
- Payment tokens are usable as a mean of exchange for goods or services and possibly also as a store of value and a unit of measurement;
- Often referred to as virtual or cryptocurrencies in general. Examples of these types of tokens (coins) are Bitcoin and Litecoin.

Most states see all types of cryptocurrencies as an "asset" and not as a currency as payment tokens portray themselves to be. The reasons that states often do not legally categorize a cryptocurrency as a currency is because of the following; cryptocurrencies are decentralized, they have a lack of backing by the local governments, the price volatility of cryptocurrencies is an issue and the limited use of the cryptocurrency as a means of exchange. Similarly, for income tax purposes, almost all countries that have issued a statement on the matter have declared these to be a form of property for tax purposes[5].

Some of the few countries that have stated that payment tokens are treated as a form of currency within their local government are Belgium, Italy, Poland and Cote d'Ivoire.

1.2. Security Token

A token can be categorized as a security token if it has the following characteristics according to the OECD:

- Designed as tradable assets that are held for investment purposes and classified as a security (or equivalent) under applicable laws. Security tokens could be equated to shares or share options, a security token represents ownership for the token holder;
- Examples given by the OECD are the cryptocurrencies Spice and tZero. But in my opinion cryptocurrencies like NEO and Ontology are better representatives of a Security token. These cryptocurrencies also periodically give out a form of dividend called Gas.

1.3. Utility Token

A token can be categorized as a security token if it has the following characteristics according to the OECD:

- Their primary use is to facilitate the exchange of or access to specific goods or services;
- They may for instance. Act as a license to allow the holder access to particular service, as a pre-payment or voucher for a good or service (even where that good or service is not yet available);
- Examples are Bee Token, Storj.

A utility token in my opinion is a token with a very closed system and similar currencies have already existed without operating on a blockchain and thus be classified as a cryptocurrency. Think of the currency used in World of Warcraft (WoW Tokens) for example. The utility token in my opinion is the least appealing type of cryptocurrency for investment purposes.

As stated above these are the qualifications that are given by the OECD. But that having been said; different jurisdictions can have their own definition of the above category of cryptocurrency, that may result in different classifications of assets and different tax implications.

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1 Rahimzadeh, P. (2021, march 10). NAZALI GUNDEM | THE CORRECT TAXATION OF CRYPTOCURRENCIES IN 2021. Nazaligundem.Com. http://nazaligundem.com/en/press/the-correct-taxation-of-cryptocurrencies-in-2021

2 Bal, A. (2019). Taxation, Virtual Currency and Blockchain, par [B]) p. 38

3 OECD (2020), Taxing Virtual Currencies: An Overview Of Tax Treatments And Emerging Tax Policy Issues OECD, Paris. www.oecd.org/tax/tax-policy/taxing-virtual-currencies-an-overview-of-tax-treatments-and-emergingtax-policy issues.htm p. 13

4 A currency issued and declared as legal tender by a central bank or public authority is considered fiat currency, such as British Pounds and Euros.

5 OECD (2020), Taxing Virtual Currencies: An Overview Of Tax Treatments And Emerging Tax Policy Issues, OECD, Paris. www.oecd.org/tax/tax-policy/taxing-virtual-currencies-an-overview-of-tax-treatments-and-emergingtax-policy issues htm p. 22.

1.4. Debt token

It could be argued that a debt token could fall under the same category as a security token. But for reasons of this article I will also discuss the debt token as a separate token. I noticed that the OECD has not mentioned an – in my opinion – important category of cryptocurrency, namely the debt token. Debt token[6] have been described as interest-accruing tokens representing the debt owed by the token holder. There are 2 types of debt tokens:

- Stable debt tokens, representing a debt to the protocol with a stable interest rate;
- Variable debt tokens, representing a debt to the protocol with a variable interest rate.

As the OECD has stated, most member states of the OECD classify cryptocurrencies as (intangible) assets, but cryptocurrencies are also classified, as financial instruments, currency, legal payment methods or the category of "not specified". To have a clear distinction in what kind of category cryptocurrencies in general fall and the sub-categories of cryptocurrencies as stated above fall within is essential for the correct tax treatment of cryptocurrencies and essential for avoiding possible hybrid mismatches due to the different classification that states uphold.

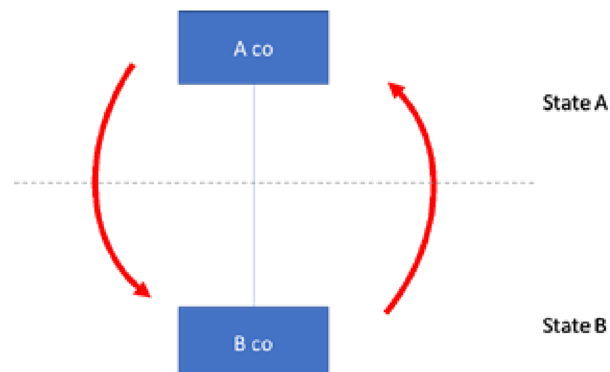
2. HYBRID MISMATCHES

ATAD2 aims to counter hybrid mismatches. Hybrid mismatches are situations in which a tax benefit is obtained between related entities in EU member states and between EU Member States and third countries. These benefits are obtained due to qualification differences of entities, financial instruments or permanent establishments. The differences between these corporate tax systems can result in the following:

1. A payment (in one country) is deductible, but the corresponding revenue (in the other country) is not taxed (deduction – no inclusion); or
2. One and the same payment (cost or loss) is deductible multiple times (double deduction).

This principle of obtaining benefits by using the different interpretation of a financial instrument also applies to cryptocurrencies.

On the basis of an example I will show how the different qualification that are upheld by different states can cause for hybrid mismatches.



For this example we have to assume that both states equate cryptocurrencies to existing financial instruments and that the states classify the same cryptocurrency as a different financial instrument due to their local legislation.

A co and B co are affiliated companies. They are both EU member states. A co provides an equity provision to B co. This equity provision is granted by means of a token (cryptocurrency). State B considers this token to be a (hybrid) loan in the form of a debt token. Because in state B, the equity provision is viewed as a loan, payments by B co to A co in relation to this token are treated as deductible interest expenses.

Country A labels the transaction (transfer of the token) as a provision of equity and labels the token as a payment token, in state A, payment tokens are qualified as assets. As a result of which a related payment by B co qualifies as a distribution of dividends instead of interest.

Because of the affiliation in which A co holds shares in B co, it is possible that the dividend is not included in the tax base since profit distributions are exempt[7] in certain circumstances. This results in that the payment by B co to A co is not included in the tax base of A co, but that B co can deduct the payment to A co (deduction, no inclusion), deductible expenses at the level of the subsidiary, with no corresponding tax at the parent company.

This is a hybrid mismatch with a financial instrument because there is:

- a deduction without relating it to tax; and
- this outcome is due to a difference in the qualification of the instrument.

This hybrid mismatch can be overruled however, via the Parent Subsidiary Directive ("PSD") if the parent (A co) would have 10% or more shares in B Co. According to the PSD, the participation exemption cannot be applied to benefits received by A co if they are deductible, de jure or de facto, at the level of B co in State B.

That would result in that the participation exemption that can be applied in State A would not be applied. Which would mean that there would be a deduction at B co and a inclusion in the tax base of A co. And with this there would not be a hybrid mismatch anymore because the PSD takes precedence over ATAD2. Please note that in the above sketched situation, if State B would not be an EU member state, the PSD would not be applicable and ATAD2 is applicable. If in this situation State B would be The Netherlands in which B co is the payer of the interest and state A would be a third country, The Netherlands would apply the primary rule of refusing the deduction at the level of B co. Therefore neutralizing the tax benefit that arises due to the hybrid mismatch[8].

If in this situation State A would be The Netherlands and A co would be a Dutch BV for example, The Netherlands would apply the secondary rule[9] in which the Netherlands would refuse the application of a possible participation exemption[10] and therefore adding the receivable to A co its tax base. And neutralizing the raised tax benefit due to the hybrid mismatch.

CONCLUSION

At this point of writing there is much more that has to be known and developed about the correct taxation of cryptocurrencies and what eventually will be the correct qualification of cryptocurrency categories on a multilateral scale. Because of the lack of unity in qualification of cryptocurrencies by OECD member states and the lack of any concrete guidance by the OECD as of yet, hybrid mismatches may occur between member states and between member states and third countries. For now this would seem not to be a very valid problem because cryptocurrencies are not relatively used as much as traditional fiat currencies or traditional financial instruments. But the question is that even if hybrid mismatches would occur due to the different interpretations of cryptocurrencies by different states, would these hybrid mismatches even be recognized by the local tax authorities in the relevant states? How this will work out in practice remains to be seen.

6 *Bal, A. (2019). Taxation, Virtual Currency and Blockchain chapter 3, p 39*

7 *For example, if State A would be The Netherlands and the participation exemption is applicable which allows to exempt the dividend distributions from the subsidiary to the parent company.*

8 *Article 12aa CITA*

9 *Article 12ab CITA*

10 *Article 13 paragraph 17 CITA*

ABOUT NAZALI RUSSIA

NAZALI RUSSIA started its activities in December 2019.

In Moscow, NAZALI has signed up a promising team of players from prominent Russia-based law firms, top-ranked in most legal directories. Our associates have a wide-range expertise and knowledge of the local market, which is combined with all the advantages of the Head of Russia Partner thorough knowledge of the Turkish business major industries.

Our Russian team has credible experience and ample expertise to meet the legal and tax needs of companies doing business in Russia. NAZALI Moscow office is also providing comprehensive legal and tax support for international clients anticipating investments in Russia or expanding their presence, both inbound and outbound.

Now, NAZALI in Russia mostly focuses on high quality day-to-day legal and tax support required from small to large businesses of broad spectrum of industries. This includes ad-hoc advice, projects support, compliance issues, dispute resolution and litigation etc.

Our clients include a number of international and domestic businesses, including leading Turkish and international companies, and entrepreneurs.

As conditions continuously evolve, NAZALI always aims to further itself remaining true to its motto "GROW WITH KNOWLEDGE" and has set out with the aim of providing the most efficient and comprehensive solution for its clients. Hence, to meet these high standards our team is also constantly growing, both enhancing its expertise and welcoming new talents.

In response to the clients' needs NAZALI Moscow team has recently taken on board impressive professionals in the field of audit and accounting, thus, significantly enlarging the scope of assistance offered to clients.

NAZALI RUSSIA is headed by Ms. Altinay Sheralieva who launched the office in 2019. She worked as legal counsel of international investment projects, she is experienced in a wide range of issues, including, legal due diligence, merger and acquisitions, corporate law, contracts law. Ms. Altinay Sheralieva acts as Partner and General Director and has solid experience in assisting clients with regard to their projects in the Russian Federation and CIS jurisdictions.

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CURRENT NEWS ABOUT RUSSIA

» Denunciation of the Double Tax Treaty between Russia and the Netherlands.

Russia served official notification on denunciation of the Double Tax Treaty to the Netherlands. Therefore, the application of this Double Tax Treaty will stop on January 01, 2022.

Official Dutch authorities still express some hope to find a mutually acceptable solution and conclude a new treaty that would be beneficial for both parties.

» Clarifications of taxation of dividends.

Russian Federal Tax Service issued a clarification letter regarding taxation of dividends paid by a Russian company to a foreign company, the actual right to which belongs to individuals, whether Russian tax residents or non-residents (Letter No. BS-4-11 / 7571@ dated 01.06.2021).

In the said case, Russian paying company shall be recognized as a tax agent and shall withhold personal income tax. For individuals, being Russian tax residents, the rate shall be (i) 13% on the amounts within 5 million rubles and (ii) 650 thousand rubles and 15% on the amounts exceeding 5 million rubles.

Applicable withholding tax rate with respect to dividends the actual right to which belongs to individuals, being Russian tax non-residents, is defined based on relevant double tax treaty.

» Amendments to the list of import VAT exempt equipment.

The list of technological equipment (including accessories and spare parts to it), analogues of which are not manufactured in Russia, which is exempt from VAT in case of import to the Russian territory has recently been amended. New version is shorter as compared to the previous one, even though it was added with some new positions.

» Further lifting of currency control barriers.

Non-commodity exporters will be exempt from the obligation to repatriate foreign currency earnings. A bill developed by the Ministry of Finance of Russia allows non-commodity exporters to receive payments in foreign currency under export agreements concluded with non-residents directly to their bank accounts opened abroad, bypassing authorized banks. Lifting this repatriation requirement is scheduled for July 01, 2021. This is one of the steps aiming at liberalizing currency controls and stimulating non-commodity export growth.

Cancellation of repatriation requirement will not apply to loan agreements as well as to advance payments to non-residents made under foreign trade agreements.

» Registration of Russian legal entities via a notary will be simplified.

The bill on the simplification of company registration formalities via a notary passed the second reading. In case the company's founders certify their signatures on the registration application vis notary, the latter will be liable to submit the application to the tax authorities on the same day. This will become a single notarial act. New rules will not apply to specific types of legal entities subject to a different registration procedure (i.e. banks).

» Single tax payment for legal entities.

A bill enabling legal entities to benefit from single tax payment mechanism has been submitted to the Russian Parliament.

According to the said bill, the companies will have a possibility to make a single tax payment and, thus, to pay at a single time for taxes and social charges, including arrears, upcoming payments, penalties, fines and late payment interest. The Federal Tax Service will properly re-allocate the amounts on its own.

Overpaid and overcharged amounts of taxes and charges could also be offset against the single tax payment on the basis of the taxpayer's application.

The amounts of single tax payment can also be claimed back by the taxpayers in the part that has not been offset by the tax authorities. The return is made within a month pursuant to an application submitted by the taxpayer. If the tax authorities do not comply with the deadline, late payment interest will be due.

Third parties should have the right to make single tax payments for the companies. However, in such a case, they would be unable to claim the return of these sums from the budget.

The bill in question also extends the system of overpayments offset among taxes and social charges. At present, it is unavailable and the overpaid taxes can be offset against other taxes but not against social charges and vice versa.

» Moral damage caused to employees.

New law, entering into force on April 16, 2021 fixed 2 options when an employee can claim compensation for moral damage: (i) together with a claim for restoration of his/her labor rights or (ii) within 3 months following the date of entry into force of the court decision, which fully or partially restored his/her labor rights. Disputes on compensation for moral damage are considered only by courts. The said deadlines will be incorporated into the provisions of the Labor Code of Russia.

» Electronic apostille to be available in Russia.

Starting from July 01, 2022, competent Russian authorities will be able to affix an electronic apostille with a two-dimensional barcode. It will encrypt the address of the Internet page with entries about this apostille from a special register. Requests for electronic apostille will be made online and will need to be certified with a strengthened unqualified electronic signature. Along with an electronic apostille, the applicant, upon his request, will be entitled to obtain a paper one.

» Investment tax deduction for Russian software.

As an initiative to support the IT industry, the Russian Government is considering proposals to include in the investment tax deduction for corporate income tax the costs for the implementation of Russian software, software and hardware complexes and computer equipment registered in the unified register of Russian programs and the unified register of Russian radio-electronic products. This measure should stimulate the import substitution and purchase of domestic software and computer equipment by state-owned and private companies.

POWERS AND RESPONSIBILITIES OF THE GENERAL DIRECTOR UNDER RUSSIAN LAW

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Senior Associate

ABSTRACT

Russian law traditionally gives particular importance to the figure of the general director of limited liability company. This article analyses the powers of the general director of a limited liability company as a person who has the right to manage the company's activities directly and make key decisions. Furthermore, issues such as control of the actions of the general director and his responsibilities before the company and its shareholders are also considered.

Key Words: Corporate Control, Responsibility, the Principle of "Two Keys", General Director

Introduction

With purpose of increase of the investment attractiveness, a few legal instruments of corporate control over the activities of the general director have been introduced to Russian legislation in last decade.

1. "UNLIMITED" POWERS OF THE GENERAL DIRECTOR

In accordance with the legislation of the Russian Federation the position of the sole executive body shall be established in each legal entity. As a rule, this position is held by the general director of the company. The law stipulates that the general director "manages the day-to-day operations" of the company[1]. Which means that absolutely all issues related to the activities of the company fall within the competence of the general director. Therefore, the general director, by virtue of the law, has the right to conclude any transactions on behalf of the company, bind the company with any obligations, hire employees at its sole discretion, including top executives, set the terms of employment agreements, including determination the amount of a remuneration[2].

The legislation of the Russian Federation establishes accountability obligation with respect to the general director before the shareholders of the company, however specific reporting forms have not been approved yet[3]. Accordingly, absence of the concrete accountability obligation before shareholders of the company, also incompetent management decisions and transactions made with affiliates on non-market terms in some cases may result unprofitability of the company. As it is known, unprofitability of the company will require additional funding to improve the financial situation of the company. As for transactions concluded by the general director at a loss of the company, the procedure of invalidation of such transaction is too complex, lengthy and, as practice shows, not always effective. Russian courts in most of the cases do not recognize that the general director acted to the detriment of the company while concluding a particular transaction. From the point of view of Russian court practice and decisions, the general director acts in the interests of the company and in the interests of its shareholders, unfortunately it is too difficult to prove the opposite.

2. FORMS OF CONTROL OVER THE ACTIVITIES OF THE GENERAL DIRECTOR

1. The most common way to control the activities of the general director is to include in the company's charter provisions that establish the obligation with respect to the general director to obtain the prior approval of all shareholders of the company to conclude certain types of transactions[4]. However, the wording of the related provisions of the charter shall be clearly verified, otherwise the day-to-day operations of the company may be slow downed: on the one hand, the charter, which establishes preliminary approval for a large number of transactions, can lead to "paralysis" of operational work in the company and in this case, company shareholders will carry out operational management of the company instead of making decisions only on key and strategically important issues.

   On the other hand, charter with the general wording regarding the prior approval of shareholders on certain types of transactions may still allow general director to conclude transactions at a loss of the company that in fact shall be subject to the preliminary approval of the shareholders.

B. Another way control of the activities of the general director is establishment of the short term of his appointment. For instance, the company's charter may establish that the general director of the company shall be appointed for a year. At the end of this period, the shareholders of company at the general meeting upon evaluation of performance of the general director may adopt decision regarding prolongation of the powers of the general director for another term or may dismiss him.

C. The practice of appointing two or more general directors to manage a company (the so-called "two keys" principle) is relatively new to Russian legislation[5]. The obvious advantage of appointing two or more general directors to the company is that each of the general directors has the right to control the activities and decisions of the other general director and at the same time can direct the company's activities for the benefit of the shareholders who have appointed him.

   However, following points shall be regarded. In case the shareholders of the company establish that all general directors are obliged to act jointly, this means that the signatures of all the general directors are required to make any decisions on the company's current activities. This mechanism may be cumbersome and difficult to use because it can "slow down" the operational solution of issues.

   Also, if the company's charter contains a division of powers between general directors, in this case the difficulty of applying the "two keys" principle may arise for the counterparties of such a company. As a rule, counterparties shall carefully review the charter and other internal documents of a company to make sure that signer general directors have the authority to conclude a particular transaction.

   Unfortunately, present legal control mechanisms do not always allow shareholders to quickly get information regarding current status of the company and regarding the decisions adopted by the general director.

3. FORMS OF RESPONSIBILITIES OF THE GENERAL DIRECTOR

If the shareholders of the company suspect that the general director has committed actions to the detriment of the interest of the company, shareholders may hold the general director accountable.

For instance, if the property losses are resulted due to the fact that the company was brought to administrative or civil liability and imposed a fine, the company shareholders have the right to recover a specific amount of the fine directly from the general director[6].

1 Federal Law dated 08.02.1998 No. 14-FZ "On the limited Liability companies", art. 40
2 Federal Law dated 08.02.1998 No. 14-FZ "On the limited Liability companies", art. 40
3 Federal Law dated 08.02.1998 No. 14-FZ "On the limited Liability companies", art. 44
4 Federal Law dated 08.02.1998 No. 14-FZ "On the limited Liability companies", art. 45, 46
5 Civil Code of the Russian Federation, art. 53, 65.3
6 Civil Code of the Russian Federation, art. 15

Moreover, the activities of the general director can lead to the fact that the company loses its position in the market, the customer base, sales. In such circumstances shareholders would like to hold the general director accountable too. However, in practice it is next to impossible to held general director accountable to recover profit loss.

CONCLUSION

Currently, Russian corporate law does not provide, effective mechanisms that would allow company shareholders to control the activities of the general director quickly and effectively. The broad powers of the general director are not comparable to his limited liability. Accordingly, company shareholders are recommended to regularly monitor the current activities of the general director to avoid losses that may arise due to incompetent or malicious actions of the general director. In addition, the shareholders of the company may apply abovementioned control mechanisms over the activities of the general director to mitigate potential risks.

RISKS OF FRAUD IN CONDITIONS OF CORONAVIRUS CRISIS. IMPLICATIONS ON AUDITING.

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Audit Director

ABSTRACT

Fraud issues became more actual in ongoing pandemic's unprecedented expansion. This creates new opportunities to commit fraud and make companies more vulnerable to corporate failure. Auditors' assessments and responses to risks of financial statements misstatement due to fraud are critical to audit quality. Therefore, examination of non-financial measures deserves more attention from the auditors. These ones are difficult to manipulate and should be used along with financial measures.

Key Words: Audit, Analytical Procedures, Risk Assessment, Risk of Material Misstatement in the Financial Statements, Fraud, Non-Financial Measures.

INTRODUCTION

Fraud is a serious, and sometimes underestimated, issue that causes irreversible harm to people, companies and economy. Its consequences can weaken the public's confidence in markets and have long lasting damaging effects on society. Coronavirus crisis increased the pressure on companies due to restrictions in production, trade, consumption, travel bans, etc. These new circumstances may hamper internal control and risk management procedures and, thus, open new opportunities for committing fraud.

Auditors can play a crucial role in tackling fraud and stakeholders expect that auditors should be doing more or better in this area. For this reason, the auditors may need to rethink their traditional approaches to fraud risk assessment and make appropriate modifications/adjustments to the audit procedures.

1. FRAUD RISK

Two primary fraud categories are relevant for a financial statements audit:

i. assets misappropriation, which includes embezzling, stealing or misusing the company's resources by its management, employees, and/or third parties;

ii. fraudulent financial reporting, in which the offender intentionally causes a material misstatement or omission in the company's financial statements, such as reporting fictitious revenue or understating liabilities.

The distinction between these two categories is not always clear, and one may lead to the other. For example, stealing company's resources will most likely result in fraudulent financial reporting. We note that stakeholders are mainly concerned with the risk of fraudulent financial reporting that involves the company's management.

Considering the fraud risk triangle, the current environment provides the individuals with the incentives or pressure to perpetrate a fraud, an opportunity to commit it and a rationalization to justify a fraudulent action. With all of these factors, the risk of fraud is substantially increased. (see "The Fraud Triangle in the Context of COVID-19"[1] below).

1 *Ines Liu. Business Risk Management in China in the Era of COVID-19// China Briefıng Magazine, June 8, 2020.*

Incentives (pressure): As many businesses were economically affected, employees may have felt pressure to make fraudulent journal entries to sustain the company's viability. For example, if the company was on the verge of violating a loan covenant, there may have been pressure and incentive to misstate results to avoid that outcome. Employees may have also felt pressure if their personal financial situation worsened.

Opportunity: Breakdowns in internal controls over financial reporting may have presented opportunities for fraudulent financial reporting or misappropriation of assets. For example, if a client's accounting department was suddenly unable to access their office and many of their controls were manual, management may have overridden controls. In many cases, this reaction may have been well intentioned, however, auditors should approach management override with a healthy degree of professional skepticism.

Rationalization: An additional element required for fraud to continue over a period of time is the ability of the offender to rationalize the situation as being acceptable. Employees stealing from a company's petty cash box could rationalize these fraudulent activities as merely borrowing, with the intent of paying back the funds at a later date. Management team may adjust reported earnings for a few months during mid-year, expecting that the sales will rise towards the end of the year, allowing them to eliminate the adjustments by year-end.

Fraudulent financial reporting is fraud that involves intentional misstatements, including omissions of amounts or disclosures in financial statements, made with a view to deceive users of those statements. The year 2020 brought the uncertainty, which made the following main types of financial manipulation more actual in the current situation than ever:

- recognition of income or expenses in later periods;
- recognition of non-existent income transactions;
- understatement of liabilities and /or expenses;
- overstatement of assets;
- non-disclosure of related party transactions;
- manipulations with accounting estimates (associated with revenue recognition, allowance for doubtful accounts, goodwill or intangible assets, etc.).

Identifying these types of fraud risks can be a challenge for the auditors. The evolving environment requires auditors to consider if the design and implementation of their usual responses to the identified risks are still relevant. In many cases, they should implement alternative procedures to obtain sufficient and appropriate audit evidence. It is also crucial to document under which circumstances these procedures have been performed.

2. AUDIT CONSIDERATIONS

Auditors' assessments and responses to risks of financial statements misstatement and fraud are critical to audit quality. Risk assessments in the current environment became different, as clients are dealing with significant changes to their businesses, the work environment, and the economy overall as a result of COVID-19. Despite the added complexities, auditors must continue to focus on high-quality audits that fully comply with standards for objectivity and professional skepticism. Auditors should recall the objectives of international standard on auditing ISA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", paragraph .10, which are as follows:

i. to identify and assess the risks of material misstatement of the financial statements due to fraud;

ii. to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud through designing and implementing appropriate responses; and

iii. to respond appropriately to fraud or suspected fraud identified during the audit.

While developing the audit strategy and plan, the auditor and the key members of the engagement team discuss the susceptibility of the company's financial statements to material misstatement. A particular emphasis is placed on how and where the company's financial statements may be subject to material misstatement due to fraud. Based on their risk assessment, auditors design and perform procedures which take into account materiality and sampling methodologies.

When identifying and assessing the risks of material misstatement due to fraud, auditors presume that there are risks of fraud related to revenue recognition as required by ISA 240[2]. Based on this presumption, they evaluate which types of revenue transactions or assertions give rise to such risks. In addition, management can override controls in unpredictable ways. Hence, ISA 240 requires auditors to consider this as a risk of material misstatement due to fraud and thus as a significant risk[3].

Auditors should incorporate an element of unpredictability when performing audit procedures in response to identified risks related to fraud. For instance, auditors could perform substantive procedures on selected account balances and assertions not otherwise tested due to their materiality or risk. Auditors could also adjust the timing of audit procedures from that otherwise expected. Another option could be to use different sampling methods or test an entire population, which could help provide sufficient appropriate audit evidence to support the opinion.

As long as auditors perform their engagements for clients impacted by the pandemic, remaining vigilant and skeptical will help to ensure the objectives of ISA 24 are met.

MORE ATTENTION TO NON-FINANCIAL MEASURES

ISA 240 states that the risks of material misstatement due to fraud may be indicated by unusual or unexpected relationships identified through performing analytical procedures[4]. Analytical procedures designed to assess the risks of material misstatement due to fraud are covered by ISA 520 "Analytical procedures". The standard recommends analytical procedures, such as comparing current period financial and other information with previous periods data, comparing the actual results with the expected ones (i.e. estimates or forecasts, auditor's assumptions), comparing financial and other information with the results reported by other companies in similar markets (i.e. comparing the profitability of the audited company with other companies of similar size in the same industry), etc.[5]

Analytical procedures are diverse and highlighted in the works of such authors as Roxas M.L.[6], Dechow P.M.[7], Spathis C.T.[8], Alekseev M. A., Dudin S. A[9], Glinsky V. V.[10]

However, it should be noted that dishonest management of the company, when it intentionally misstates the financial statements, may also mispresent certain financial indicators in order to ensure that the control ratios indicating the integrity of the financial statements remain as acceptable. For example, when the management of the company overstates the reported sales in order to demonstrate the achievement of budgeted results, they may also overstate the cost of sales in such a way that the change in profit sales looks reasonable.

2 *ISA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", par. 26.*

3 *ISA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", par. 31.*

4 *ISA 240 "The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements", par. 22.*

5 *ISA 520 ""Analytical procedures", par. A1.*

6 *Roxas M.L. Financial Statements Fraud Detection Using Ratio and Digital Analysis // Journal of Leadership, Accountability and Ethics, 2011, Vol. 8(4), p. 56-66.*

7 *Dechow P.M., Ge W., Larson C.R., Sloan R.G. Predicting Material Accounting Misstatements // Contemporary Accounting Research, 2011, Vol. 28, № 1, p.17-82.*

8 *Spathis C.T. Detecting False Financial Statements Using Published: Some Evidence from Greece // Managerial Auditing Journal, 2002, Vol. 17, № 4, p. 179-191.*

9 *Alekseev M. A., Dudin S. A. The indicators detecting misstatements in results of the company's activities / /Vestnik IPB (Professional accountants magazine), 2017, № 6.*

10 *Alekseev M. A., Glinsky V. V. Assessment of probable misstatements in the financial statements / M. A. Alekseev, V. V. Glinsky, L. K. Serga, M. L. Pyatov / / statistical issues, 2019, № 7.*

In this regard, a number of authors (Amzelt A. G.[11], Arzhenovsky S. V., Bakhteev A.V.[12], J.F. Brazel, K.L. Jones, M.F. Zimbelman[13], C. Ittner and D. Larcker[14]) suggest to use non-financial measures along with financial ones when performing risk assessment analytical procedures. Non-financial data are difficult to manipulate, or at least such manipulations are difficult to hide. In the work of J. F. Brazel, K. L. Jones and M. F. Zimbelman, it is noted, for example, that there is a relationship between the revenue trends and changes in non-financial indicators, such as the number of employees, the number of retail outlets, the number of distribution centers of the company, etc.

Non-financial measures are encouraged by accounting standards and many auditors today do use them as part of their analytical procedures. Though non-financial measures were not typically used by auditors 10 years ago, J. F. Brazel says, about 50% of all auditors use them in some capacity today. But still, that leaves about half of auditors who do not use these measures and who may be missing inconsistencies or failing to detect fraud at public companies.

Auditors tend to avoid looking at non-financial information because of time constraints and other job pressures, or because their focus is elsewhere. But J. F. Brazel and others say fraud is easier to detect with non-financial measures because this data is disclosed in a public company's annual filings, and companies that commit fraud often fail to hide the non-financial evidence of their wrongdoing.

Therefore, the auditors should be more focused on examining non-financial measures when performing risk assessment analytical procedures, especially it is actual in ongoing pandemic in order to efficiently detect the cases of fraud. Auditors who only examine financial data may be missing some important clues.

Experts offer the following tips for using non-financial measures in audit:

<u>Determine the most risky areas in the client's business.</u> For instance, the area of greatest risk could be revenue or receivables. Once you determinetheriskarea,figureoutthekeynon-financial indicators pertaining to such an area.

<u>Incorporate non-financial measures into the planning and analytical steps of an audit.</u> While it is a given that non-financial measures should be used, auditors should expressly include them in the planning and substantive testing stages of the audit.

<u>Go a step further than the obvious.</u> If you know a company produces 100 000 product items per year, find out how they produce that number of items and on how many machines. Non-financial information can help auditors understand the client, the business, the industry that business operates in, and the economic environment.

<u>Look for all relevant information</u>. Ask for the records you need in order to gather all information that could impact your audit.

<u>Finally, look for glaring inconsistencies.</u> For example, if revenue growth is exceeding the growth in the operational data by 20% or more, our research says that while it may not be fraud, it is something to look into.

CONCLUSION

The first anniversary of the outbreak of the pandemic has passed. However, increased risks and opportunities of fraud still exist, as well as the pressure on auditors, who are under increased control of the regulators. In such circumstances, it is important to keep in mind the main types of fraud listed above, and apply professional skepticism in developing efficient audit procedures aimed at detecting such phenomena.

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12 *Arzhenovsky S. V., Bakhteev A.V. The risk of falsification of financial statements and its assessment during the audit. - Rostov-on-Don.: RSEU (RINH), 2017, p.104.*

13 *Brazel J.F., Jones K.L., Zimbelman M.F. Using non-Financial Measures to assess fraud risk / Journal of Accounting Research, 2009, Vol. 47, № 5, p.1135-1166.*

14 *Ittner C. and Larcker D. Are Nonfinancial Measures Leading Indicators of Financial Performance? An Analysis of Customer Satisfaction // Journal of Accounting Research, 1998, Vol. 36, p.1-35.*

MOROCCO

ABOUT NAZALI MOROCCO

Started providing services in January 2020 at Casablanca office, Nevados Morocco Consultancy Sarl Au is one of the first abroad offices of NAZALI.

With its sound experience in tax and legal area, NAZALI Morocco team works with many local and international companies in the field of, amongst others: Tax, Legal, Accounting, Corporate Governance, Customs, Foreign Exchange Office, Litigations and M&A.

NAZALI Morocco aims to collaborate with clients closely in country's challenging tax and legal environment so they can concentrate on their daily business activities in the market. NAZALI provides assistance to the clients in a comprehensive way of whole regulations to assure that necessary measures have been taken on time as well as corrective actions on ongoing issues.

NAZALI Morocco is headed by Ms. Esma Parmak Kahraman as a Partner and Managing Director. Esma is an expert in taxation, financial reporting and audit and has gained a considerable experience in local and international taxation, tax inspection, transfer pricing and audit in different countries. With her knowledge on Morocco and Algeria and with her experienced tax and legal teams, Esma is assisting local and international companies for their investment journey in Morocco, from company set-up to investment planning, mergers and acquisitions, tax inspections and day-to-day businesses. Esma is a Certified Public Accountant, Independent Auditor and has a Certificate of Risk Management Assurance (CRMA).

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CURRENT NEWS ABOUT MOROCCO

» Morocco: law 88-17 overcame waiting times and the use of paper at the trade register

From next September the 3rd, the process regarding any declaration to the register of commerce (regarding the changed concerning the commercial activity) shall be done only electronically through a digital platform created by law n° 88-17.

Creation of new companies and deposit of the annual financial statements shall be done through this electronic platform as well.

The law n°88 – 17 provides that all the taxes related to the declarations shall be paid electronically as well.

An updating of the model forms to be attached to the declarations file subject to the formality also took place and has been published.

The register of commerce is intended to make known the existence, the characteristics and the corporate information regarding a commercial activity in order to inform third parties (any person can request the communication).

In addition of the above, the information contained in the register of commerce is updated by the persons in charge of the commerce activity through declarations regarding the changes occurred in the activity, the governance, the head office... of the commercial activity.

» Morocco: Maintaining of the central bank's policy rate at 1.5% and presentation of other key indicators

The Board of Bank Al Maghrib, the Moroccan central bank, has decided to keep its policy rate at 1.5%. This decision follows an analysis of the health and economic situation's evolution, both nationally and internationally, as well as its macroeconomic projections over the medium term.

Bank Al Maghrib also estimated that the recovery in activity is continuing at a sustained pace, helped by easing restrictions, accommodating financing conditions, and the tax stimulus.

The Board has also noted that after reaching rates of 0.7% in 2020 and 0.1% in the first quarter of 2021, inflation averaged 1.7% during April and May. Given the expected rise in international oil and certain food prices and the improvement in domestic demand, it should continue to accelerate while remaining at moderate levels, standing at 1% on this year as a whole, and 1.2% in 2022.

For the current year, the central bank forecasts growth to reach 5.3%, driven by a 3.6% increase in the value added of non-agricultural activities and a 17.6% rebound in those of the agricultural sector.

In terms of external accounts, after a notable attenuation to 1.5% of GDP in 2020, the current account deficit would end the year at 3.8% of GDP before easing to 2.6% in 2022.

PRIOR TRANSFER PRICING AGREEMENT IN MOROCCO: PROCEDURE & ANALYSIS

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ABSTRACT

As part of Morocco's efforts to ensure a favorable tax environment for attracting and retaining foreign investors, the Moroccan general tax code introduced in 2015 the possibility of concluding a prior agreement on the price of transfer with the tax administration.

Indeed, even in the presence of documentation justifying the transfer pricing policy adopted, the companies of multinational groups are not certain of escaping a possible disagreement with the inspectors during tax audits. The conclusion of a prior agreement therefore remains the best way to protect against the tax risks arising from transactions carried out with associated companies.

Key Words: Transfer Pricing, Advanced Pricing Agreement (APA), TP Documentation.

INTRODUCTION

In an era of globalization, multinational companies are more and more tempted to optimize their after-tax profits by shifting their revenues to territories presenting advantageous tax regimes. In order to do this, acting on the prices adopted in the framework of cross-border controlled transactions between related companies remains one of the most widespread tax avoidance games. This practice usually takes the form of the application of exaggerated prices to the expenses borne by group companies located on high tax countries in order to shift the profits to low tax countries, or tax heavens.

This manipulation of tax results can be achieved by exploiting one or many of the following mechanisms[1]:

- Making entities located in countries with high taxation bear excessive or fictitious management fees and/or royalties.
- Reducing or increasing the prices applied to goods and services transferred between related entities;
- Applying reduced or increased rates to the interests paid on intercompany loans;

However, to prevent such profit erosion on its territory, Morocco, like many tax legislations all over the world, has introduced the obligation for companies belonging to international groups, which carry out transactions with other group companies, to document their transfer pricing policies, and to prove their respect of the arm's length principle.

Indeed, by virtue of the supervisory power conferred on the tax administration, tax inspectors are entitled to request, during tax audits, the documentation justifying the relevance of the transfer prices applied by certain companies meeting specific criteria, which have direct or indirect dependency links with companies located outside of Morocco and with which they carry out transactions. Companies failing to meet this obligation may incur a fine equal to 0,5% of the covered transactions' amount, which minimum cannot be less than two hundred thousand dirhams (MAD 200K) per financial year concerned, and also have their tax basis reassessed.

Notwithstanding the presentation of the said documentation during a tax audit, the Moroccan tax administration still have the right to adjust the audited company's tax basis in case they question the relevance and accuracy of the adopted transfer pricing methods.

Companies that have priorly concluded an Advanced Pricing Agreement with the tax administration, can however be guaranteed that the methods they employed to determine their transfer prices will not be call into question during a tax control for the fiscal years covered by the Advanced Price Agreement, as long as the entity complies with the agreed method and the obligations contained in the Advanced Price Agreement, and that the latter is established based on sincere and truthful information.

1 *Detailed in circular note 717 from the Moroccan tax administration, published on May 24, 2011*

PROCEDURE AND ANALYSIS

In order to reduce the risk of being subject to adjustments during a tax audit, the General Tax Code [2]provides for the conclusion of Advanced Pricing Agreement between the taxpayer and the tax administration. This procedure[3] allows the company to discuss the strategy adopted for determining its transfer prices with the tax administration, as well as every useful information justifying its choice of the pillars on which its policy would be based.

The submitted file is qualified as a basis for the discussions between the applicant company and the tax administration. However, the arrangements and assumptions advocated by the company may be amended during the negotiations.

To this end, the decree setting the procedure for the conclusion of the said Agreement, and the circular note[4] published by the General Directorate of Taxes, presents the necessary stages for fulfilling this procedure, which are as follows:

1. Submission of an application at least six months before the opening of the first financial year covered by the Advanced Price Agreement, at the initiative of the taxpayer, with the possibility of a preliminary meeting with the competent service of the tax administration;
2. The request must specify certain information such as:
   a. The associated companies linked to the applicant company;
   b. The transactions subject to the Advanced Price Agreement;
   c. The duration of the Advanced Price Agreement within the limit of 4 years;
   d. The method advocated for determining transfer prices and its key assumptions.
3. The request must be accompanied by the necessary documentation for its study by the tax administration, in particular:
   a. The general business environment of the associated companies;
   b. The existing contractual agreements between the associated companies;
   c. The Advanced Price Agreements concluded between the applicant company with other foreign authorities as well as the tax consultations established by the latter;
   d. Any other relevant information.

Further to the discussions, the tax administration adopts a position on the transfer pricing method proposed by the taxpayer, which is subsequently notified in writing.

In addition, it should be reminded that filing a request for an Agreement does not automatically give rise to a tax audit, nor to its impediment, and also that the Advanced Price Agreement is qualified as null in the two (2) cases detailed in the 2nd paragraph of the General Tax Code's article 234 stipulating that "*… However, the agreement is considered null and of no effect since its date of entry into force in the following cases:*

- *Misrepresentation of facts, concealment of information, errors or omissions attributable to the company;*
- *Failure to comply with the agreed method and the obligations contained in the agreement by the company or the use of fraudulent maneuvers.*"

2 *Article 234 bis of the General Tax Code*
3 *Decree n° 2-16-571 of Chaoual 8, 1438 (July 3, 2017)*
4 *Circular note n° 36/2018 D.L.E.C.I of December 14, 2018*

After to the acceptance of the Advanced Price Agreement's terms by both parties, the applicant company must produce an annual report[5] and submit it to the tax administration, based on which the latter will ensure the compliance of the applied methods to the terms of the Advanced Price Agreement. This report must contain[6]:

- *"A detailed statement of the calculation of the transfer prices provided for in the Advanced Price Agreement;*
- *A summary statement of any changes brought to the conditions under which the transactions covered by the Advanced Price Agreement are exercised;*
- *A copy of the organizational structure of all the associated companies and their legal ties as well as their capital's distribution;*
- *A copy of the associated companies' annual activity report."*

CONCLUSION

The adoption by the OECD member countries of the arm's length principle for intra-group transactions aims to avoid the outburst of conflicts between the involved tax administrations for the distribution of multinational groups' worldwide results.

To this end, concluding an Advanced Price Agreement remains the best solution both for companies and tax administration in order to overcome the uncertainty arising from the adoption of transfer prices.

Although the procedure for concluding an Advanced Price Agreement can be long and pricey for both parties, its adoption remains advantageous compared to the financial consequences resulting from the rejection by the tax administration of the applied transfer pricing methods in case of a tax audit.

Finally, it is highly recommended to carry out an in-depth tax audit before embarking on the process of concluding an Advanced Price Agreement in order to detect and assess the tax risks relating to the previous years that are still open for a tax audit, and for which the tax administration could adjust the used transfer prices.

5 *Article 6 of decree n° 2-16-571 of Chaoual 8, 1438 (July 3, 2017)*
6 Ibid, Article 7

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LAUNCH OF PAYMENT ORDER PROCEDURE: THE MOST EFFECTIVE REMEDY AGAINST BAD DEBTORS UNDER MOROCCAN LEGISLATION

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ABSTRACT

Since its reform of by Law 1-13 in 2014, now in Morocco the Payment Order is the most successful payment procedure due to the speed, flexibility and efficiency that characterize it. However, few conditions limit its scope of application." would be more clear

Key Words: Payment Order (PO), Recovery Procedure, Creditors, Bad Payers, 2014's Reform.

INTRODUCTION

In everyday life, we as creditors may be confronted to bad payers. In such cases, it is necessary to recover the debt by legal means. If the debt is disputable and its existence is questionable, the creditor is obliged to follow up the recovery action before the trial court.

But if the debt is payable and its existence is established, in particular as regards its amount, by a written document (contract, invoice, etc.), the Payment Order (PO) remains a strategy of first choice to force the debtor to clear his debt.

The PO is a very simple way of recovering a debt. It is quick and inexpensive.

This procedure is non-adversarial, not requiring the appearance of the parties or the defendant. It can be used in civil or commercial matters. Once notified to the debtor, it becomes adversarial if the debtor objects the PO.

The PO's regime was established for the first time in Morocco by the Cherifian Dahir dated 20 January 1951, which was revised by the Dahir of 27 July 1970, itself modified by the Dahir of 28/09/1974 known as the code of civil procedure (CCP) where it is governed by articles 155 to 165.

What are then the characteristics of this procedure, its objectives and conditions, to whom it is introduced, how it is notified and enforced, what recourse is available, what difficulties the enforcement of an order for payment may face?

We propose to deal with these questions along two lines:

- The conditions of the PO's procedure and with whom it is lodged;
- The remedies against the PO and Its enforcement.

1. THE CONDITIONS OF PO PROCEDURE AND COMPETENT COURT

The PO is an exceptional recovery procedure that requires a series of formal and substantive conditions to be met.

A. Conditions of admissibility of the application

1.1. Formal requirements

According to the provisions of Article 156 of the CCP, the formal requirements for lodging a PO are:

- The presentation of a written request, by the claimant or his representative, including the last names, first names, profession and domicile of the parties, the precise indication of the sum requested and its cause. If one of the parties is a legal person, the request should include: the company name, legal form and its registered office.

- In support of this request, the title justifying the validity of the claim must be produced.
- It should be emphasized that the application should be submitted by a lawyer, in accordance with the provisions of law[1] establishing the commercial courts, and provisions law [2] of the statute of the lawyer,
- The presentation of the application for a PO should be accompanied by as many copies as there are defendants, and this is not so that the application is notified to the other parties for their response, the PO not being an adversarial procedure, but so that the secretariat of the court clerk's office can notify each debtor of the PO pronounced[3]
- According to the established case law, the failure to respect this condition does not prevent the admission of the application and the condemnation of the injunction, but the fact of notifying the injunction to pay without attaching the copy of the application is vitiated by a formal defect and consequently by the nullity of the notification
- The presentation of the debt instrument justifying the request, so request should be accompanied by a certified copy of the original[4].
- The payment of the judicial tax: according to the provisions of Law no. 1-13 on the payment order procedure law, only the requests for payment of a sum of money higher than MAD 5.000, due by virtue of a debt instrument or a recognized promise, can be subject of a PO, contrary to the former text which fixes this amount to a sum of money higher than MAD 1.000. The corresponding judicial fee is MAD 100.

1.2. SUBSTANTIVE REQUIREMENTS

Articles 155 and 157 of CCP as amended by Law no. 1.13 summarize the substantive requirements of the PO procedure as follow:

- The application should relate to a demand for payment of a claim, and cannot relate to an order to do or not to do;
- The value of the claim exceeds MAD 5.000 for civil courts and MAD 20.000 for commercial courts;
- The claim that is the subject of the application:
  - Should be written and subject to an established debt instrument;
  - Should not be time-barred or extinguished;
  - Should be certain (its existence must be incontestable);
  - Should be liquid (its amount should be assessable, (articles 155, 157 CCP)); and
  - Should be payable (it should be due).
- The debtor should not be subject to judicial liquidation proceedings. (Art 653 CCP);
- The debtor should have a known domicile in Morocco.

B. THE COMPETENT COURT

1 *See article 13 of Commercial Courts Regulations: "the commercial court shall be seized by a written application signed by a lawyer registered with the roll of one of the bars of Morocco"*

2 *See article 31 of the Lawyer statute law "Only lawyers registered with the roll of the bars of the Kingdom are authorized, in the context of representation and assistance of the parties, to present requests, conclusions and defense briefs in all cases except for criminal cases, alimony cases before the courts of first instance and the courts of appeal and cases that fall within the jurisdiction of the courts of first instance in the final instance*

3 *See article 160 of the code of civil procedure (hereinafter 'CCP')"The decision of condemnation is notified to the defendant who must, within eight days of this notification, pay the amount of the condemnation, under penalty of being forced to do so by all legal means, in particular by seizure of his movable faculties"*

4 *See article 1 of Law no. 1-13 on the payment order procedure law "In support of this request must be produced the title justifying the validity of the claim"*

The jurisdiction of the court is defined as follows.

1. **The amount of the claim**

- less than MAD 5.000: the local courts[5] have jurisdiction;
- more than MAD 5.000: the President of the Court of First Instance or the judge he appoints to deal with PO;
- more than MAD 20.000 of a claim arising from a commercial transaction.

2. **The nature of the claim**

- The first instance courts are competent to hear civil and commercial claims of less than MAD 20.000;
- The commercial courts are competent to deal with commercial debts exceeding MAD 20.000.

Contrary to the above, the procedure cannot be applied for the payment of any claims in the penal sense, the payment of damages for non-performance of a contract or the restitution of a deposit paid after an agreement resolution. The payment of an unfunded cheque cannot be recovered by means of the payment order procedure since a specific procedure is provided for in the criminal code.

3. REMEDIES AGAINST THE PO AND THE EXECUTION OF THE PO

The PO procedure also presents a particularity even for the (A.) remedies and for the (B.) enforcement.

A. REMEDIES

The application for a PO can have several outcomes. It can be either:

- Rejected: the rejection decision is reasoned and refers the claimant to the court in accordance with the ordinary law. No appeal may be lodged against the decision to reject the application; or
- Partially rejected: the president of the court will only validate part of the claimant's claims. The creditor will then either have to accept this decision and notify the order for the part admitted or abandon the order for payment procedure and start a new procedure under ordinary law; or
- Fully accepted: the judge will issue a decision in the form of an order for payment. The judge orders the debtor to pay the principal and interest, plus any costs, accessories and expenses (court fees, service of process, etc.).

The convicted debtor is entitled to contest the PO by way of opposition. No reasons need to be given for the opposition decision at the opposition statement. The debtor will have to prove the basis of his claim at the adversarial hearing, which means that the Debtor should present the proof in support of his opposition. The debtor has 8 days from the notification date of the decision by a bailiff to bring an action before the court that issued the order to defend himself.

The opposition is made by a declaration filed at the clerk's office of the court that issued the decision. It should be accompanied by the order and the supporting documents substantiating the debtor's opposition.

The parties will then be summoned to resolve the dispute. If a solution is found, the new judgment will replace the notified order. The latter will lapse.

If within eight days of notification in person or at home the debtor has not complied with the request or lodged an appeal, the order becomes enforceable by virtue of law. Where the claim is based on a bill of exchange, the order shall have all the effects of a protest against the bearers and endorsers

If the creditor or debtor does not agree with the new decision, he has the following means of appeal:

- Appeal of the decision before the first instance court for claims of less than MAD 20,000 and before the Court of Appeal;

5 *The local court is a court created by law 42.10, in order to decongest the courts of first instance adopted in 2011, the local judge does not judge in cases such as real estate, social, family, ...*

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- In other cases, the matter must be referred to the Court of Cassation.

B. ENFORCEMENT OF THE DECISION

If the debtor makes no opposition following the PO notification, he should then proceed with the debt payment (under cover of the enforcement formula affixed by the clerk of the court, which gives the decision its final value).

The PO enforcement can only be done by a bailiff, who is the only one competent to proceed with the contentious recovery of a debt.

In practice, it is advisable to obtain a certificate from the court clerk's office that has issued the order to pay that there are no objections or appeals against the decision to be enforced and then to request an enforceable copy of the sentence that has been issued, which is the basis for any enforcement action.

The enforcement of the award may be delayed due to enforcement difficulties. The president of the court is then competent, in his capacity as interim relief judge, to deal with all difficulties relating to the enforcement of a judgment or an enforcement order.

It should be noted that this PO procedure was subject to inconsistencies in the case law regarding the statute of limitations for debts until 2017.

Indeed, in the absence of legislative provisions, the decisions rendered by the judges were based indifferently on the civil statute of limitations of 2 years or the commercial statute of limitations of 5 years. A lack of harmonization that the President of the Casablanca Court of Appeal decided to stop by sending a circular to the different jurisdictions of the economic capital. From now on, magistrates are required to implement the civil prescription, whatever the dispute character is.

CONCLUSION

From the above, we can easily say that the PO is a judicial recovery procedure whose relevance is undeniable, although its limitation to cases that meet the conditions set out in our study raises questions about the recovery methods used in other cases that do not fall within its scope, which continue to suffer from the slowness of the process, hence the need for the Moroccan legislator to devise appropriate recovery methods that are as effective as the PO.

ABOUT NAZALI UKRAINE

September 2020 marked NAZALI's presence in Ukraine as Kyiv office was opened.

For the past couple of years, Turkey has become one of the biggest trade partners of Ukraine. Turkish companies are actively investing in the Ukrainian market, especially in energy, infrastructure, construction, transport and agriculture sectors. Therefore, an availability of a reliable partner, which could guide the foreign investors through the constantly changing business environment, appears to be one of the key elements necessary to succeed in Ukraine.

At NAZALI Ukraine, we exercise strategic approach to deliver distinctively high degree of quality to resolve any legal challenges in the most efficient manner.

The main difference which makes NAZALI stand out from the rest of the Ukrainian market consultants is that we not only provide regular legal advice but also render services in the fields of tax, accounting and customs. The Ukraine's team is ready to provide high-quality consultancy services to all types of clients, which require provision of target-oriented solutions with consideration of each particular business strategies and work necessities.

NAZALI Ukraine's office is led by Mr Doğus Gulpinar, who previously advised foreign investors as a private practitioner, and later oversaw the Turkish desk in a reputable Ukrainian law firm. Mr Gulpinar's experience includes provision of legal services in the areas of energy, construction, real estate, and immigration law. Our mission, according to Mr Gulpinar, is not only to advise Turkish clients in Ukraine, but also to provide an opportunity to the local companies to commence their business in Turkey, as well as in other countries of NAZALI's presence.

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CURRENT NEWS ABOUT UKRAINE

» The Parliament of Ukraine Ratifies the Protocol to Amend the Double Taxation Convention between Ukraine and the Netherlands

The Protocol, signed on 13 March 2018, amends the Convention in order to bring its provisions into compliance with the OECD Model and to increase the rates of taxation of passive income in the source state.

The Protocol provides, in particular, for:

- taxation of dividends at the rate of 5% - if the beneficial owner is a company (other than a partnership) which holds directly at least 20% of the capital of the company paying dividends (the provision for taxation of dividends at the rate of 0% was excluded), and 15% - in all other cases;
- an increase in interest tax rate from 2% to 5%;
- an increase in royalty tax rate from 0% to 5% for the use of, or the right to use any copyright of scientific work, any patent, trade mark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience.

Apart from that, the Protocol introduces 'principal purpose test' which denies treaty benefits if the main purpose of a transaction is to obtain such benefits when they were not intended. The Protocol also introduces amendments aimed at enhancing the capacity of the competent authorities of the Contracting States to exchange tax information.

» Ukraine Approves Tax Amnesty Law

On 15 June 2021, Ukrainian Parliament adopted the Bill No. 5153 intended to stimulate de-shadowing of Ukrainian economy by allowing individuals to declare previously undisclosed assets with impunity.

The Bill provides for the opportunity to voluntarily declare personal assets with paying one-time (special) fee to the budget and thus be pardoned for tax and currency control offenses with respect to such assets. Declaration timeframe is from 1 September 2021 to 1 September 2022.

The reportable assets will be imposed with special fee at the rate from 2.5% to 9% depending on circumstances.

Under-aged individuals and high-rank public officials may not enjoy the tax amnesty.

The Bill also provides for declaration through an authorized representative, i.e. Ukrainian notary, without disclosing the identity of an applicant.

The Bill is currently awaiting the President's signature.

INDIRECT ALIENATION OF SHARES IN UKRAINIAN 'IMMOVABLE PROPERTY-RICH' COMPANIES BY TAX RESIDENTS OF CYPRUS

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ABSTRACT

The article provides a brief overview of the tax consequences of indirect alienation of shares in Ukrainian 'property-rich' companies by tax residents of Cyprus, with particular emphasis made on difficulties arising in the course of interpretation of the relevant double taxation agreement.

Key Words: Alienation of Shares, 'Property-Rich Companies', Withholding Tax (WHT), Double Tax Treaty interpretation.

INTRODUCTION

In 2019, Ukrainian tax legislation experienced significant revamp as a result of joining international anti-BEPS agenda followed by adoption of new international tax rules. Along with introduction of anti-tax avoidance and evasion measures, certain provisions aimed at 'redistribution' of taxing rights between jurisdictions were implemented.

Among others, Ukrainian source taxation rules with respect to alienation of shares in Ukrainian residents were significantly revised.

The previously existing rule that allowed Ukrainian jurisdiction to tax capital gains from alienation of shares in Ukrainian entities was significantly broadened to cover 'indirect holding' whereby disposal of shares in non-residents became taxable under certain circumstances.

In particular, capital gains derived by a non-resident from alienation of shares became subject to Ukrainian withholding tax if the shares being disposed derived their value, directly or indirectly, from immovable property located in Ukraine at any time during the 365-day period prior to such alienation.[1] The relevant mechanism has also been introduced that enables to collect the Ukrainian withholding tax (WHT) due in cases of both direct and indirect alienation.[2]

The article examines how this new rule applies to alienation of shares by tax resident of Cyprus in light of application of the relevant double-tax treaty, as well as points on certain technicalities that arise in the course of such application.

Consideration of Ukraine-Cyprus case is of particular relevance as using Cyprus holdings in international structures by Ukrainian businesses is quite popular.

1. UKRAINIAN DOMESTIC RULES WITH RESPECT TO ALIENATION OF SHARES BY NON-RESIDENTS IN UKRAINIAN 'PROPERTY-RICH' COMPANIES

As per the amendments to the Tax Code of Ukraine taking effective on July 2020, capital gains from alienation of shares or other participatory interests in non-resident entities that at any time during 365 days prior to their disposal derive 50% or more of their value from shares (other participatory interests) in a Ukrainian legal entity, and, at any time during 365 days before disposal, the value of shares, participatory interests in Ukrainian legal entity derive 50% or more of their value from immovable property located in Ukraine (owned or leased by Ukrainian legal entity) are considered taxable in Ukraine under standard 15% withholding tax rate.

1 Item 'e' of Article 141.4.1 of the Tax Code of Ukraine (the 'TCU') (with the relevant changes effective as of July 2020)

2 Art.141.4.2 of the TCU (with the relevant changes effective as of July 2020), whereby a non-resident that acquires shares in Ukrainian property-rich company from other non-resident shall register with the Ukrainian tax authorities prior to such acquisition, withhold the Ukrainian tax due and remit it to the budget.

The value of shares in Ukrainian entity and the value of real estate should be determined based on their largest balance sheet value in financial accounting at any time during 365 days preceding the alienation. The value of shares in a Ukrainian entity as well as the real estate value should be compared with the balance sheet value of other assets based on financial accounting of a Ukrainian entity.

The real estate test prescribes that the largest balance value of real estate any time within the last 365 days should be determined and compared with the balance value of the total property (assets) based on balance sheet data. The real estate to be considered also includes the leased immovable property based on balance sheet data.

New Ukrainian WHT rules related to transfers of shares in real estate rich Ukrainian companies are associated with a number of uncertainties. As a result, multiple interpretations and different approaches to calculation are possible, and no statutory guidance is currently available. For instance, it is not clear whether the real estate should conclude unfinished construction. It is also obviously burdensome to check whether the real estate test is satisfied on a day-by-day basis; therefore, whether it would appear sufficient for entities to apply sample testing (on a quarterly basis).

Due to quite recent introduction of new rules, there is no practice of their application so far and very limited guidance from the tax authorities which triggers uncertainties, which will be discussed further.

2. APPLICATION OF UKRAINE-CYPRUS DOUBLE TAX TREATY

As it reads starting November 2019, Article 13 of Ukraine-Cyprus double-tax treaty provides for different tax treatment of capital gains realized by a resident of either contracting state from alienation of shares depending on whether such shares derive more than 50% of their value (directly or indirectly) from immovable property located in the other contracting state.

More specifically, gains derived by a resident of a contracting state from the alienation of shares deriving more than 50 per cent of their value directly or indirectly from immovable property situated in the other contracting state may be taxed in that other state.[3]

Given the above, as a general rule, capital gains realized by an entity- tax resident of Cyprus from alienation of shares that derive their value from immovable property located in Ukraine, shall be subject to 15% Ukrainian WHT.

Meanwhile, Para 5 of Article 13 provides for the so-called 'saving clause' and stipulates that Para 4 above shall not apply to income from capital gains realized from alienation of shares in immovable property-rich companies, when the immovable property from which shares derive their value is immovable property in which the business is carried on.[4]

Since the treaty does not indicate which immovable property should be regarded as used for commercial activities, the relevant clarifications are to be inferred from the Ukrainian legislation. The tax authorities also clarified that the provisions of the Tax Code of Ukraine are to apply for the interpretation of this expression. In particular, if real estate is used in transactions of taxpayers involving the production and/or sale of goods, performing services, works, as well as aimed at receiving taxable income, such real estate should qualify as corresponding to real estate within the meaning of the treaty for the purposes of application of the exemption of the capital gains derived by a resident of Cyprus from the alienation of shares in a Ukrainian real estate-rich company.

That said, the approach towards defining which immovable property is to be regarded as 'in which the business is carried on' is rather uniform and, as a general rule, does not pose any particular difficulties.

3 Para 4 of Article 13 of the Convention between the Government of the Republic of Cyprus and the Government of Ukraine for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income (the 'Convention') (as amended by the Protocol amending the Convention between the Government of Ukraine and the Government of the Republic of Cyprus for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income)

4 Para 4 of Article 13 of the Convention

For the rest of cases not covered by general rule of Para 4 as well as not falling within the case where immovable property is that in which the business is carried on, the treaty provides for the 'subject-to-tax' clause, whereby all capital gains not specified above derived by residents of Cyprus shall be exempt from Ukrainian WHT, provided such gains are subject to tax in Cyprus.[5] It is worth mentioning in this regard that this particular clause was subject to rather heated debate as the capital gains in question are not taxable in Cyprus, which makes them automatically subject to Ukrainian WHT – the result which was hardly intended by the Cyprus side.

Apart from misunderstanding raised in the course of negotiation of Para 6 of Article 13 above on whether all other capital gains not specifically addressed shall remain taxable in Ukraine (due to Cyprus waiving its taxing rights), in the course of practical application it appeared that seemingly obvious exception with respect to the immovable property in which business is carried on also lacks certainty.

Due to design flaws of the wording of the mentioned Article 13, which will be closer considered further in this article, there may be reasonable grounds to claim that there is no definitive answer that the fact that the immovable property in question is that in which the business is carried on would deprive the source jurisdiction of its taxing rights.

3. INTERPRETATIVE DIFFICULTIES INFERRED FROM THE TEXT OF ARTICLE 13 OF UKRAINE-CYPRUS DOUBLE TAX TREATY

As mentioned above, under Para 5 of Article 13 of the Ukraine-Cyprus DTT, by means of exception from Para 4 of Article 13 (a general rule which subject alienation of shares in Ukrainian 'real estate-rich' companies to Ukrainian WHT), Ukrainian withholding tax of 15% should not apply if the real estate is used for commercial activities.

It may be reasonably contended that by providing the exception from a general rule, the parties to the treaty reserved the right to tax the mentioned income only in Cyprus.

Such course of action to be followed in light of the intentions of the parties to exclude such gains from source state taxation, is also proposed by OECD. The relevant section of the OECD Commentaries on Article 13 reads as follows:

'*some States consider that the paragraph* [the general rule whereby the capital gains that derive (directly or indirectly) their value from immovable property located in a contracting state] *should not apply to gains derived from the alienation of shares of companies, or interests in entities or arrangements, … where the immovable property from which the shares or comparable interests derive their value is immovable property (such as a mine or hotel) in which a business is carried on*'.[6]

Although common sense might suggest that the only purpose of such a clause is to exempt such capital gains from source taxation, due regard is also to be had of the wording of the clause as it was formalized by the parties. The precise wording of Para 5 (b) of Article 13 is as follows:

'*Paragraph 4 does not apply to gains derived from alienation of shares …where the immovable property from which the shares derived their value is immovable property in which the business is carried on*'.

That is where the other interpretative approach lies. In their individual tax ruling, the Ukrainian tax authorities considered a situation where a tax resident of Cyprus disposed of shares in a Ukrainian real estate-rich company. A taxpayer sought advice on whether the fact that the immovable property was used in a company's business activity would exempt the realized gains from Ukrainian taxation.

The tax authorities opined that Para 5 of Article 13 did not exempt the mentioned capital gains from Ukrainian taxation but merely provided that such capital gains did fall within the ambit of a general rule of Para 4, whereby such gains are subject to taxation in Ukraine.[7]

5 *Para 6 of Article 13 of the Convention*

6 *OECD Model Tax Convention on Income and on Capital: Commentary on Article 13 para 28.7 (2017), Models IBFD*

7 *Individual tax ruling of the Ukrainian tax authorities No 4805/ІПК/99-00-05-05-02-06 dated 24 November 2020*

They further elaborated that if taxation of such gains was not covered by Para 4, then they shall inevitably be regulated by Para 6, under which all not aforementioned capital gains shall be exempt from taxation in Ukraine, provided such gains are taxable in Cyprus.

However, Para 6 of Article 13 clearly stipulates that it is only dealing with gains '*other than that referred to in paragraphs 1,2,3,4 and 5.*'

Having said that, Article 13, though intended to comprehensively cover taxation of capital gains, does not clearly distribute taxable rights between the two jurisdictions, which obviously leaves the issue unresolved.

It is also advocated by certain international tax scholars and practitioners that the recourse to Article 20 ('Other income') is to be had in order to define the taxing rights of the treaty partners, which in its turn would lead to the mentioned capital gain being exempt from Ukrainian WHT.

In the mentioned individual tax ruling, the tax authorities opposed to application of Article 20 as, given their way, due to the fact that the latter was only applicable to '*items of income not dealt with in the foregoing articles*', the issue of capital gains taxation should be ultimately resolved by Article 13. Meanwhile, such contention is not convincing and cannot be considered consistent: just like Article 20 applies to '*items of income not dealt with in the foregoing articles*', Para 6 of Article 13 applies to the capital gains other than referred to in Para 4 and 5. So, why should then Para 6 of Article 13 take precedence over Article 20 in covering items of income with which, given the tax authority's way, they both are not designed to be dealing?

Omitting theoretical speculations on correlation of Articles 13 ('Capital gains') with Article 20 ('Other income') which goes beyond the purpose of our particular study, the author of this article is also among those who deem application of Article 20 appropriate in this particular case.

In light of the above, due to its poor wording, Article 13 does not provide for clear and definitive procedure to establish taxing rights of the parties to the Convention. Given such flaws, different outcomes could follow as a result of application of Article 13 because of different interpretative approaches. Having said that, it is very much expected that the Ukrainian tax authorities would follow fiscal approach in construing the provisions of the Ukraine-Cyprus double tax treaty to secure the source taxing rights with respect to mentioned capital gains.

As of the date of this article, there had been no court practice on application of the provisions of the relevant double tax treaty on taxation of the mentioned capital gains that admit such ambiguous interpretation.

CONCLUSION

The discussed situation is an example where deficiencies in the wording of the text pose practical problems. The concrete tax implications for the taxpayers largely depend on the interpretative approach. The situation is further deteriorated by highly fiscal manner undertaken by the Ukrainian tax authorities who most likely will exploit the uncertainties of the text to deny the treaty benefits granted by Article 13.

Apart from the above, the case also presents interest for academic community as a good material on double-tax conventions interpretation. It is expected that the court practice to be evolved in this regard will clarify the issue and uphold the approach whereby the gains from indirect alienation of immovable property where such property is in which the business is carried on.

ANTICIPATED PRIVATIZATION IN UKRAINE

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ABSTRACT

This article is dedicated to familiarize the reader with the relevant legislative framework regarding the privatization tenders in Ukraine, as well as the most attractive assets which will be tendered during the privatization.

Key Words: Ukraine, Privatization, Infrastructure, Auctions.

INTRODUCTION

Due to its socialistic past in the Soviet Union, the role of the state remains to be immense in Ukraine's economy nowadays despite 30 years of independence and a pro-Western course aimed at implementing the liberal market reforms. Certain state authorities in Ukraine not only carry out controlling and supervision functions, but also involved in the management of state-owned enterprises (SOEs) and state-owned assets. Currently, around 100 separate public bodies manage around 3,500 SOEs in Ukraine[1], which number is very high in comparison with the Central and Eastern European countries[2]. It is evident that the availability of so many SOEs is not well-justified, and the state cannot dedicate the necessary resources to ensure a proper operation of the most SOEs. The lack of transparency in the corporate governance and the bureaucratic mechanisms of a day-to-day management of the SOEs make the state an inefficient owner, while the enterprises themselves become a burden on the state budget and are often involved in corruption schemes on embezzlement of state funds. Therefore, the Government of Ukraine decided to sell the assets, which do not possess a strategic importance to Ukraine's economy on the privatization tenders.

1. WHAT IS THE PRIVATIZATION IN UKRAINE?

The legislative framework for privatization implementing the best international practices in the area has undergone a large reform in the recent years and is supported and assisted by international partners such as the International Monetary Fund, the World Bank, and the European Bank for Reconstruction and Development.

Privatization is a sale of state-owned property to private individuals or legal entities. All objects to be privatized are divided into small-scale and large-scale privatization objects. Objects of small-scale privatization include not only state-owned enterprises or its shares but also objects of unfinished construction, separate movable and immovable property, the price of which does not exceed UAH 250 million. Such objects can be sold exclusively through government's electronic trading system ProZorro. Sale, which implemented the best international practice of full transparency[3] of the tender process – the entire sale process is open to the public to avoid corruption. The State Property Fund ensures full disclosure of asset information. All documents become available to investors after signing a non-disclosure agreement.

As a general rule, the privatization in Ukraine is carried out on the basis of English auction model, where a winner is selected on the basis of the highest price bid.

1 Dmytro Sennychenko, "Reloading Ukraine's privatization process", Access date: December 14, 2020, https://www.atlanticcouncil.org/blogs/ukrainealert/reloading-ukraines-privatization-process/.

2 Uwe Böwer, "State-Owned Enterprises in Emerging Europe: The Good, the Bad, and the Ugly", IMF Working Paper, October 2017, p. 6.

3 Amongst other recognitions, Prozorro received the showcase status as an exceptional example of public e-procurement from the European Bank of Reconstruction and Development (EBRD) and was a winner of World Procurement Award 2016, a major international award in the field of procurement - https://prozorro.gov.ua/en/about/achievements

If the price of the object is higher than UAH 250 million – these are large-scale privatization objects, which are mostly the shares in the large SOEs. The sale process of such objects contemplates the involvement of investment advisers, who gather all the necessary information, determine the starting price, prepare the object for privatization and liaise with potential investors. Usually, large consulting, audit and investment companies act as investment advisors for large-scale objects. There are currently 23 large-scale assets scheduled for privatization including enterprises in the mining, chemicals, machine-building, and energy industries[4].

However, there are around 300 SOEs in Ukraine that have strategic value and are not subject to the privatization. Those are the enterprises in the defense sector, natural monopolies, and companies with high social value such as Ukrposhta (state postal service), Ukrzaliznytsia (national rail transport operator), Boryspil International Airport, and others. According to the Government's intentions, all non-core state assets that do not have a strategical importance in defense or other core areas must undergo privatization.

Under the Law of Ukraine "On Privatization"[5], the following types of persons cannot act as buyers on the privatization tenders:

- state bodies, SOEs, employees of state privatization bodies;
- buyers registered in offshore zones with non-transparent ownership structures which ultimate beneficial owners are not disclosed;
- buyers from the aggressor state (Russian Federation) (including the buyers which ultimate beneficial owners (10% or more) are registered there);
- buyers registered in states that included in the FATF blacklist, as well as direct or indirect subsidiaries (50% or more) of such buyers;
- persons under the Ukrainian sanctions regime and their affiliates;
- Ukrainian legal entities whose beneficial owners have not been disclosed in the Ukrainian companies register;
- persons that have concluded a privatization agreement which privatization agreement was terminated as a result of violations by such persons or their affiliates; and
- advisers involved in the privatization process.

If a tender participant will not comply with the above requirements, then the tender application of such buyer will be disqualified following the investigation of the relevant corporate documents provided by the respective participant.

2. RECENT SUCCESSFUL PROJECTS

The first steps to launch the large-scale privatization were taken in 2018; however, due to the economic decline on the major markets and the Covid-19 restrictions, the large-scale privatization was put on hold. Only on 30 April 2021, the President of Ukraine signed the law aimed at unblocking the privatization of large-scale objects and facilities, renewing auctions and pre-sale activities that were suspended due to the Covid-19 pandemic. According to the head of the State Property Fund of Ukraine, Mr Sennychenko, the adoption of this law would allow attracting UAH 12 billion[6] (ca. USD 450 million) to the state budget in course of privatization auctions.

Nevertheless, in 2020, despite the economic crisis caused by the Covid-19 pandemic, the Government was able to raise around UAH 3.03 billion from the small-scale privatiza-

4 Order of the Cabinet of Ministers of Ukraine No. 36-p dated 16 January 2019, http://www.spfu.gov.ua/userfiles/files/rozporiad_v.pdf.

5 Part 2 of Article 8 of the Law of Ukraine "On Privatization of the State and Municipal Property", https://zakon.rada.gov.ua/laws/show/2269-19#Text

6 Dmytro Sennychenko, "First privatization auctions will be held in the Summer", Ukrinform, Access date: March 30, 2020, https://www.ukrinform.ua/rubric-economy/3218280-persi-aukcioni-velikoi-privatizacii-vidbudutsa-vze-vlitku-golova-fondu-derzmajna.html

tion, which is six times more than was initially planned. To achieve this, the State Property Fund of Ukraine has carried out around 1,900 privatization auctions[7].

Among the most successful tenders was the privatization of the Dnipro Hotel, with a winning bid of UAH 1,111 billion (with the initial tender price of UAH 80,93 million)[8], and the privatization of "Kyivpasservice" Joint-Stock Company with the final price of UAH 231 million (with the initial tender price of UAH 195 million)[9].

However, the privatization does not affect only single enterprises but entire industries - for example, as part of the demonopolization of the alcohol market, the State Property Fund of Ukraine has carried out transparent auctions on the privatization of Ukrspyrt, state-owned producer of alcohol and alcohol-containing products which operated 41 alcohol production plants before the privatization, 25 of which have been already sold starting from 2020[10]. As a result, the budget will receive more than UAH 1.2 billion, and the economy will have a positive effect from the development of the entire industry.

3. LARGE-SCALE PRIVATIZATION OBJECTS OF 2021

The Government intends to carry out the first large-scale privatization tenders still in the first half of 2021[11]. The State Property Fund of Ukraine prioritises the privatization of the following facilities:

- First Kyiv Machine-Building Plant ("Bilshovyk"), one of the oldest industrial enterprises in Ukraine dealing with mechanical engineering and renting of premises. The plant's territory can be potentially used for the implementation of a major real estate project;
- Odesa Portside Plant, a major producer of ammonium nitrate, carbamide, liquid nitrogen, carbon dioxide, liquid oxygen, and sodium sulphate;
- United Mining and Chemical Company, a leading producer of titanium ore, zirconium, rutile and ilmenite concentrates in Ukraine and Europe; and
- President-Hotel, a four-star hotel in the central business district of Kyiv, ranked among the largest hotels in Ukraine's capital by a number of rooms.

Also, among the largest objects which may be of great interest for potential investors are the following:

- privatization of the Public Joint Stock Company "Centrenergo", a leading energy generating company in Ukraine engaged in the production and supply of electricity and heat. The production facilities include three combined heat-and-power plants (CHPs) – Vuhlehirska, Zmiivska and Trypilska – with a total installed capacity of 7,690MW (which amounts to approximately 15% of the total power generation volume in Ukraine) and there is a separate manufacturing company, Remenergo, which repairs and maintains the main and ancillary equipment of CHPs;
- privatization of JSC "Turboatom", a large enterprise involved in the design and manufacture of steam turbines for thermal power plants, central heating plants, and nuclear power plants; and hydro turbines for hydropower plants. The company can produce steam turbines with a total design capacity of 8 million kW per year, and 2 million kW of hydro turbines per year;
- privatization of State Enterprise "Electrovazhmash Plant" involved in the production of electric motors, generators and transformers. It is one of the largest enterprises in the CIS in its field, having electrical insulation, tooling, foundry and welding production, as well as testing and R&D facilities;
- privatization of "Zaporizhzhya Titanium and Magnesium Plant" Limited Liability Company involved in production and sale of high quality titanium products. The quality of ZTMK products is guaranteed by a certified management system in accordance with the requirements of the international standards ISO 9001, EN 9100, ISO 14001, ISO 50001 and ISO 45001. Part of the spongy titanium is used as a raw material for the production of ingots and slabs of titanium and titanium alloys, the rest of the spongy titanium is sold to consumers as marketable products;
- privatization of "Sumykhimprom" Public Joint-Stock Company, which produces mineral fertilizers, coagulants and additives to cement, acid, titanium dioxide and pigments, and other types of chemical products. This large energy-chemical complex has an industrial site of 226 ha.

CONCLUSION

Following the implementation of best international practices regarding the sale of state-owned property into its legislation and the availability many SOEs and state-owned assets with great technical and scientific base and relatively low-paid professionals, Ukraine appears to be a great destination for international investors intending to acquire an operating business under an adequate price.

For Ukraine, the privatization will generate revenue for the state budget, and will trigger economic growth, attract investment, and create jobs. Therefore, the privatization of Ukrainian SOEs is one of a few win-win instances during these uncertain times.

7 State Property Fund of Ukraine, "Privatization-2020: Following the Results of Transparent Tenders, Around Three Billion Hryvnias Should Be Transferred to the State Budge", State Property Fund of Ukraine, Access date: December 30, 2020, http://www.spfu.gov.ua/ua/news/7063.html

8 State Property Fund of Ukraine, "Successful Privatization of Dnipro Hotel – State Will Receive UAH 1,111,111,222", State Property Fund of Ukraine, Access date: July 15, 2020, http://www.spfu.gov.ua/ua/news/6679.html

9 State Property Fund of Ukraine, "Privatization-2020: Following the Results of Transparent Tenders, Around Three Billion Hryvnias Should Be Transferred to the State Budge", State Property Fund of Ukraine, Access date: March 3, 2020, http://www.spfu.gov.ua/ua/news/uspishne-zavershennya-aukcionu-z-prodazhu-derzhavnih-akcij-%C2%ABkiivpasservis%-C2%BB-6344.html.

10 State Property Fund of Ukraine, "State Property Fund Will Not Allow the Manipulation with the Concluded Privatization Agreements", State Property Fund of Ukraine, Access date: February 22, 2021, http://www.spfu.gov.ua/ua/news/7234.html

11 Dmytro Sennychenko, "First privatization auctions will be held in the Summer", Ukrinform, Access date: March 30, 2020, https://www.ukrinform.ua/rubric-economy/3218280-persi-aukcioni-velikoi-privatizacii-vidbudutsa-vze-vlitku-golova-fondu-derzmajna.html

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