Institute for Economic Leadership

Research on European experience in tax administration

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Glossary

“Nudge letters” are official but gentle letters sent by tax authorities to taxpayers to encourage them to voluntarily adjust their tax behavior.

“One-stop” – a concept that refers to the possibility for citizens to obtain all necessary services in one institution. Examples include EU OSS (a tax system for VAT in the EU, where a company files a report in only one country, even if it sells throughout the EU), the Estonian e-Business Register portal, and the “Дія” app.

The EU Blacklist of Non-Cooperative Jurisdictions for Tax Purposes is an official list of jurisdictions that the European Union considers to be tax opaque because they do not implement international transparency rules (CRS, BEPS, etc.) or have overly lenient offshore regimes.

EU acquis (from French – "achievements") – the achievements of European integration in the political, legal, and economic spheres, which are based on the common European values defined in Article 2 of the EU Treaty and constitute a set of rights and obligations of EU member states.

Advance pricing agreement (APA) is a formal agreement with the tax authorities that determines in advance how to set prices (transfer pricing) in cross-border transactions between related companies. An APA provides a legal guarantee that the transfer pricing method is acceptable to the tax authorities and protects against penalties and audits.

Annual investment allowance (AIA) is an annual investment tax credit in the UK that allows companies to write off 100% of the cost of fixed assets immediately in the year of purchase, with a limit of £1,000,000 per year.

API (application programming interface) is an interface for interaction between different programs, allowing them to exchange data and commands automatically.

BEPS rules (Base Erosion and Profit Shifting) are a set of international tax rules aimed at combating tax avoidance by large companies when they transfer profits to low-tax countries without paying taxes where they actually operate.

CBI (Confederation of British Industry) – a royal business association that brings together nearly 190,000 companies of various sizes to lobby the government on behalf of British business. The CBI provides analytical reports, facilitates dialogue between business and government, and shapes national and international economic strategies.

CIS (Construction Industry Scheme) is a tax scheme in the UK that requires contractors to withhold tax from payments to subcontractors and transfer it directly to HMRC (the tax authority) to ensure proper tax payments in the construction industry.

Conditional Dividend WHT is a special regime that applies to dividend, royalty, and interest payments in low-tax jurisdictions.

Corruption Perceptions Index (CPI) – An index published annually by the international organization Transparency International.

CRS (Common Reporting Standard) – an international standard for the automatic exchange of tax information between countries,

developed by the OECD, in which more than 120 countries participate.

cum/cum – a tax avoidance scheme in Germany, whereby a foreign investor who would otherwise have to pay tax on dividends temporarily "loans" their shares to a resident to avoid WHT, and then returns them, resulting in the resident receiving the dividend, paying less or no WHT, and then transfers it to the foreigner.

cum/ex – a tax scheme in Germany for evading or reducing dividend tax, in particular withholding tax (WHT), whereby participants in the scheme, as a result of manipulation, received dividends from shares and paid tax on them once, but received tax refunds several times.

Declining-balance depreciation – a method of accelerated depreciation where a fixed percentage of the residual value of an asset is written off each year, rather than the initial value.

Defence tax – a tax levied by the state to finance defense, the armed forces, or military needs.

Digiport – a central electronic gateway for the exchange of official communications between businesses and the Dutch government.

e-Estonia – digital infrastructure in Estonia that involves transferring most of the interaction between government agencies and citizens to an online environment, including data exchange between government agencies and businesses, voting in elections, residency, etc.

e-Residency is a digital status that Estonia has been issuing to permanent residents since 2014 so that they can set up and manage companies in the EU entirely online, regardless of their country of residence.

ECT (Exit Capital Tax) is a tax levied when capital leaves the country or when tax residency changes, especially if it is related to tax avoidance.

ELSTER (Elektronische Steuererklärung) – the official online portal of the German tax service for submitting tax returns in electronic form.

Enterprise Investment Scheme (EIS) – a UK government program that encourages investment in young and innovative companies by offering tax incentives to investors.

Forschungszulage – a tax incentive for research and development (R&D) in Germany, effective since 2020.

Fourth Bureaucracy Relief Act (BEG IV, Bürokratieentlastungsgesetz IV) – a legislative initiative in Germany aimed at reducing administrative barriers for citizens, businesses, and government agencies, which came into force on January 1, 2025. The package raises the threshold for mandatory VAT reporting ( ) from €7,000 to €9,500, digitizes tax reporting, and simplifies transfer pricing documentation.

Full expensing is a tax rule that allows a company to immediately write off 100% of the cost of investments in fixed assets (assets) as expenses in the same year they were purchased. For example, a company purchases new equipment for UAH 1,000,000. Under normal circumstances, it would write off this amount in installments over several years, but with 100% full expensing, it can immediately deduct the entire UAH 1,000,000 from its taxable income, reducing its taxes for the current year. Full expensing does not reduce the total amount of expenses – it simply

accelerates the moment when the company receives a tax benefit, which is important for the cash flow of the business.

Gewerbesteuer is a tax on business activities in Germany, which is paid by all enterprises doing business within a municipality (Gemeinde). The amount of tax is determined by multiplying the base rate (basic federal coefficient – 3.5%) by the municipality multiplier set by the local authorities.

HMRC – Her Majesty's Revenue and Customs, a UK government body responsible for fiscal policy.

Innovation Box is a special tax regime that allows companies to pay less income tax if that income is derived from intellectual property: patents, software, know-how, etc.

The International Tax Competitiveness Index Tax Foundation is an annual study of 38 OECD member countries that assesses the competitiveness of their tax systems in terms of stimulating economic growth. The ITCI analyzes 41 criteria in five key categories: corporate taxes, personal taxes, consumption taxes (e.g., VAT/GST), property taxes (real estate, land), and rules on international transactions (based on WHT, CFC, BEPS, etc.).

ISORA (international survey on revenue administration) is a study of tax administrations conducted by leading international organizations (OECD, IMF, CIAT, IOTA) to collect comparative data on the functioning, performance, and practices of public administrations in tax collection.

MakeUK – a non-governmental organization and the UK's leading business association in the manufacturing and engineering sector, representing the interests of over 20,000 companies, from start-ups to large corporations. It provides advice, educational

programs, research, and influence on government policies to support industry growth and job creation.

Patent Box is a type of Innovation Box, i.e., a special tax regime that allows companies to pay reduced income tax on profits derived specifically from patented developments.

PAYE ("Pay as you earn") is a system of personal income tax in the UK, whereby the employer deducts taxes and national insurance contributions directly from the employee's salary.

R&D (Research & Development) is the process of creating new products and technologies or improving existing ones. Companies invest in R&D to develop new ideas, create new products, improve the quality of goods or services, and remain competitive.

R&D relief – a policy of reducing a company's corporate tax or refunding up to 33% of research and development costs in the United Kingdom.

R&D credit is a tax break or discount that the government gives to companies that spend money on research and development (i.e., R&D).

Real Estate Investment Trust (REIT) – an investment trust that owns, manages, or finances income-producing real estate and pays most of its profits to investors as dividends.

RVO.nl (Rijksdienst voor Ondernemend Nederland – RVO) is the official website of the Netherlands Enterprise Agency, which is part of the Dutch Ministry of Economic Affairs and Climate Policy and supports entrepreneurs, innovators, farmers, and exporters through grant programs, incentives, subsidies, and advice on innovation, sustainability, and export.

SBR (standard business reporting) – the Dutch national standard for the digital exchange of financial reports between businesses, banks, and government agencies.

Seed Enterprise Investment Scheme (SEIS) – a UK government program that encourages investment in the youngest startups by providing tax incentives for private investors.

TAS 2024 – an intergovernmental report by the OECD describing tax administration tools and trends in 58 countries, including: digitization of tax services (e-reports, electronic payments, AI-accurate control); new tools to combat tax evasion, such as tax gap estimation and improvements in tax debt collection and risk management procedures.

Wachstums-chancengesetz (German for Growth Opportunities Act) – a German law introducing a number of fiscal incentives for businesses: for companies investing in research and development, the expenditure limit has been increased to €10 million and the reimbursement rate has been raised to 35% for small businesses; Accelerated depreciation of up to 60% of the cost of fixed assets in the first year is permitted, which significantly reduces the tax burden. small businesses with a turnover of up to €800,000 can use the cash method and are exempt from the obligation to file a VAT return; introduction of electronic invoicing (e-invoicing) for B2B transactions, etc. The law also provides for simplified reporting, the possibility of broader loss carry-forward, and improved conditions for business digitalization.

Wet Bevordering Speur- en Ontwikkelingswerk (WBSO) – a tax credit granted to legal entities that pay corporate tax and have employees in R&D, or individual entrepreneurs who spend at least 500 hours on R&D per year.

X-Road – a key element of "e-Estonia" that allows the state and businesses to exchange data securely, efficiently, and transparently.

XML (eXtensible markup language) – a text format for structuring and storing data that allows information to be exchanged between different systems in an understandable, standardized form.

Advance tax ruling (ATR) – an official decision by a tax authority that responds to a taxpayer's request regarding future actions or transactions.

Tax-free window – a period or situation when the state does not require taxes to be paid on certain income or transactions in order to support business or stimulate a sector.

Business angels – private individuals who offer capital to launch a startup or expand an existing company from their own savings at an early stage of their development. Angels often work with projects that are of little interest to large venture capital funds or credit organizations.

B2C is a term used to describe commercial relationships between businesses and consumers. This market sector includes beauty salons, clothing and pet stores, and restaurants.

GDP is one of the most important indicators of economic development, reflecting the results of the production activities of resident economic entities in the field of tangible and intangible production.

Дія.City is a special legal regime for IT companies in Ukraine, which aims to stimulate the development of technology businesses by creating favorable conditions for transparent

business practices, intellectual property protection, and reduced tax burdens.

STS – State Tax Service of Ukraine, the central executive authority in the field of taxation in Ukraine.

EIA (from Dutch – Energie-investeringsaftrek) – a tax credit that allows you to write off up to 40% of the cost of investments in energy-efficient technologies, such as solar panels, heat pumps, and ventilation systems with heat recovery.

USR – Unified State Register of Legal Entities, Individual Entrepreneurs, and Public Organizations, a public register of legal entities in Ukraine that performs the role of state control and protection of the rights of legal entities, public organizations, and entrepreneurs in Ukraine, as well as the protection of the rights of third parties in legal relations with them.

ESV – a single social contribution, mandatory deductions for state social insurance to protect the rights of insured persons to receive insurance payments in cases provided for by law, which is paid by the entrepreneur for himself and for each hired employee.

Investment depreciation deferral (IDD) – a tax instrument that allows businesses to write off part of their investment costs (equipment, machinery, etc.) ahead of schedule, even before actual depreciation.

Industrial park – a land plot where participants can engage in industrial production, economic and research activities.

IP income is income that an individual or legal entity receives from the use of intellectual property, such as copyrights, patents for inventions, computer programs or mobile applications, and trademarks. IP income arises from the sale of rights, permission

for others to use one's intellectual property, and monetization. For example, in Ukraine, an individual who receives income from IP (e.g., royalties) usually pays 18% personal income tax (PIT) and 1.5% military tax, but there are exceptions—for example, in the IT sector or with certain licenses—where tax breaks may apply.

KIA (from Dutch – Kleinschaligheidsinvesteringsaftrek) – a tax benefit in the Netherlands for small and medium-sized businesses, which allows them to write off part of their investment costs in assets from their taxable income.

Klima-Prämie (German for "climate bonus") is a cash compensation or benefit that the government may grant to households or companies in connection with the introduction of a carbon tax or carbon pricing.

Compliance is a system of measures, procedures, rules, and controls designed to ensure that an organization or employee complies with legislation, ethical standards, regulatory requirements, and internal rules.

MIA (from Dutch – Milieu-investeringsaftrek) – a tax benefit that allows companies in the Netherlands to write off up to 45% of the cost of investments in environmentally friendly technologies and equipment in addition to normal depreciation.

SMEs (small and medium enterprises) – small and medium-sized enterprises.

OECD nexus – intangible assets related to research and development (R&D) that are eligible for tax relief under intellectual property (IP box/ Patent box) only if created or developed by the company itself. According to OECD standards, in

order to be eligible for an IP benefit, a company must have a "nexus" between R&D and IP income.

The OECD is an international organization aimed at strengthening and improving the economies of member states, improving socio-economic conditions and employment by developing recommendations for governments around the world.

An option is a contract that gives its holder the right, but not the obligation, to buy or sell a specific asset (e.g., shares, currency, commodities) at a fixed price in the future or by a certain date. The value of an option depends on the price of the asset.

VAT (value added tax) is an indirect tax that is included in the price of goods (works, services) and paid by the buyer, but its accounting and transfer to the state budget is carried out by the seller (tax agent).

PIT (Personal income tax) – a tax on the income of an individual, which provides for the collection of a mandatory payment from funds received by an individual in the form of wages, scholarships, profits from entrepreneurial activities, and other types of income.

Tax invoices and settlement adjustments.

Tax depreciation is a method by which a company gradually writes off the cost of long-term assets (e.g., equipment, buildings, machinery) in order to reduce taxable income.

Tax gap – the difference between how much tax the state should have received according to the law and how much was actually paid.

CIT (corporate income tax) – a tax on corporate profits, a tax paid by companies on the money remaining after all expenses have been covered.

SM KOR – a system for monitoring the compliance of tax invoices/adjustment calculations with risk assessment criteria. It was introduced in Ukraine to combat VAT fraud. SM KOR operates on the basis of an analysis of VAT payer reporting data, available tax information, and information submitted by the VAT payer that reflects the specifics of their economic activity separately for each type of economic activity. The SM KOR is designed to preventively respond to abuses by unscrupulous VAT payers at the stage of tax invoice registration.

Tonnage Tax is an alternative taxation system for shipping companies, under which they pay tax not on actual profits, but on a fixed amount calculated on the basis of the tonnage of the fleet.

TP documentation is an official set of documents that justifies prices in controlled transactions between related parties in order to prove their compliance with the arm's length principle. (a fundamental principle in transfer pricing, which means that prices in transactions between related parties should be the same as if these transactions were carried out between independent parties in an open market). Typical components of TP documentation include: Master File – a general description of the group's activities, Local File – details of specific transactions in the jurisdiction, and Transaction Matrix / CbCR (in some countries) – a table with data on financial indicators by country and type of transaction.

Fragmented rates are a system in which different tax rates are applied to different types of income, activities, or categories of taxpayers, often without a single logic or a single base.

Introduction

Due to the consequences of full-scale war, the budget deficit increased to 20.6% of GDP**. The tax burden (including social security contributions) rose to ≈ 32–33% of GDP, which is significantly higher than the pre-war level of 26%**[1] **.** Today, the Ukrainian fiscal sector faces two key challenges: finding a balance between filling the budget and maintaining a favorable business climate, which is particularly affected by the tax burden.

The tax service performs classic functions: fiscal (attracting resources for defense and reconstruction), stabilizing (introducing customs duties and excise taxes), and redistributive (PIT + SSC = 40% labor tax). By 2025, integration will be added to the main functions, as harmonization of rules with the EU Acquis[I] is a prerequisite for future membership in the Organization for Economic Cooperation and Development (OECD).

The administrative burden remains excessive. According to the World Bank's Ukraine: 2024 Tax Compliance Cost Survey, businesses spend an average of 74.4 days per year on tax compliance[2] . That is why there is an urgent need to find management solutions that will reduce the administrative costs of business to the OECD average of 6.6 days (158.8 hours/year)[3] and make the business climate more attractive to investors.

The purpose of the study is to conduct a comparative analysis of the key features and indicators of the tax systems of Ukraine, the

[I] The set of rights and obligations of EU member states.

Netherlands, the United Kingdom, Estonia, and Germany, with a focus on business incentives, the fight against tax evasion, and the specifics of local taxation. Such a comparison allows us to:

1) Identify best administrative practices (the Netherlands, the United Kingdom),

2) Assess the impact of full digitalization on transparency and costs (Estonia),

3) Track how a large welfare state (Germany) maintains a balance between high tax contributions and business incentives.

Methodology: desk research based on the analysis of open statistical sources, industry reports, and official publications of tax administrations. Institute for Economic Leadership We collected and compared indicators of actual time spent on tax administration and frequency of audits, and studied the features of digital solutions and legislative cycles.

We focused on factors affecting tax administration and Ukraine's investment attractiveness, and proposed practical management solutions to reduce the administrative burden and stimulate economic growth. In the first section, we revealed the essence and components of the time, organizational, and financial costs of business for preparing and submitting declarations, paying taxes, and complying with regulatory procedures. Using the example of leading European countries: the Netherlands, the United Kingdom, Germany , and Estonia, we showed how digital solutions and stable regulation can reduce tax routine. In the second section, we analyzed the tax instruments that countries use to attract investment and support innovation. The third section is devoted to modern approaches to identifying and combating tax

evasion and the shadow economy. The conclusions and recommendations summarize the diagnosis of Ukraine's tax system and outline priority steps for reforming the SMKOP based on trust and analytics, introducing R&D credits and Innovation Box, creating a "one-stop-shop" for administering benefits, and stabilizing the regulatory process. The recommended management decisions should increase administrative predictability and ensure post-war recovery and sustainable development of Ukrainian business.

Section 1. Administrative burden

The administrative burden in tax administration is the total time, effort, and money spent on preparing and filing returns, paying taxes, and complying with all procedures required by law. The tax administration indicator also determines the competitiveness of countries. According to European Commission estimates, administrative procedures will cost small businesses in the EU €9,899 per year in 2024[4] . Digital tools — from pre-filled declarations to "virtual office" portals — are already proving their ability to reduce errors and time spent on preparing reports. However, the effect of these solutions varies from country to country.

All EU countries are linked by the common logic of a "single window" for VAT reporting. The starting point was the Mini One Stop Shop (MOSS) in 2015: it allowed digital service providers, especially companies outside the Union, to keep records in only one member state instead of thirty, effectively eliminating most duplicate registrations and significantly reducing paper bureaucracy by about three-quarters[5] . The evolution of MOSS was VAT One Stop Shop (OSS), launched on July 1, 2021. Now, through a single portal, it is possible to declare and immediately pay VAT for all remote B2C sales of goods and services within the Union, and the national tax authority itself transfers the amounts

to the consumer countries. According to the European Commission's estimates, this approach reduces administrative costs by up to 95%, which previously arose due to multiple registrations, separate reports, and payments[6] .

According to the World Bank Paying Taxes (2019) methodology, the average business in the Netherlands spends 21 hours per year preparing, filing, and paying corporate income tax. This figure was published by the Tax Foundation in a comparative study entitled "Complexity of the Corporate Income Tax in Europe," in which the Netherlands shares the top spot with Belgium and Finland, trailing only Estonia and Ireland[7] . This low figure is achieved thanks to the fact that CIT requires only one payment per year and an almost complete transition to electronic channels. The key technical condition for this cost reduction was the transition to Standard Business Reporting (SBR). SBR forms a single taxonomy for all financial and tax forms and transmits them in XBRL (eXtensible Business Reporting Language) packages. XBRL is an open XML standard that "marks up" each field of the declaration with a machine-readable tag, allowing the company's accounting system to automatically generate a file and the Digiport gateway to validate it without human intervention[8] . In 2017, 85% of CIT declarations were already submitted in XBRL format. According to the OECD ISORA (TAS 2024) cycle published in 2024, the share of electronic submissions reached virtually 100%, with 92% of them being transmitted via SBR gateways[9] . In June 2024, the government presented the concept *of real-time taxation:* algorithms will automatically calculate and write off tax liabilities even before the declaration is submitted, which, according to the forecast of the Dutch Ministry of Finance, will "unburden" taxpayers and increase confidence in the system[10] . The

digitalization strategy is supported by a moderate frequency of changes: on average, three to four tax acts per year are published in a single *Belastingplan* package, which provides businesses with a predictable annual planning horizon.

The digital foundation of the British tax system is the Making Tax Digital for VAT (MTD) program. Research by Ipsos MORI and the HMRC final report **recorded** a ~13% **reduction** in **errors** when completing tax returns and found that ≈ 69% of taxpayers no longer print primary documents after switching to electronic invoices and API connections with accounting software[11] . However, the effect of digitization did not offset the increase in the tax service's own costs. The National Audit Office (NAO) recorded an increase in HMRC's administrative costs of £563 million (+15%) between 2019/20 and 2023/24, while the total compliance cost for small businesses reached £15.4 billion per year[12] . In 2020/21, the total compliance bill for small businesses fell significantly (from £4,955 million in 2019/20 to £3,741 million in 2020/21). This is due to the COVID-19 pandemic: part of HMRC's resources were redirected to support assistance schemes, which led to a decrease in the amount of identified underpayments of taxable amounts in small businesses. In 2021/22, this figure rose[13] to £5,761 million, approaching pre-crisis levels. In 2022/23, it fell again[14] to £4,753 million, and in 2023/24, it rose[15] to £5,294 million. For medium-sized businesses, the trend was different. The compliance bill for medium-sized businesses fell[16] from £6,115 million in 2019/20 to £5,154 million in 2020/21. In 2021/22, it fell slightly[17] to £4,715 million. However, in 2022/23, the figure rose[18] to £5,902 million, and in 2023/24, it rose sharply[19] to £9,365 million. This jump in 2023/24 is linked, in particular, to[20] the updating and strengthening of control measures for larger taxpayers (high

amounts of tax adjustments in large and medium-sized companies).

The growing burden on businesses is exacerbated by operational delays: in spring 2025, the Guardian reported that PAYE and CIS refunds were taking more than four months, which was "freezing" SMEs' working capital[21] . The reason for the heavy losses, despite the existence of extensive digital infrastructure, lies in budgetary practices. Each tax year is accompanied by two major packages of changes – the Spring and Autumn Budgets – which materialize in separate Finance Acts. Although formally there are only two budget waves per year, their content is often difficult to predict and they create significant fiscal uncertainty for businesses, which is feared by the manufacturing associations Make UK and CBI: a survey in autumn 2024 showed that fiscal uncertainty ahead of the Autumn Budget was the main factor in the reduction of business investment plans . [22]

Germany is balancing on the edge of digital progress and social bureaucracy. In 2020, more than 28 million tax returns were filed through the ELSTER portal, and by the end of the same year, a total of 1.75 billion electronic applications of all types had been processed. 99% of companies and employers submit advance VAT and payroll returns through ELSTER[23] . [24]Despite the comprehensive online infrastructure, making payments to social funds consumes an additional 134 hours of accounting time, and businesses make a total of nine electronic payments per year, with four different funds having their own tax ceilings and reporting files. The average compliance time (41 hours and two CIT payments) still exceeds the average for high-income countries[25] . Bürokratieentlastungsgesetz IV, adopted in March 2024, will save

businesses €944 million per year by eliminating paper employment contracts and raising thresholds for small-scale reporting, according to estimates by the German Ministry of Finance[26] . At the same time, the Growth Opportunities Act (March 2024) reduces advance payments and introduces pre-filled CIT forms for SMEs[27] . Despite these steps towards "digitalisation", the federal-municipal two-tier model (CIT + Gewerbesteuer) maintains fragmented rates and requires separate accounting settings, which preserves a high proportion of "paper" reporting work in a hybrid format.

The Estonian e-Tax platform now covers 99% of all tax returns filed by individuals and legal entities[28] . For the average citizen, the process takes three to five minutes: the user logs in with Mobile-ID, reviews the pre-filled form, and confirms it with a digital signature[29] . At the business level, corporate tax sets a record: all annual CIT reporting takes only 5 hours—the lowest rate in Europe[30] , **while the full tax package (CIT + VAT + social contributions) costs the company ≈50 hours compared to the European average of 130-140**[31] . The secret to this speed lies in X-Road data, which combines more than 900 public and private registries. The Estonian *once-only* principle means that taxpayers never have to enter the same information twice: the system pulls in salary, bank interest, and mortgage payments and immediately generates a draft declaration[32] . After submission, VAT refund requests are also processed almost instantly: the average refund time is up to five days, which practically eliminates the post-filing burden[33] . As a result of the digitization of the system, possible "schemes" with fictitious VAT refunds are minimized – the VAT gap in Estonia is[34] 4.4% of its VAT Total Tax Liability (€218 million) and is one of the lowest in the EU, where the average[35] is 7% of the total

VAT Total Tax Liability (VTTL) across member states (€83.9 billion). Thanks to its digital infrastructure and cash basis of income taxation (CIT is paid only when dividends are distributed), Estonia has topped the Tax Foundation's International Tax Competitiveness Index[36] for the eleventh consecutive year. The Estonian case also demonstrates that full digitalization brings tangible results only when paired with a clear data architecture and a small amount of regulatory changes. In 2015-2022, the parliament passed an average of 1-2 tax acts per year, limiting itself to specific adjustments to excise taxes. In 2024, the trend changed dramatically: the Tax Changes 2024 package was adopted, raising the basic VAT rate from 20% to 22% (and a temporary "defense tax" of 24% from 2025) and introducing a new tax on cars, while from 2025 the CIT and PIT rates will increase to 22%[37] . The government is still maintaining its "anchor" – 0% CIT on reinvested profits, which businesses regard as the main tool for predictability. However, from January 1, 2026, a temporary "security tax" of 2% of the company's accounting profit will be added to this system, even if the profit is not distributed. This tax will be paid quarterly for several years.

In Ukraine, the mobile application "Дія" is the most popular symbol of the "state in a smartphone" policy. The platform is called a "low-cost, highly resistant to corruption, and fast" tool[38] . The taxpayer's e-Cabinet provides PIT/CIT/VAT filing and already covers 97.6% of legal entities' reporting[39] .

However, compliance time (37 hours) and the unpredictability of rules remain a major problem:

in 2023, more than 90 amendments were made to the Tax Code, and in Q1 2025, eleven new laws were already introduced.

The SM KOR system monitors over a million VAT invoices daily, but in 2023, it blocked 76% of invoices by mistake[40] . 29.6% of companies consider the risk of blocking to be the "main obstacle" to dialogue with the State Tax Service[41] .

The Business Ombudsman notes that administrative procedures in Ukraine are "significantly more complex and time-consuming than in other countries"[42] . Ukraine has achieved almost total electronic filing, but procedural unpredictability and the control-oriented design of the SM KOR negate the benefits. Electronic services reduce paper, but they do not reduce hours.

Digitalization without public trust does not guarantee a proportional reduction in the administrative burden. The Netherlands and Estonia confirm the effect of comprehensive integration (XBRL-SBR, X-Road) and a stable annual cycle of changes. The United Kingdom and Germany show that large digital projects without synchronization of the legislative schedule can even increase costs if the number of adjustments remains high. Ukraine, with 97% e-filing, highlights the "digitalization paradox": without predictable rulemaking and service design (pre-filing instead of blocking), even almost total digitization does not eliminate hundreds of "forced" hours of accounting time.

Section 2. Business incentive policy: carrots instead of sticks?

Taxation is not limited to a purely fiscal function. In the global competition for talent and capital, it is national tax incentives that increasingly determine where a research center will open, where a patent will "go," or in which jurisdiction the founders will conduct the first round of financing. For example, economists at USC Schaeffer note[43] that overall reductions in corporate tax encourage the relocation of innovative assets and R&D to jurisdictions where the tax burden is lower, even if the overall global level of innovation remains unchanged. In the US, the R&D tax credit has shown[44] an economic effect: every dollar spent on the credit stimulates more than a dollar of investment in R&D. This confirms the direct link between tax incentives and increased innovation activity.

In this section, five benchmark countries—the Netherlands, the United Kingdom, Germany, Estonia, and Ukraine—are examined through six key prismatic planes: 's base income tax rates, flagship incentives for research institutes and intellectual property, investment and "green" deductions, sectoral regimes, and regulatory risk hot spots.

Country	Basic CIT rates	Flagship for R&D / IP	Other investment/green deductions	Sectoral regimes	Hot spots and risks
Netherlands	19% on the first €200,000, then 25.8%[45]	**Innovation Box** – 9% CIT on profits from own R&D assets (OECD nexus)[46] **WBSO** – 36% compensation (50% for start-ups) on the first €380,000 of R&D salary costs from 2025[47]	MIA 27-45%, EIA 40%, KIA up to €19,769[48]	Tonnage tax for 10 years [49]	On January 1, 2024, **a Conditional Dividend WHT of 25.8%** was introduced for low-tax jurisdictions; stricter anti-avoidance rules for cooperatives and APA/ATR[50]
United Kingdom Britain	19% (<£50k) / 25% (>£250k) + marginal relief window[51]	**R&D Expenditure Credit** 20% (27% for R&D-intensive loss-making SMEs) from April 1, 2024[52] **Patent Box** – 10% effective[53]	Permanent **Full expensing 100%**+ AIA £1 million per year[54]	SEIS/EIS – 50%/30% Income-tax relief for private investors; Creative-industry credit 25-39%; Tonnage tax[55] [56]	Discussions on increasing the share of benefits from Patent Box after CIT increase; government shows willingness to adjust the scheme[57]
Germany	No reduced rate (≈ 30% CIT + Gewerbesteuer)	**Forschungszulage** – 25% (35% SME) on salaries + equipment depreciation; base limit raised to €10 million from 27.03.2024 [58][59]	**IAB 50%** of future capital investments (profit ≤ €200k[60] ; **Climate bonus 15%** (max €30 million, 2025-29)[61] ; accelerated 5% declining-balance	Tonnage tax: 6,500 TEU vessel taxed at a base of around €65k per year [63]	The 2024 Growth Opportunities Act significantly expanded R&D credits and accelerated depreciation, but increased control over abuse

			depreciation for housing[62]		
Estonia	0% CIT on undistributed profits (from 2026 – 2% security tax; when paying dividends from 2025, the rate is 22% (14% abolished) [64]	No special R&D credits; innovation rate offset by zero CIT on reinvested profits	Up to 50% additional depreciation on energy-efficient equipment (tax clarification 2023)[65]	Tonnage tax (until 06.2026), 0% PIT + reduced social contributions for seafarers; employee options tax-free after 3 years, no social security contributions – attractive for startups[66]	From 2025, the PIT rate will be increased to 22%, which partially negates the advantages for founders, but administration remains extremely simple
Ukraine	18% standard rate (9% ECT optional in Diia.City)[67] [68]	**Diia.City**: You can choose 9% Exit Capital Tax; 5% PIT on developers' salaries; 0% PIT on dividends once every 2 years.[69]	Industrial parks: 0% CIT for 10 years, 0% VAT + customs privileges subject to reinvestment[70] ; exemption from VAT and customs duties on imports of energy equipment (July 2024)[71]	Targeted incentives for critical energy infrastructure; reconstruction fund with grant R&D windows planned	Fragmented legislation, complex administration. Current 50% CIT for banks (2024) distorts competition

Estonia offers the simplest model: zero CIT as long as profits are reinvested. The Netherlands and the UK combine reduced rates on IP income (Innovation Box / Patent Box) with generous early-stage cost reimbursement (WBSO, R&D Credit). The preferential 50% SEIS in the UK and 50% WBSO rate for Dutch startups form a "tax bridge" between business angels and the first sale of the product. The German IAB and the increased 35% Forschungszulage rate for SMEs reduce the cash gap until commercialization.

Sectoral regimes (maritime transport, REIT, creative industry) – in all five jurisdictions, tonnage tax remains a popular way to "lock in" low taxation within the BEPS rules.

In the area of incentive regulation, the EU/OECD are tightening requirements for advance rulings and cooperative structures in the Netherlands in order to enforce legislation against tax avoidance, in particular through the cooperative instrument; Conditional Dividend WHT has already narrowed the tax-free window since 2024.

Compared to other digital solutions, the Ukrainian platform Diya.City **has come close to the effective rate of UK SME-R&D (≈11% after credits),** but the country still lacks the "one-stop" digital services and administrative predictability offered by Estonian e-Residency or the Dutch portal RVO.nl. Consolidating the benefits provided by industrial parks and energy import deferrals into a single application through a "single window" would increase transparency and reduce compliance costs.

Thus, the incentive policies in Estonia and the Netherlands are distinguished by the simplicity and depth of their research and development incentives (0% reinvested profit; Innovation Box +

WBSO). The UK uses a set of tools for all stages of the innovation cycle (from R&D relief to EIS). Germany focuses on direct wage subsidies. Ukraine should consolidate and simplify the administration of existing schemes and introduce one-stop shop digital services, similar to Estonia's e-Residency and the Dutch RVO portal, to increase the attractiveness and effectiveness of its own "bonuses."

Section 3. "Fighting the shadow" – combating tax evasion and the shadow economy

The new generation of administration systems is based on the exchange of information between jurisdictions and risk assessment using big data analytics, which facilitates the early detection of evasion schemes.
At the same time, countries are stepping up criminal prosecutions of tax evaders, introducing tougher penalties and even prison terms for serious cases, especially in the area of offshore schemes and VAT fraud.

Following the[72] scandal involving the discriminatory use of algorithms in the "toeslagenaffaire," the Dutch tax authority (Belastingdienst) radically changed its approach to control. Today, it effectively combines self-learning artificial intelligence algorithms for risk assessment with traditional checks, maintaining a balance between protecting taxpayers' rights and detecting abuse [73][74] . Machine learning systems generate risk profiles for taxpayers, but the final decision is made by a human. The algorithm does not automatically block the taxpayer, but only generates a recommendation for the employee. This avoids mass errors, ensures contact with the taxpayer before sanctions are applied, and increases trust in the system. This approach is

fundamentally different from the Ukrainian SM KOR system, which is also based on the automatic detection of risky transactions, but operates much more strictly. Appeals are only possible through formal administrative procedures or lengthy court proceedings. At the same time, the risk criteria are not public, and the system is based on a priori distrust of the payer.

In the United Kingdom, the tax gap for 2021–2022 is estimated at £36 billion, of which £4.9 billion is attributable to direct evasive behavior; HMRC is actively expanding its audit capabilities and increasing its staff to reduce this gap[75] . The Tackling offshore tax non-compliance program[I] provides for strict CRS data exchange and increased prosecution of offshore asset schemes, and in 2023-24, the number of voluntary disclosures abroad increased by 22% (5,643 cases) thanks to nudge letters and fines[76] . Thanks to the automated exchange of financial information under the CRS standard, HMRC receives annual data on the accounts of UK residents in more than 100 jurisdictions, including classic offshore jurisdictions. This allows them to accurately identify taxpayers who have not declared foreign assets and to verify their tax returns against actual data. The wording of the nudge letters is designed to reduce anxiety, but at the same time contains a clear hint of serious consequences in case of inaction. The inevitability of criminal liability for deliberately failing to declare foreign assets (even without the need to prove intentional fraud) is the third important factor—fines can reach 200% of the amount of unpaid tax, and in some cases, imprisonment is even possible.

[I] In general, this term is used to refer to the strategies and measures that states implement to detect hidden income and encourage citizens to act transparently.

Recent HMRC reports on tax gaps (tax gap and VAT gap) have shown[77] significant losses to the state budget, especially in the e-commerce sector. In the 2022–23 fiscal year, the VAT gap in the UK reached £8.8 billion, with a significant portion of these losses related to online marketplaces and sales through non-residents who evade VAT registration and payment. This has necessitated a review of the tax control strategy. E-commerce grew rapidly after the pandemic, but millions of small transactions on platforms such as Amazon, eBay, Wish, and Etsy remained outside of proper monitoring. The problem is that many foreign sellers were effectively operating without VAT registration or declaring lower sales volumes. The "missing trader fraud" scheme also remained widespread, where the seller receives funds but disappears without paying VAT. In response, HMRC tightened regulations on platforms in 2023-24. Online marketplaces now have "joint responsibility": they are required to verify the tax status of sellers, automatically withhold VAT on certain sales, and report transaction volumes to the tax authorities. All of this is regulated by[78] new rules, in particular under the OECD DAC7 program and national legislation[79] .

Germany's legislative framework has been updated through the Fourth Bureaucracy Relief Act, which expands measures to combat transfer pricing evasion and oversight, and integrates components of the EU's "blacklist" for high-risk jurisdictions[80] . [81]Among the measures are a reduction in the deadline for submitting documentation from 60 days to 30 days after receiving a request or notification of an audit; an obligation to submit a new tabular document detailing information about the agreement between the business and the counterparty; and the tax authority may request TP documentation both during and outside the audit

process. Criminal prosecution has also intensified: court proceedings concerning cum/ex and cum/cum schemes in Bonn and Munich demonstrate the willingness of the prosecutor's office to severely punish large-scale dividend fraud[82] .

Estonia has one of the smallest shadow economies in the EU (approximately 18% of GDP), due to high trust in state institutions and maximum transparency of all transactions on the e-Estonia platform. The strategy is based on trust and simplification: about 98% of declarations are submitted online in 3 minutes, and risky cases are instantly tracked through the integration of business, banking, and other registries[83] .

Estimates of Ukraine's shadow economy range from 30% to 45% of GDP, with tax loopholes and administrative barriers playing a significant role[84] . Currently, data integration between the Unified State Register, the State Tax Service, and the Diya platform is being implemented for rapid identification control, and there are plans to increase penalties for late registration of tax invoices/adjustment calculations and discrepancies between amounts paid and registers[85] . However, effectiveness depends on the further development of analytical platforms and the strengthening of tax and economic authorities (State Tax Service, State Customs Service, Financial and Economic Investigation Service) in order to comprehensively respond to complex evasion schemes.

In addition, a comparison of our five countries shows a clear correlation: the higher the score in the Corruption Perceptions Index (CPI) (less perceived corruption), the smaller the share of the shadow economy in GDP.

Country	Shadow economy, % of GDP	CPI-2024 (0-100)[86]
Netherlands	9.4[87]	78 points (9th place)
United Kingdom Britain	10.8[88]	71 points (20th)
Germany	10.4%[89]	75 points (15th)
Estonia	17.9%[90]	76 points (13th)
Ukraine	19.3%[91]	35 points (105th)[92]

Conclusions

The Ukrainian tax system faces the challenge of a dual transformation that will allow it to quickly fill the budget in wartime and provide an attractive environment for business. A comparative analysis of the tax systems of the Netherlands, the United Kingdom, Germany, and Estonia shows that the key to this balance lies not only in low rates or strict audits, but in simple and predictable rules, digital integration, and trust in institutions.

The administrative burden in Ukraine remains excessive. The reason is not the lack of digital tools, but their lack of integration and punitive nature (such as SM KOR with 72% of false blocks[93]). Where tax systems rely on stable rule-making, automatic filling of declarations, and unified data exchange channels (X-Road, XBRL-SBR), efficiency increases rapidly. The UK and Germany demonstrate that even high rates can be combined with generous R&D credits if businesses know the rules years in advance. Estonia shows that simplification, trust, and the logic of "single data entry" can reduce both the "shadow" economy and costs.

In terms of incentives, Ukraine already has a competitive platform—Diy.City has come close to the British level in terms of effective rates for innovative SMEs. But without a "single window" for benefits, without a transparent selection algorithm, and without a link to the State Tax Service's analytics, the potential remains limited. And even more critically, it is necessary to bridge the gap between digitalization and corruption. The data confirms

that countries with a high CPI have half the share of the "shadow economy." If Ukraine can raise its CPI by at least 5 points and simultaneously introduce service analytics (rather than total control), the effect will be calculated in tens of billions of hryvnia each year. For example, an analysis of 1999-2004 showed[94] that a 1-point increase in the CPI is accompanied by an average increase in GDP per capita of 2.4% for Eastern European countries. The OECD believes[95] that digitization (Prozorro, Diia) and institutional efforts to combat corruption could save up to 0.8% of GDP, or about UAH 50 billion annually.

Therefore, the main conclusion is simple: it is not rates and penalties that shape modern tax competitiveness, but trust, stability, and service. For Ukraine, the path lies not only in digitalization, but also in radically simplifying the administration architecture—so that every minute of accounting time works for development, not circumvention.

Policy proposals

The priority measure for improving the fiscal environment is the reform of the SM KOR based on trust and data analysis. However, adopting the experience of the Dutch tax service, where the final decision on blocking is made by the tax officer, is risky until the State Tax Service is rebooted. **Therefore, the first recommendation, for which the legislative framework has already been developed, is to reboot the State Tax Service and create a Public Control Council under it to prevent abuse.** The key problem with the SM KOR remains the lack of transparency in the criteria for assessing taxpayer risk, so **the next recommendation is to revise paragraph 201.16 of Article 201 of the Tax Code of Ukraine** (or related provisions of Section V on VAT administration), establishing the tax authority's obligation to disclose general risk criteria and give the taxpayer the opportunity to prove the reality of the transaction before refusing to register the tax invoice. Also, **supplement Article 20 of the Tax Code of Ukraine** with the right of the State Tax Service to obtain the necessary data from other state registries for automatic comparison of information (in compliance with data protection) and **amend Article 42 of the Tax Code of Ukraine** regarding electronic interaction: provide for sending a warning notice to the taxpayer before blocking registration so that they can voluntarily clarify the data or documents. In addition, we emphasize the need to take into account **the recommendations made by the NACP based on the results of the study "Corruption risks in the procedure for suspending/resuming registration of tax**

invoices/adjustment calculations in the Unified Register of Tax Invoices"[96] .

The next initiative is **to ensure the predictability of tax legislation**, which will guarantee stable rules of the game for businesses over a sufficient period of time to promote investment and planning, as well as reduce the costs of adapting to constant changes in the law. The best practice for implementing tax changes is moderate frequency (for example, 3-4 acts per year in a single package), which ensures predictability and taxpayer confidence. Therefore, it is necessary **to supplement Article 4 of the Tax Code with the principle of stability:** tax rates and rules cannot be changed more than once a year, and the budget law must contain all planned changes for the following year. Appropriate provisions should be added to **the Final Provisions of the Tax Code,** obliging the Government to submit a single draft law on tax changes once a year.

With regard to the predictability of tax policy, in accordance with budget legislation, amendments to tax laws shall come into force **only at the beginning of the new budget year**, except in cases of force majeure. This principle is enshrined in[97] in subparagraph 4.1.9 of Article 4 of the Tax Code of Ukraine: "Changes to any elements of taxes and fees may not be made later than six months before the start of the new budget period in which the new rules and rates will apply. Taxes, their rates, and tax benefits cannot be changed during the fiscal year." Thus, the legislator should adopt tax innovations in advance (before July 1 of the previous year) so that businesses have time to prepare. In practice, the principle of stability is systematically violated. Almost every year, the Verkhovna Rada adopts tax changes in the last days of December

(as part of the budget for the next year) or even in the middle of the year, without complying with the 6-month rule. For example, at the end of 2014, Laws No. 1621-VII (July 31, 2014) and No. 71-VIII (December 28, 2014) were adopted, which **doubled the[98] gas royalty rate** from 28% to 55% starting in 2015. [99]Both laws were adopted less than six months before the new budget period, but they came into force immediately – Law No. 1621 on August 3, 2014, and Law No. 71 on January 1, 2015. [100]Enterprises challenged these additional charges, referring to paragraph 4.1.9 of the Tax Code of Ukraine, and some courts of first instance sided with the taxpayers, recognizing that the new rates should only apply retroactively from 2016. [101][102]However, in April 2022, the Supreme Court changed its approach, deciding that the violation of the 6-month period did not invalidate the tax provision. The court stated that the Constitution does not oblige parliament to follow a special procedure for the entry into force of tax laws, and therefore the principle of stability cannot automatically change the effect of the adopted rules. Similarly, in other cases, tax changes were introduced without a proper transition period – suffice it to recall the annual "budget" amendments adopted a few days before the new year, or emergency fiscal decisions during crises. For example, even before the war in 2023, a number of changes (cancellation of privileges, indexation of rates, etc.) were adopted[103] in December 2022 and introduced on January 1. In a state of war, this is explained by force majeure, but even in peacetime, tax rules have repeatedly been changed "on the fly," ignoring the deferral period specified by the regulations. The principle of stability is in fact of a recommendatory nature. The Tax Code does not provide for a mechanism that would automatically postpone the entry into force of a tax provision in case of violation

of the 6-month period. As emphasized by[104] the Supreme Court, this principle is part of the principle of legal certainty, but in itself it does not change the procedure for enacting laws. [105]The absence of a direct prohibition allows parliament to change taxes at its discretion at any time. Judicial practice has also definitively sided with the fiscal authorities, refusing to recognize tax laws as illegal due to non-compliance with the principle. Often, the government and parliament deliberately violate the principle for the sake of urgent budget filling or reforms. Delays in decision-making (due to political bargaining or crisis circumstances) lead to the adoption of changes close to the new year. There is a lack of political will to adhere to the postponement, as it is easier to introduce a new tax immediately than to wait a year. The norm makes an exception for force majeure, but the criteria are vague. This creates a loophole: virtually any complication (economic downturn, the need for military funding, etc.) can be tacitly considered a reason, even though formally, a state of emergency or war has not been declared until 2022. The lack of clear conditions for applying the exception allows the rule to be circumvented. In addition, there is no body or procedure to monitor compliance with the principle during lawmaking. Parliamentary regulations do not contain safeguards: tax changes can be included in any bill at the end of the year. Because of this, the principle of stability is easily circumvented even without formal repeal. However, if the Public Council at the State Tax Service had broader powers and the supervisory body was more accountable to it, this rule would be effective. In addition, it would be possible to enshrine the principle of a 6-month vacancy period as an imperative requirement of the law . For example, **Article 92 of the Budget Code** could be supplemented with a direct provision

that tax laws adopted after July 1 automatically apply from the following budget year. This would eliminate ambiguity and support the position of taxpayers in the event of disputes. It should also be clearly defined what constitutes **force majeure** for the purposes of this provision (e.g., the introduction/abolition of taxes during a state of war or emergency). If there is an urgent need to make changes earlier, it is proposed to introduce a special parliamentary procedure: a separate vote on recognizing the bill as urgent, stating the reasons. Without such a decision, no tax law should come into force before the new year. It is also worth providing for liability — for example, if the State Tax Service applies a provision that contradicts the principle of stability, the taxpayer can appeal the additional charge, and the court will have grounds to side with them. It might be possible to combine tax changes with the budget planning cycle. In particular, **the government could be required** to submit a single comprehensive bill on changes to tax legislation each year by a certain date (e.g., June 1). After that date, the adoption of new tax rules (that increase the tax burden) would not be allowed.

The next set of recommendations concerns stimulating the innovative activity of Ukrainian companies, since as of 2024, the volume of funding for scientific research is[106] 0.17% of GDP. For comparison, in the Netherlands, this share is 1.6-1.7%[107] . A number of factors influence the financing of innovation, one of which is fiscal pressure. To reduce this pressure, it is proposed to:

1. **introduce a tax credit mechanism for R&D**, which would allow companies that carry out R&D or order these services from other institutions to receive a reduction in their income tax liability by a certain percentage of salaries and

other R&D expenses. For example, 50% compensation for R&D employee salaries for small businesses, and a lower percentage (30-40%) for others. To do this, it is necessary to establish a maximum base of expenses eligible for the credit and a requirement for documentary confirmation of the R&D project. Therefore, the recommendation is **to supplement Section III of the Tax Code (income tax)** with a new article establishing the taxpayer's right to reduce their tax liability by the amount of eligible R&D expenses (define the list of expenses and the percentage of compensation), **define** the term "R&D" **in Article 14 of the Tax Code** and the criteria for classifying expenses as R&D, and **make agreed amendments to Section XX "Transitional Provisions" of the Tax Code,** providing for the procedure for implementing this credit (for example, from 2025, with a gradual expansion of the base limit);

2. **Introduce an "Innovation Box" regime** – a reduced income tax rate on intellectual property. It is proposed to establish a reduced rate for Ukrainian income tax payers, for example 9% (instead of the standard 18%) on income derived from eligible IP assets. Eligibility criteria may be based on the requirements of the OECD nexus approach (i.e., the benefit applies to income from IP created as a result of own R&D). It is necessary to define a list of objects (patents, utility models, copyrights to software, etc.) and the procedure for calculating such income. For administrative purposes, require separate accounting ( ) of IP income/expenses and obtain a preliminary ruling from the tax authorities regarding the right to the benefit in order to prevent abuse. However, it should be noted that additional research is needed to calculate the optimal rate. Therefore, the recommendation is **to create a separate section in Section III of**

the Tax Code of Ukraine dedicated to the taxation of innovative profits, **to supplement Article 136 of the Tax Code of Ukraine** with a provision on a reduced rate for profits from qualified IP objects, and **Article 135 of the Tax Code of Ukraine** with a definition of the procedure for calculating such profits. **In Article 14 of the Tax Code of Ukraine**, define the terms "intellectual property for taxation purposes," "qualified IP profits," etc.

3. To stimulate investment in Ukrainian start-ups, **introduce a tax credit (loan) for individuals who are tax residents of Ukraine for investments in certain start-ups or venture funds**. It is proposed to allow personal income tax payers to reduce their annual income tax by 30-50% of the amount of investment in shares (stakes) of a Ukrainian small innovative enterprise, provided that this investment is held for at least a certain period (e.g., 3 years) and to set an upper limit on the preferential amount (e.g., the equivalent of UAH 100,000 per year) and criteria for qualifying as a startup (newly created companies that meet the requirements for the number of employees, turnover, and industry – IT, science, manufacturing, etc.). Therefore, the recommendation is **to supplement Article 166 of the Tax Code of Ukraine** in **Section IV of the Tax Code of Ukraine** with a provision on the taxpayer's right to a tax credit in the amount of a specified percentage of the amount of investments in corporate rights (shares, stocks) of qualified small enterprises, **and** to introduce the definition of a "qualified innovative (start-up) enterprise" for the purposes of this discount **in Article 14 of the Tax Code**.

4. Also**, amend Article 170 of the Tax Code of Ukraine** regarding the exemption from taxation of capital gains from the sale of such investments if they were held for longer than the established period, so that investors would not fear tax consequences upon exit.

In the context of a state budget deficit, an important set of recommendations is to expand soft tax compliance tools to reduce the tax gap. The recommendation is to introduce the practice of sending taxpayers so-called "nudge letters" from the tax service. Such letters should indicate any identified discrepancies or suspicious transactions on the part of the taxpayer and offer them the opportunity to rectify the situation themselves (clarify their tax return, pay additional tax) within a certain period without immediate penalties. At the same time, penalties for deliberate evasion should be increased to motivate a response to such letters. For example, fines should be increased to 200% of the amount of unpaid tax in cases of proven intent or failure to file a tax return on foreign income, and for large-scale schemes, criminal penalties (imprisonment) should be provided for. The combination of "soft" letters and "tough" penalties is a modern approach that is already yielding results in OECD countries. Therefore, it is necessary **to amend Article 86 of the Tax Code of Ukraine** and related provisions, allowing tax authorities to officially send taxpayers notices proposing that they voluntarily correct violations with a deferral of penalties. **Clarify Article 112 of the Tax Code:** voluntary corrections after receiving a "reminder letter" should be considered grounds for a minimum fine, and increase the penalties in Article 123 of the Tax Code for underpayment in case of failure to comply with the requirements after the "reminder." Additionally, **in Article 25 of the Tax Code of**

Ukraine, grant tax authorities the right to send such written notices to taxpayers without initiating an audit.

Subparagraph 14.1.49 of Article 14 of the Tax Code expands the concept of dividends to include so-called **"constructive dividends"** – hidden payments to a related party that are in fact a distribution of profits. In particular, for tax purposes, the following transactions are treated as dividends[108] : payments to the founder in connection with the distribution of net profit; payments to a non-resident for securities or corporate rights in excess of the arm's length level; overpayment to a related non-resident for goods, works, or services in excess of market value; shortfall in revenue from a non-resident (sale below market price); and payments to a non-resident in the event of a reduction in authorized capital or repurchase of shares, if they result in a reduction in the undistributed profit of the enterprise. These rules were introduced in 2021 as an anti-offshore measure: their purpose is to tax profits transferred abroad through transfer pricing or hidden dividend payments. In particular, if a Ukrainian company overpaid a subsidiary of a foreign corporation for goods above market price, the difference is considered[109] as a dividend payment to this non-resident with the corresponding tax (15% non-resident income tax, unless otherwise provided by double taxation agreements). The introduction of such a mechanism was intended to prevent tax evasion through overstatement of expenses or other *hidden repatriation* of income. In practice, this rule has encountered a number of problems, so "constructive dividends" are rarely declared voluntarily. Most taxpayers are in no hurry to voluntarily recognize part of their payments to related non-residents as dividends. For example, if a Ukrainian company purchases raw materials from its parent company (a non-resident) at an inflated

price, it usually does not withhold repatriation tax on the amount of this inflation when paying. Companies refer to the contractual price rather than the estimated "market" price—until the moment of inspection, this is treated as ordinary expenses rather than dividends. As a result, only a few taxpayers declared constructive dividends in their 2021 reports. Only after the introduction of mandatory transfer pricing (TP) reporting for 2021 did the situation begin to emerge: in 2022, when analyzing controlled transactions, many companies found that their prices did not comply with the arm's length principle and were forced to adjust their financial results. According to the State Tax Service ([110]), in 2022 alone, taxpayers submitted independent adjustments (TC annexes) amounting to **UAH** 3**.6 billion,** which is 62% of all adjustments for that year. This means that a significant portion of controlled transactions did not comply with market conditions. [111]This raises the question: did these companies tax *the adjusted amounts* as dividends? The tax authorities discovered this loophole and began sending companies demands to pay additional tax on non-resident income from these amounts. [112]In the second half of 2022 and in 2023, many large taxpayers received requests from the State Tax Service demanding that they explain the adjustments and pay 15% tax on the hidden "dividend" amounts. This led to numerous disputes: businesses insisted that they had only made adjustments for profit purposes, while tax authorities interpreted this as a payment of income to a non-resident. Thus, the rule did not work preventively — it is mainly applied after the fact, during audits or analysis of reports. No significant penalties or high-profile court precedents regarding constructive dividends have been announced yet, but there is *a systemic problem:* taxpayers and the tax authorities do not have a common understanding of

the criteria and procedure for applying this rule. Subparagraph 14.1.49 is formulated in general terms, without clear calculation methods. For example, it is unclear how to determine the "arm's length amount" for different situations — whether there is an acceptable range of deviations or whether the average price should be taken. Also, the rule does not directly describe the taxation mechanism in the case of non-monetary payments (as in the case of the sale of goods at a reduced price – the tax must be paid on the "lost" income without receiving money from the non-resident). Without detailed rules, taxpayers are unsure how to comply with the requirements and prefer to wait for clarification or action from the regulatory authorities. According to the provisions of the Tax Code of Ukraine, tax on non-resident income must be withheld when income is paid. However, in the case of constructive dividends, the "income" itself is only revealed after the transaction is completed – when a transfer pricing analysis is carried out, often at the end of the year or during an audit. This results in a legal conflict: the company would have to withhold tax if it knew about the "hidden" dividend in advance. In practice, however, it does not do so because at the time of payment everything is formalized as a regular purchase or return of capital.

capital. This time lag makes it impossible to perform timely

Then, when the violation is established, the company no longer has a mechanism to withhold tax from the non-resident—in fact, the payment is made at its own expense, often with penalties. The retroactive nature of the rule reduces the motivation to voluntarily comply with it. Only eight months after the introduction of these rules did the Ministry of Finance issue General Tax Consultation No. 480 (September 27, 2021) on the taxation of

non-resident income equivalent to dividends. It outlined[113] the general mechanism, in particular the application of tax agreements. However, many specific questions remained[114] unanswered. For example, what if a non-resident is a resident of a country with which Ukraine has an agreement: can a reduced tax rate on dividends be applied under the Convention? How can the "marketability" of the price be documented to avoid it being recognized as a dividend? The lack of detailed instructions has led to differences in interpretation. Local tax authorities interpret the rule aggressively, demanding tax on any adjusted amounts, while businesses sometimes reasonably argue that not all adjustments mean an actual transfer of funds to a non-resident. This generates numerous inquiries, acts, and potential disputes. To prove a constructive dividend case, the controlling authority needs to conduct a transfer pricing study: find comparable market prices, prove deviations, and determine the amount of excess. This requires expertise and resources. In practice, the State Tax Service focuses on large taxpayers with significant controlled transactions. Smaller companies or transactions that do not formally fall under the definition of "controlled" (for example, if the volume of transactions with a related non-resident did not exceed the threshold, or the non-resident is not included in the list of low-tax jurisdictions) can avoid attention and continue to withdraw profits without consequences. Thus, some potentially hidden dividend schemes remain outside the scope of the regulation. Taxpayers have found ways to minimize risks: for example, instead of overpricing goods, they use royalty or interest payments, which are not mentioned in the list of constructive dividends. Although such payments are also taxable (at a repatriation tax rate of 15% or lower under agreements), they

should not be equated with dividends—therefore, there is no double effect in the form of additional tax on top of what has already been withheld. Another way is structuring through third parties: when a contract is formally concluded with an independent trader at market price, and the excess profit is already deposited in a third jurisdiction (outside the reach of Ukrainian rules). Such schemes are not covered by regulations, so the purpose of the rule is partially negated. The wording of subparagraph 14.1.49 of the Tax Code needs to be revised to eliminate ambiguity. In particular, it should be explicitly stated that for the purposes of determining amounts that comply with the arm's length principle, the procedure provided for in Article 39 of the Tax Code (transfer pricing) shall be used. It is advisable to add tolerances or thresholds: for example, not to consider deviations within a certain "safe harbor" (5%) from the market price as dividends in order to avoid insignificant additional charges. A clear legislative definition with examples of typical situations will reduce the scope for arbitrary interpretation. The Ministry of Finance and the State Tax Service should update and expand their general tax consultations on this issue. It is necessary to answer all the problematic questions raised by the professional community (regarding the application of double taxation agreements, documentary evidence of market prices, taxation of non-monetary transactions, etc.). It is advisable to develop a detailed guide for businesses with examples of constructive dividend calculations in different scenarios. The more certainty there is, the higher the voluntary compliance. Introduce a special mechanism for pre-trial settlement of disputes regarding constructive dividends. For example, if the payer does not agree with the State Tax Service's claim for additional tax assessment on a non-

resident, provide the opportunity to appeal to *a special commission* under the Ministry of Finance or the Council on Transfer Pricing. Such a commission could quickly assess the validity of the controlling authority's claims (whether the market price has been correctly determined, whether the transaction meets the criteria of subparagraph 14.1.49). In order for the rule to achieve its goal, consideration should be given to extending its scope to other common schemes for hidden profit withdrawal. In particular, the possibility of equating interest on excessively large related loans that do not fall under thin capitalization, as well as royalties in favor of related parties in cases where they clearly perform the function of profit withdrawal (for example, are paid offshore without proper economic justification) with dividends should be assessed. Such a measure requires caution and clear criteria so as not to scare off investors, but it will specifically close loopholes. Alternatively, thin capitalization and other rules could be tightened to eliminate incentives to disguise dividends as interest/royalties. Effective detection of constructive dividends requires expertise in transfer pricing. It would be advisable to create a separate group of specialists within the State Tax Service responsible for monitoring hidden profits. Use modern data analysis tools (reports on controlled transactions, financial statements, etc.) for risk profiling—identifying companies with unusually low profitability and significant payments to non-residents. This will allow for proactive detection of violations, rather than ing voluntary adjustments. Incentives for voluntary compliance with the rules should be introduced. For example, if a taxpayer independently declares and pays tax on a constructive dividend before the deadline, they should be exempt from penalties and this should not be considered a violation. It is also

possible to stipulate that in the case of a voluntary price adjustment in a controlled transaction, the tax should not be levied twice (both through an increase in profit and as a dividend) — instead, the amount should be credited to the budget as the appropriate income or dividend tax, but not duplicated. Such steps will make the system more equitable and motivate businesses to cooperate rather than conceal information.

To counteract the transfer of profits to low-tax jurisdictions, we recommend introducing the concept of "conditional dividends," which essentially means that payments made by a Ukrainian company to a related party in an offshore or low-tax jurisdiction may be recognized by the tax authority as a dividend payment, even if they are formally recorded as other expenses. In the event of such recognition, repatriation tax (dividend tax) is levied on the amount of the payment at the established rate. It is proposed to establish that the list of such jurisdictions includes countries on the EU blacklist. If the total payments to a related party for the year exceed a certain percentage of the company's profit and do not comply with the arm's length principle, the tax authority may impose a conditional dividend tax. Therefore, in **Article 14 of the Tax Code**, the term "conditional dividends" and the criteria for classifying payments as such should be defined, based on subparagraph 14.1.49 of the Tax Code – definition of dividends, supplemented with a new paragraph. **In Articles 136 and 140 of the Tax Code of Ukraine**, it should be stipulated that the amount of conditional dividends is not included in expenses when determining profit, and **Article 141 of the Tax Code of Ukraine should be supplemented with** a new paragraph establishing that payments to a non-resident from the "list of jurisdictions" or a related person may be recognized as dividends for tax purposes

and taxed at a rate of 15% (as the standard repatriation tax rate, unless otherwise provided by conventions). For practical application, the same article should define the list or criteria of jurisdictions and **amend Article 39 of the Tax Code,** allowing the tax authority to classify excessive payments as conditional dividends during an audit.

Separately, we would like to emphasize once again that any changes, especially those aimed at reducing corruption risks and counteracting tax evasion, must be accompanied by personnel changes in the controlling authorities. Therefore, the primary task is to reboot the State Tax Service with the participation of international experts.

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