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ANALYSIS OF DOUBLE TAX RELIEF PROVISIONS IN DOUBLE TAX TREATIES BETWEEN UKRAINE AND MEMBER STATES OF THE EUROPEAN UNION

Master thesis

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LIST OF ABBREVIATIONS

Art.	Article
BEPS	Base Erosion and Profit Shifting OECD Project
CJEU	Court of Justice of the European Union
Double tax treaty	Convention between Contracting States for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital
ECHR	European Court of Human Rights
EU	European Union
OECD	Organisation for Economic Cooperation and Development
OECD Model Convention	OECD Model Tax Convention on Income and on Capital
Para.	Paragraph
Residence state	State of tax residence
Source state	State of income origin
TCU	Tax Code of Ukraine
UN	United Nations
UN Model Convention	UN Model Double Taxation Convention between Developed and Developing Countries
VCLT	Vienna Convention on the Law of Treaties

ABBREVIATIONS FOR FORMULAS

RI	Income earned in the residence state (residence income)
RT	Tax rate in the residence state (residence tax)
SI	Income earned in the source state (source income)
ST	Tax rate in the source state (source tax)
TB	Tax amount paid in the residence state (tax burden)

INTRODUCTION

"Division of the tax pie among countries"

Professor Nancy Kaufman[1]

Researched problem. On 23 June 2022, the status of a candidate country on accession to the EU was granted to Ukraine.[2] Nevertheless, the EU Commission warns that the capacity to cope with the competitive pressure in the EU will depend on post-war investments in Ukraine.[3] Subsequently, the first step in this direction shall be the establishment of strong economic ties between Ukraine and the EU. But more crucially, due to the geographical proximity of the EU to Ukraine, Ukrainian legal entities may consider expanding their businesses abroad to the EU. Meanwhile, companies established in the EU might be willing to join the Ukrainian market for the same reason. Since tax burden is one of the primary considerations to commence economic activity in a particular state, methods of preclusion of double corporate taxation between Ukraine and the EU Member States require consideration.

While the residence state (for instance, Ukraine) taxes the worldwide income of a legal entity, the source state (for instance, EU Member State) taxes only the income generated by a permanent establishment of this legal entity therein. Consequently, a legal entity becomes subject to double taxation. The same problem is relevant when the EU Member State is the residence state while Ukraine is the source state. Double taxation is an obstacle that precludes a company from operating in two states. Subsequently, methods of double taxation preclusion undertaken by Ukraine and EU Member States in their economic interrelations require analysis.

Double tax relief methods are prescribed in tax treaties on double taxation preclusion concluded between two states.[4] Ukraine has double tax treaties concluded with all twenty-seven EU Member States.[5] The current practice and problems linked with the avoidance of double taxation reveals the **novelty of the research**. Ukraine taxes non-residents' income earned in Ukraine. Under Para. 133.2.2 of the Tax Code of Ukraine (hereinafter – TCU), a non-resident taxpayer, that carries out an economic activity in Ukraine through a permanent establishment, is subject to a corporate

[1] Nancy Kaufman, "Fairness and the Taxation of International Income," *Law and Policy in International Business* 29, 2 (1998): 153.

[2] "European Council conclusions on Ukraine, the membership applications of Ukraine, the Republic of Moldova and Georgia, Western Balkans and external relations, 23 June 2022," European Council, accessed 18 November 2023, https://www.consilium.europa.eu/en/press/press-releases/2022/06/23/european-council-conclusions-on-ukraine-the-membership-applications-of-ukraine-the-republic-of-moldova-and-georgia-western-balkans-and-external-relations-23-june-2022/.

[3] "EU Commission's Recommendations for Ukraine's EU candidate status,“ Delegation of the European Union to Ukraine, accessed 18 November 2023, https://www.eeas.europa.eu/delegations/ukraine/eu-commissions-recommendations-ukraines-eu-candidate-status_en?s=232.

[4] The full of such a treaty is the Convention between Contracting States for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital.

[5] "International agreements of Ukraine on avoidance of double taxation," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

income tax if they receive income with a source of origin from Ukraine.[6] Secondly, Ukraine taxes national residents' income earned in Ukraine and abroad (so-called worldwide income). Given Para. 133.1.1 of the TCU, a tax resident of Ukraine is subject to a corporate income tax on all its income obtained from economic activity regardless of whether the income is earned in Ukraine or abroad. Therefore, Ukrainian tax residents who conduct business in the EU risk being taxed twice.

Double tax treaties with the EU Member States intend to alleviate this issue. Treaties prescribe how tax revenues shall be distributed between two states. Otherwise, they delineate the way two countries agreed to divide "a tax pie prepared by one taxpayer".[7] To exemplify the double taxation issue, the economic activity in Ukraine of Schwarz Pharma AG might be observed. Schwarz Pharma AG is a German tax resident, and it possesses a fixed place of business in Ukraine - permanent establishment.[8] The permanent establishment represents a German tax resident in Ukraine. Germany taxes the worldwide income[9] of Schwarz Pharma AG, while Ukraine taxes the income generated by Schwarz Pharma AG only in Ukraine. If no double tax treaty between Ukraine and Germany were concluded, Schwarz Pharma AG would pay a corporate income tax in both states at the fullest extent. However, according to Art. 23(1) of the double tax treaty between Ukraine and Germany, Germany allows exemption of the income earned in Ukraine to its tax residents. However, it is required to consider such an income for the matter of application of a higher tax rate.[10] This double tax relief is the exemption with progression method.

This example demonstrates that under a double tax treaty, a pair of states decide how their tax systems will interact to ensure that residents of each state get the tax relief to which they are entitled.[11] Such agreements assumingly balance the interests of a taxpayer as well as of sovereign states. On the one side, a taxpayer intends to broaden its economic presence beyond domestic borders without being "punished" by an extra tax burden. On the contrary, a state’s first and foremost interest is to replenish a state budget with maximum tax revenues.

The international community, namely the Organisation for Economic Co-operation and Development (hereinafter – OECD) and the United Nations (hereinafter – UN), reacted to this challenge. Both organisations suggest model bilateral tax conventions to be followed by countries

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[6] "Tax Code of Ukraine № 2755-VI from 02 December 2010," Parliament of Ukraine, accessed 18 November 2023, https://zakon.rada.gov.ua/laws/show/2755-17#Text.

[7] Maarten Floris de Wilde, *Sharing the Pie: Taxing Multinationals in a Global Market* (Erasmus University Rotterdam, 2015), 45.

[8] "Judgement № 826/3192/13-a from 07 February 2019 (Exo Platform SAS)," Supreme Court of Ukraine, accessed 18 November 2023, https://reyestr.court.gov.ua/Review/79758304.

[9] "Taxes on corporate income in Germany," PwC Worldwide Tax Summaries, accessed 18 November 2023, https://taxsummaries.pwc.com/Germany/Corporate/Taxes-on-corporate-income.

[10] "Double tax treaty between Ukraine and Germany № 276_001 from 04 October 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[11] L. Oats, A. Miller, and E. Mulligan, *Principles of International Taxation*, (London: Bloomsbury Publishing Plc., 2017), 144.

while drafting their own double tax treaties. There are the OECD Model Tax Convention on Income and on Capital (hereinafter – OECD Model Convention)[12] and the UN Model Double Taxation Convention between Developed and Developing Countries (hereinafter – UN Model Convention).[13] The Ukrainian scholars, in particular, L. Vdovichena,[14] O. Lepetiuk,[15] state that the OECD Model Convention served as a sample for Ukraine during concluding double tax treaties with EU Member States. Additionally, the Supreme Court of Ukraine in the *Polpharma S.A. case* emphasizes that the OECD Model Convention and Commentaries should be taken into account while applying a double tax treaty signed by Ukraine since provisions of the latter are based on the OECD Model Convention.[16] Following legal doctrine and case law, this research interprets double tax treaties concluded between Ukraine and the EU Member States under the OECD Model Convention and its Commentaries.

The OECD Model Convention examines double tax relief methods in Article 23A (exemption method) and Article 23B (credit method). Further elaboration on them is given in the Commentaries. The text of the OECD Model Convention portrays an ***exemption method*** as one that does not require a residence state to consider the income earned abroad. A tax resident merely pays a corporate income tax on the income earned in its residence state. On the contrary, according to the OECD Model Convention, a ***credit method*** requires to calculate the worldwide income and to apply a domestic tax rate to it. Then, the amount of tax paid abroad is deducted.

Nevertheless, the Commentaries to the OECD Model Convention delineate four types of double tax relief, namely the full exemption, exemption with progression, full credit, and ordinary credit. The ***full exemption*** description is similar to the one provided in Art. 23A of the OECD Model Convention. The description of the ***ordinary credit*** method in the Commentaries resembles Art. 23B of the OECD Model Convention analogously. Newly appeared double tax relief "deviations" in the Commentaries constitute the exemption with progression and full credit methods. The ***exemption with progression*** method still allows the application of a domestic corporate tax rate to the income earned only in the residence state. However, the applicable domestic tax rate might be higher than the ordinary tax rate depending on the amount of income earned abroad. The full exemption favours a

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12 "OECD Model Tax Convention on Income and on Capital: Condensed Version 2017 with Commentaries," Organization for Economic Co-operation and Development, accessed 18 November 2023, https://read.oecd-https://www.oecd.org/finance/model-tax-convention-on-income-and-on-capital-condensed-version-20745419.htm.

13 "UN Model Double Taxation Convention between Developed and Developing Countries 2017 with Commentaries," The United Nations, accessed 18 November 2023, https://www.un.org/esa/ffd/wp-content/uploads/2018/05/MDT_2017.pdf.

14 Lidiya Vdovichena, "Legal regulation in double tax avoidance domain" (doctoral dissertation, Dnipro State University of Internal Affairs, 2012), 81, https://law.chnu.edu.ua/lidiia-vdovichena/.

15 O. Lepetyuk, "Characteristics of Ukrainian double taxation treaties with EU member states by the example of royalties," *Scientific Journal of Uzhgorod National University* 24, 4 (2014): 170.

16 "Judgement № 826/3192/13-a from 13 June 2019 (Polpharma S.A.)," The Supreme Court of Ukraine, accessed 09 July 2023, https://reyestr.court.gov.ua/Review/82384034.

taxpayer more than its exemption with progression variation.[17] On the contrary, the ***full credit***, described by the Commentaries, suggests a less burdensome regime for a taxpayer compared to the ordinary credit. The application of a full credit does not depend on whether the tax rate abroad is higher than a domestic one. The deduction is conducted at the fullest amount of tax paid abroad.[18]

Thus, efficient tax planning depends on applicable double tax relief to a taxpayer that possess a permanent establishment in a respective state (Ukraine or the EU Member State).

Level of the analysis of a researched problem of the final thesis. The academic papers in the double taxation sphere examine the practical application of double tax relief methods. Double taxation problems and methods to diminish it are reviewed by Lynne Oats, Angharad Miller, Emer Mulligan,[19] Prianto Budi Saptono, Ridwan Andretya Cunis, Tri Handoko Sitorus,[20] Nicoleta Barbuta-Misu and Florin Tudor,[21] Valentin Bendlinger[22] and others. Researchers monitor the concrete double tax treaties while describing how double tax relief works. Though double tax relief methods are scrutinised in the literature, there is a need for a more specified academic study on preventing double corporate taxation between Ukraine and the EU Member States given striving of Ukraine to integrate into the EU.

Aim of the research. The aim of this thesis is to analyze and establish the types of double tax relief methods and mechanisms of their applications between Ukraine and EU Member States.

Objectives of the research. To achieve the aim of the research, the objectives of the research are these: 1) to identify double tax relief types and mechanisms of their work; 2) to determine the most beneficial and the most burdensome double tax relief for a taxpayer; 3) to examine which double tax relief methods are present in double tax treaties concluded between Ukraine and EU Member States; 4) given these findings, to suggest that Ukraine implement the most beneficial double tax relief for its tax residents operating in the EU, which would stipulate their onward economic activity therein.

Originality of the final thesis. The research reveals double tax relief instruments that Ukrainian tax residents, operating in the EU, may apply while computing their tax obligations in Ukraine. It is accompanied by calculations demonstrating the result of the double tax relief application. The research suggests formulas to calculate the amount of tax obligations attributable to

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[17] "OECD Model Convention 2017 with Commentaries," *supra note*, 12: Page 382, Para. 14 of the Commentaries part.
[18] *Ibid.*, Page 383, Para. 16 of the Commentaries part.
[19] Oats et.al., *supra note*, 11.
[20] Prianto Budi Saptono, Ridwan Andretya Cunis, and Tri Handoko Sitorus. "Exemption And Credit Methods In International Double Tax Avoidance Agreements: Literature Study." *International Journal of Scientific and Research Publications*, 11, 8 (2021).
[21] Nicoleta Barbuta-Misu and Florin Tudor, "The International Double Taxation - Avoiding Methods," *EIRP Proceedings* 4, 1 (2009).
[22] Valentin Bendlinger, "Chapter 6: Credit Method and Maximum Tax Credit," in *Exemption Method and Credit Method,* Georg Kofler et al. (Vienna: Vienna University Press, 2021).

the residence state depending on the type of double tax relief applied. Despite their simplified nature, the suggested calculations make this research more practically oriented.

Research methodology. The method of data selection and data analysis examines legislative acts, soft law documents, and scientific papers. Additionally, a comparative method finds out the most beneficial double tax relief method. This thesis concentrates on double tax relief on the corporate income tax paid by legal entities and does not examine double tax relief on the income of natural persons. The research revolves around juridical (legal) double taxation and does not address the economic double taxation.

Structure of the research. The first chapter describes concepts of residence, types of double taxation, permanent establishment, double tax treaties, and double tax relief. The second chapter suggests simplified formulas to calculate the eventual amount of tax to be paid in the residence state. The third chapter examines double tax treaties concluded between Ukraine and twenty-seven EU Member States. The third chapter encompasses two pieces. First, it specifies double tax reliefs that Ukraine applies to its tax residents possessing a permanent establishment in the EU. Second, it specifies double tax reliefs that each of twenty-seven EU Member States applies to its tax residents possessing a permanent establishment in Ukraine.

Defence statements. The full exemption method is the most favourable for taxpayers as it permits them to pay less tax and is less burdensome bureaucratically. Ukrainian legislators should opt for the full exemption method in their tax reform to stimulate investments in the Ukrainian economy.

CHAPTER 1. EMERGENCE OF DOUBLE TAXATION BETWEEN UKRAINE AND EU MEMBER STATES

1.1. Double taxation caused by operation of a tax resident abroad

We live in an era of globalization. Domestic markets have gradually opened up, steadily evolving into a single worldwide marketplace.[23] More and more legal entities tend to extend the boundaries of their economic presence. They supply goods or provide services not only in the state of their residence but also abroad. However, a borderless economy is not only about generating income worldwide but also taxing it.

1.1.1. Taxing rights of the residence state and the source state

When it comes to taxation of income, it is quite standard practice that a state asserts taxing claim on the basis of both territorial link with the person of the taxpayer (on the basis of its "fiscal residence") and territorial link with the taxable object (on the basis of "source of income").[24] Essentially, almost every country in the world distinguishes between two broad categories of taxpayers – residents and non-residents – in exercising its income tax jurisdiction. Residents are usually taxed in respect of their worldwide income, regardless of the geographic origin of their income, while non-residents are taxed only in respect of their income arising from domestic sources.[25] The OECD Model Convention does not provide the precise definition of a "resident", leaving it up to the consideration of each state.[26] The same approach is maintained in the UN Model Convention.[27] Neither of the model documents answers precisely what the residential bond means. Filling this gap is left up to a state.

Traditionally, residence means that a legal entity is linked with a certain state closer than with any other state. Possessing the resident status allows a state to demand computing the taxpayer's tax base by adding the income generated inside and outside the state of residence. In other words, the state of tax residence taxes the worldwide income of their tax residents. Criteria to impose the residential link differs from a state to state. It might be based upon a) place of incorporation (legal seat criteria) and b) place of effective management (real seat criteria).[28] Place of incorporation is one

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23 Wilde, *supra note*, 6: 5.

24 Stjepan Gadžo, "The Principle of Nexus or Genuine Link as a Keystone of International Income Tax Law: A Reappraisal," *Intertax* 46, 3 (2018): 194.

25 *Ibid.*, 205.

26 "OECD Model Convention 2017 with Commentaries," *supra note*, 12: Art. 4(1).

27 "UN Model Convention 2017 with Commentaries," *supra note*, 13: Art. 4(1).

28 Jean-Marie Meier and Jake Smith, "Improving the Measurement of Tax Residence: Implications for Research on Corporate Taxation," *SSRN*, February 15, 2022, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4035673; Luca

of the most common approaches given its plainness and predictability. Most controversies are attributable to determinations the place of effective management (it can be given such factors as headquarters, bank account, property, etc.).[29]

As a general rule, Para. 14.1.213(a) of the TCU perceives legal entities as Ukrainian tax residents if they are registered there (legal seat criteria). Given Para. 134.1.1. of the TCU, Ukrainian tax resident are subject to corporate income tax on their income earned worldwide.[30] However, in 2020, Ukraine has introduced a real seat criteria to determine tax residence. Upon this, new provisions to the TCU were included, though this reform raises controvercies. In accordance with Para. 133.1.5. of the TCU, a legal entity registered abroad shall register itself as a tax resident of Ukraine in case managerial decisions of this foreign legal entity are taken in Ukraine, and refusal of a legal entity to register itself as a tax resident of Ukraine equals liquidation of this legal entity in Ukraine. Controversy implies the possibility of liquidating an entity that was not even registered in Ukraine. Nevertheless, for the purposes of this research, the only fact that matters is the presence of both legal seat and real seat criteria to determine residence according to the Ukrainian tax legislation.

To compare, an approach to determine residence might be observed in two EU Member States, - Lithuania and the Czech Republic. Lithuanian legislation also considers the place of incorporation in Lithuania as a factor in attributing a residential link to a legal entity.[31] Like in Ukraine, Lithuania taxes the worldwide income of their taxpayers. The tax base of a Lithuanian legal entity shall be all income earned in Lithuania and foreign states which are sourced inside and outside of Lithuania.[32] Czech tax residents are liable to tax on income arising from sources in both the Czech Republic and abroad. Czechia considers legal entities having their registration or headquarters in the Czech Republic as residents.[33]

Nevertheless, some states do not impose taxation on their residents' worldwide income, narrowing themselves only to taxation of income generated in the state of residence. In the EU, France can serve as an example. A resident company is subject to corproate income tax in France on its French-source income.[34] In that respect, income attributable to foreign business activity (if there is no treaty in force between France and the relevant foreign country) or to a foreign permanent

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Cerioni, „The "Place of Effective Management" as a Connecting Factor for Companies' Tax Residence Within the EU vs. the Freedom of Establishment: The Need for a Rethinking?,“ *German Law Journal* 13, 9 (2012): 1096.

[29] There is no EU Directive dedicated to the cross-border transfer of company seats, which makes this process more complex; see: Stephan Rammeloo, "Cross-border company migration in the EU: Transfer of registered office (conversion) – the last piece of the puzzle? Case C-106/16 Polbud, EU:C:2017:804," *Maastricht Journal of European and Comparative Law,* 25, 1, (2018): 87.

[30] "Tax Code of Ukraine," *supra note*, 5: Para. 133.1.1.

[31] "Law of Lithuania on Corporate Income Tax № IX-675 from 20 December 2001," Parliament of Lithuania, accessed 18 November 2023, https://e-seimas.lrs.lt/portal/legalAct/lt/TAD/1375cd60a50f11e8aa33fe8f0fea665f: Art. 2(2).

[32] *Ibid.*, Art. 4(1).

[33] Michal Radvan, *Czech tax law* (Brno: Masaryk University, 2020), 46.

[34] "Taxes on corporate income in France," PwC Worldwide Tax Summaries, accessed 18 November 2023, https://taxsummaries.pwc.com/france/corporate/taxes-on-corporate-income.

establishment (if a tax treaty applies) is excluded from the French tax basis.[35] Nevertheless, this example is an exception rather than a general rule. Even Cyprus, one of the most famous tax jurisdictions to establish a company in, levies corporate taxation on the worldwide income of their Cypriot tax residents.[36]

Double residence. As observed, there is no unanimous approach to determining a legal entity as a tax resident. Each state possesses discretion on this matter. The problem arises when several states consider one taxpayer as their tax resident and pretend to impose taxation on their worldwide income. Supposing state A considers a legal entity as their tax resident if it is incorporated in state A. Meanwhile, state B perceives a legal entity as a tax resident if its headquarters are located therein. Assume that company X is registered in state A, but its managerial board seats in state B. Consequently, states A and B consider company X as their tax resident and deem to tax the worldwide income of this company.

Transferring headquarters or registration to another place could preclude the issue. However, the double tax treaty might assist a taxpayer on this matter too. Pursuant to Article 4(3) of the OECD Model Convention, where a legal entity is a resident of both Contracting States, the competent authorities of the Contracting States shall determine by mutual agreement the Contracting State of which such an entity shall be deemed a resident. The regard can be given to a place of effective management, a place where it is incorporated or otherwise constituted and any other relevant factors. Thus, it is up to states to choose a characteristic that prevails while determining a place of residence in a double residence conflict. Given Para. 133.1.5 of the TCU, a legal entity, recognized as a non-resident of Ukraine in accordance with the international treaty of Ukraine on the avoidance of double taxation, is automatically recognized as a non-resident taxpayer.

Only upon attributing a legal entity to a certain state as their resident, double tax relief applies. If the double residence conflict is not solved, a taxpayer cannot apply the double tax relief method to diminish double taxation. Article 23A(1) and Article 23A(2) of the OECD Model Convention determine that double tax relief methods are out of assistance to a taxpayer should both states consider it as their tax resident:

"1) Article 23A(1). Exemption method. Where a resident of a Contracting State derives income which may be taxed in the other Contracting State in accordance with the provisions of this Convention (*except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State*) [...]

[35] In the context of double tax relief, it has some negative consequences for some catagories of taxpayers. If a state has a double tax treaty with a state, where a taxpayer possesses a permanent establishment, and this treaty provides less beneficial regime than domestic law (for intance, it does not grant exemption like in a double tax treaty between Ukraine and France), this regime under a double tax treaty shall prevail over domestic law.

[36] "Annual Cyprus Tax Facts Review 2022," EY Cyprus Offices, accessed 13 July 2023, https://www.ey.com/en_cy/news/2022/01/ey-presents-cyprus-tax-facts-2022-guide

2) Article 23B(1). Credit method. Where a resident of a Contracting State derives income which may be taxed in the other Contracting State in accordance with the provisions of this Convention (*except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State*) [...]

Thus, a double tax treaty assists a legal entity with a double tax relief only if it is covered as a tax resident in one of the state parties of the treaty and is not deemed a tax resident in both.

Taxes covered. In the context of the double taxation elimination, attention shall be also paid not only to the definition of a permanent establishment under a double tax treaty but also to taxes covered by this treaty. Article 2 of the OECD Model Convention (and Article 2 of the vast double tax treaties drafted upon it), establishes the treaty's substantive scope, listing taxes covered by the treaty. Double tax relief cannot be claimed for taxes that do not fall within the scope of a double tax treaty. States specifically include certain taxes in the list of taxes under Article 2 of their tax treaties to guarantee that double tax relief is available in the other states in the case of such taxes.

1.1.2. Types of double taxation

International and domestic double taxation. There are several types of double taxation. Firstly, there is a differentiation between international and domestic double taxation. Secondly, there is a differentiation between economic and juridical (legal) double taxation. The first typology is based upon a geographical criterion. Domestic double taxation arises when comparable taxes are imposed by sovereign tax jurisdictions of equal rank within a federal state.[37] International double taxation occurs when comparable taxes are imposed in two or more states on the same taxpayer in respect of the same taxable income or capital, e.g. where income is taxable in the source state and in the state of residence of the recipient of such income.[38] This master thesis examines international double taxation.

Economic and juridical double taxation. Within international double taxation, economic and juridical double taxation may occur. Double taxation is juridical when *the same person* is taxed twice on the same income by more than one state. In the meantime, double taxation is economic if *more than one person* is taxed on the same item.[39] Thus, if the same tax object is transferred from one taxpayer to another, and each taxpayer has to pay a tax on this object, this type of double taxation is economic. The classic example is when the post-tax profits are distributed to shareholders in the form of dividends, and the shareholders are subject to income tax in part or in full on the dividend they

[37] Reuven S. Avi-Yohan, *International Tax as International Law: An Analysis of the International Tax Regime* (Cambridge University Press, 2007), 23.
[38] "Glossary of Tax Terms," Organisation for Economic Co-operation and Development, accessed 31 July 2023, https://www.oecd.org/ctp/glossaryoftaxterms.htm
[39] *Ibid.*

receive. However, this form of double taxation is not the subject of this research. We are concerned with international double taxation, which is a narrower, and technically known as juridical double taxation.[40] The term "juridical" is used by the OECD in its terminology (e.g. Glossary of tax terms, Commentaries to the OECD Model Convention),[41] while the term "legal" double taxation is mainly used in the legal doctrine.[42] This research follows the terminology of the OECD, defining this type of double taxation as juridical. To summarise, juridical double taxation occurs when more than one country attempts to tax the same income.[43] Thus, the same income is taxable in the hands of the same person by more than one state.[44]

Juridical double taxation underlines the extent to which residents and non-residents are taxed. These statutes are combined in a single legal entity should the latter possess a legal presence in the state of tax residence and an economic presence in a state of income source. Fiscal authorities of two states collect taxes concurrently on the same basis. A legal entity, therefore, bears a heavier tax obligation than if it were subject to a single fiscal authority.[45]

1.1.3. Permanent establishment operation causes juridical double taxation

From the tax point of view, there are two common models of how a legal entity might conduct business abroad. Firstly, it can incorporate a new legal entity in a foreign state (subsidiary). The latter shall pay corporate income tax only in the state of its incorporation, while its legal entity founder from another state (mother company) obtains economic benefits through dividends. In the first example, a newly incorporated legal entity is a tax resident in its place of incorporation. Subsequently, a legal entity founder and an incorporated legal entity are two different legal subjects. This business model is not a subject of the thesis.

Secondly, a legal entity can conduct business in a foreign state through a permanent establishment situated therein. The permanent establishment does not mean the incorporation of a new legal entity but is deemed the continuation of a foreign legal entity in that state (like a "hand" of a legal entity in another state).[46] A permanent establishment is a non-resident taxpayer in a state of its location. Permanent establishment abroad and a foreign legal entity constitute the same legal subject. The thesis problem examines a situation when a tax resident of one country (either Ukraine or an EU Member State) operates in another country through a permanent establishment.

[40] Oats et.al., *supra note*, 11: 95.
[41] "Glossary of Tax Terms," *op. cit.*, 30.
[42] Saptono et.al., *supra note*, 18: 12.
[43] "Glossary of Tax Terms," *supra note*, 30.
[44] "OECD Model Convention 2017 with Commentaries," *supra note*, 12: Page 376, Para. 1 of the Commentaries part.
[45] Barbuta-Misu and Florin Tudor, *supra note*, 19: 486.
[46] Peter Harris, *Corporate Tax Law* (Cambridge University Press, 2013), 35.

The problem is that a foreign legal entity shall pay corporate income tax in the state where its permanent establishment is located as long as it generates income there. Such a state is called the *state of income source* (hereinafter – the source state). On the contrary, the *state of tax residence* (hereinafter – the residence state) imposes taxation on the worldwide income of its tax resident, causing the double taxation issue.[47]

Article 7 of the OECD Model Convention prescribes that a foreign entity's business income is not taxable unless it possesses a permanent establishment status in a state of its economic activity. Cases upon which the presence of a foreign entity in another state shall be deemed as a permanent establishment are prescribed in Article 5 of the OECD Model Convention. Article 5 defines a permanent establishment as a *fixed place of business* through which the business of an enterprise is wholly or partly carried on. The term "permanent establishment" is examplified in Article 5 as a) a place of management; b) a branch; c) an office; d) a factory; e) a workshop, and f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

The concept of being *fixed* is detailed in the Commentaries to Article 5 of the OECD Model Convention. Pursuant to Para. 6 of the Commentaries to Art. 5, the definition of a "permanent establishment" contains the following conditions:

1) the existence of a "place of *business*", i.e. a facility such as premises or, in certain instances, machinery or equipment;

2) this place of business must be "fixed", i.e. it must be established at *a distinct place with a certain degree of permanence*;

3) the carrying on of the business of the enterprise through this fixed place of business. This usually means that *persons* who, in one way or another, are dependent on the enterprise (*personnel*) conduct the business of the enterprise in the State in which the fixed place is situated.[48]

Given these three features, companies that sell their goods online (especially IT companies) might generate huge profits in other states without possessing a permanent establishment status there. As a result, these entities are not subject to corporate income tax in these states although the vast of their customers stay there. The emerging digital economy allows businesses to serve their clients without necessarily being physically present and employing staff in a particular state. Thus, if a first criterion is satisfied (a company generates income in another state) but two other criteria do not (a company is neither physically present nor has employees in that state), there is no permanent establishment. Thus, income generated by such companies is *de facto* exempted from taxation.

To tackle this issue, one of the recent proposals of the OECD is to attribute the imposition of a capital income tax not to the fact of a permanent establishment status but to the market where income

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[47] Brian J. Arnold, "Taxation of Nonresidents," in *International Tax Primer,* (Alphen aan den Rijn: Wolters Kluwer, 2019), 65.

[48] "OECD Model Convention 2017 with Commentaries," *supra note*, 12: Page 117, Para. 6 of the Commentaries part.

is generated. This OECD Proposal is dubbed Pillar 1 and suggests the reallocation of taxing rights from home countries to the markets where non-residents actually have business activities and earn profits, regardless of whether firms have a physical presence there.[49] However, this proposal is still implemented in neither the OECD Conventions nor the Ukrainian domestic legal acts to the fullest extent.

Ukraine, primarily, follows a classical approach to a permanent establishment envisaged in Article 5 of the OECD Model Convention. Under Para. 14.1.193 of the TCU, a permanent establishment means a fixed place of business through which the economic activities of a non-resident in Ukraine are fully or partially carried out, in particular: the place of management; branch; office; factory; workshop; installation or structure for natural resource exploration; mine, oil/gas well, quarry or other natural resource extraction site; warehouse or premises used for the delivery of goods, server.

The very last example of a "server" does not repeat the wording of the OECD Model Convention. Assumingly, it reflects a famous tax precedent occurred recently. In 2018, Italy introduced a new rule under which a permanent establishment status results in "a significant and continuous economic presence in the territory of the State built in such a way as not to result in its physical consistency in the territory itself" (Article 162, paragraph 2, f-bis of the Italian Tax Consolidated Text). It has been likely inspired by the OECD Pillar 1 proposal. As a result of this introduction, Netflix, which had a distantly managing streaming server in Italy (cables, streaming blocks, etc.), became obligatory to register its permanent establishment status in Italy despite the absence of Netflix personnel in that state.[50]

Though the OECD Pillar 1 proposal is becoming more and more discussed, however, the prevailing approach to a permanent establishment concept remains the same and includes 1) business activity, 2) physical presence, and 3) operation through a personnel in another state. Furthermore, not only provisions of national tax legislation require assessment in regarding a non-resident as a permanent establishment, but also provisions of a particular double tax treaty between the residence state and the source state. Since the vast of double tax treaties are based upon the framework suggested by the OECD Model Convention, a separate provision in it is supposed to be purely dedicated to the definition of a permanent establishment.

To summarise, residence means a legal link between a taxpayer and a state that allows the latter to impose a certain extent of taxation on a taxpayer. Admittedly, states impose corporate income tax on revenues earned by a legal entity inside the residence state and abroad. It is called taxation of worldwide income. The most common factors in determining tax residence are the place of

[49] "BEPS Action 1: Tax Challenges Arising from Digitalisation," Organisation for Economic Co-operation and Development, accessed 31 July 2023, https://www.oecd.org/tax/beps/beps-actions/action1/
[50] Stefano Loconte and Linda Favi, "A new definition of permanent establishment in Italian domestic income tax law," *Insights* 5, 3 (2018): 7.

incorporation of a legal entity or the place of its management. The problem of juridical double taxation occurs when a resident possesses a permanent establishment status in another state and generates income therein. While the latter (source state) has already taxed the income earned on its territory, the residence state is inclined to impose taxation on the same income again, which causes a juridical double taxation issue.

1.2. Measures to avoid juridical double taxation

As aforesaid, the essence of juridical double taxation constitutes taxing a particular type of income twice. It may lead to an abusive conduct from a taxpayer's side. The willingness to declare the earned income to a tax authority is diminished if the vast part of such income is about to be "confiscated" in the form of tax.[51] Also, there is a risk that legal entities begin seeking tax residence in jurisdictions with low corporate tax rates rather than reside in states where they operate. To avoid the growth of tax havens and the outflow of taxpayers there,[52] the international community, represented by the OECD, created legal mechanisms to alleviate double taxation and introduced them in the OECD Model Convention. The instruments suggested in this document are followed by countries throughout the globe, including Ukraine and the EU Member States.

1.2.1. Bilateral and unilateral measures to avoid double taxation

Article 23A and Article 23B of the OECD Model Convention prescribe exemption and credit double tax relief methods as guidelines while drafting legally binding double tax treaties. These provisions assist the situation in which a resident of one Contracting State derives income from the other Contracting State. Article 23A and Article 23B prescribe taxing rights of the residence state and do not prescribe how the other Contracting State (the income state) has to proceed.[53] Recoursing to a double tax treaty can be named as a bilateral measure to avoid double taxation (in other words, a treaty measure). Subsequently, States are competent to determine the criteria for taxation of income by means of double tax treaties.[54]

Ukraine has concluded 72 double tax treaties overall, covering all 27 Member States of the EU. However, there is a peculiarity concerning Spain. The double tax treaty with Spain was concluded by the Government of the Soviet Union and continues to apply in accordance with Article 7 of the

[51] Ben J.M. Terra and Peter J. Wattel, *European Tax Law*, (Alphen aan den Rijn: Wolters Kluwer, 2008), 181.
[52] "UN Model Convention 2017 with Commentaries," *supra note*, 13: Para. 9 of the Introduction part.
[53] "OECD Model Convention 2017 with Commentaries," *supra note*, 35: Page 378, Para 8 of the Commentaries part.
[54] "Mr and Mrs Robert Gilly v Directeur des services fiscaux du Bas-Rhin, Case C-336/96," EUR-Lex, accessed 18 November 2023, https://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX:61996CJ0336, para. 24.

Law of Ukraine "On Succession of Ukraine"[55] until the entry into force of a new agreement with Spain concluded by Ukraine. Therefore, this agreement still remains applicable in relations with Spain.[56]

The TCU does not impose credit or exemption as a unilateral tax relief for Ukrainian tax residents in case of the absence of a double tax treaty with another country. If there is no double tax treaty between Ukraine and another country,[57] income received by a resident of Ukraine (legal entity) from sources outside of Ukraine is taken into account when determining its object and/or tax base in full.[58]

However, some states provide unilaterally methods to eliminate double taxation in their domestic law if a double tax treaty is not concluded.[59] In this way, a legislator aims to fill a gap caused by the absence of a double tax treaty with a certain state. However, the TCU does not provide a remedy to cover such a gap. It leaves the issue of double taxation unsolved with states that have no double tax treaty in force with Ukraine.

Taxpayers may allege that when one legal entity is granted a double tax relief compared to another legal entity, merely due to the presence of a double tax treaty signed, constitutes discrimination. Treatment of one group of taxpayers worse than others might potentially contravene the non-discrimination policy caused by a situation when tax residents operating in a State, with which no double tax treaty is concluded, are not subject to double tax relief compared to those tax residents who operate in a State covered by a double tax treaty. Equal treatment of all taxpayers regardless of their forms of incorporation, places of origin, and other factors is declared as one of the fundamentals of tax policy according to the TCU. Article 4 of the TCU lists the basic principles of the tax legislation of Ukraine, and one of them is contained in Para. 4.1.2. It is stated that equality of all taxpayers before the law and avoidance of any manifestations of tax discrimination means ensuring the same approach to all taxpayers regardless of social, racial, national, religious affiliation, form of ownership of a legal entity, citizenship of an individual, place of origin of capital.

The CJEU also declares a non-disciminatory approach in tax affairs. In *Saint-Gobain SA,*[60] the CJEU observed the demand for the same treatment to the Swiss company, which operated through a permanent establishment in Germany, applicable to German tax residents. The matter concerned whether the extent of the beneficial treatment of a non-resident was limited to regulation prescribed

[55] "Law of Ukraine On Succession № 1543-XII from 12 September 1991," Parliament of Ukraine, accessed 18 November 2023, https://zakon.rada.gov.ua/laws/show/1543-12?lang=en#Text: Art. 3.
[56] "International agreements of Ukraine on avoidance of double taxation," *supra note*, 4.
[57] "Tax Code of Ukraine," *supra note*, 5: Para. 141.4.9.
[58] *Ibid.*, Para. 13.1.
[59] Institute for Austrian and International Tax Law, *Exemption Method and Credit Method. The Application of Article 23 of the OECD Model* (Vienna, 2022), 4.
[60] "Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt, Case C-307/97," EUR-Lex, accessed 18 November 2023, https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A61997CJ0307.

by the double tax treaty concluded between Germany and Switzerland. The Court by para. 58 stated that "in the case of a double-taxation treaty concluded between a Member State and a non-member country, the national treatment principle requires the Member State which is a party to the treaty to grant to permanent establishments of non-resident companies the advantages provided for by that treaty on the same conditions as those which apply to resident companies", supporting the idea of non-discrimination in the tax domain.[61] However, this case considered equal treatment of non-nationals and nationals, which slighly differs from the present circumstances.

Indeed, it is a default rule that discrimination on the ground of residence is impermissible. The issue is whether the approach remains the same when the different treatment applies within national tax residents. If we observe non-discrimination principle broadly, then, all residents shall be treated as favourably as other residents. But, as it stands at present, non-discrimination in tax domain is limited by the presence of a double tax signed.[62] As a result, it becomes justifiable that national tax residents are subject to different double tax relief given a State where they operate.

1.2.2. OECD Model Convention and UN Model Convention

There are two main bilateral tax treaty recommendatory frameworks to follow by states in their own negotiation practice. Firstly, there is the OECD Model Tax Convention on Income and Capital (aforesaid OECD Model Convention). Secondly, there is a special model convention that considers the peculiarities of developing economies: the UN Model Double Taxation Convention between Developed and Developing Countries (aforesaid UN Model Convention). The latter represents a compromise between the source principle and the residence principle giving more weight to the source principle than does the OECD Model Convention.[63] The UN Model Convention, in its Introduction, announces that it favours retention of greater so-called "source state" taxing rights under a tax treaty - the taxation rights of the host country of investment - as compared to those of the "residence state" of the investor.[64] So, the core difference between both model conventions in the approach that allows attributing a more significant part of a "tax pier" to countries where the income is indeed generated (states with developing economies) in contrast to countries where the legal entities primarily reside (states with developed economies). It is presumed that the OECD Model Convention supports a vice versa division of tax revenues benefiting states of tax residence more.[65]

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[61] Servaas van Thiel, *EU Case Law on Income Tax* (Amsterdam: IBFD, 2001), 451.
[62] Claus Staringer and Herman Schneeweiss, "Tax Treaty Non-Discrimination and EC Freedoms," in in *Tax Treaty Law and EC Law,* Michael Lang, Josef Schuch, and Claus Staringer (Alphen aan den Rijn: Wolters Kluwer, 2007), 229.
[63] "UN Model Convention 2017 with Commentaries," *supra note*, 12: Para. 12 of the Introduction part.
[64] *Ibid*., Para. 3 of the Introduction part.
[65] Sijbren Cnossen "Taxing Corporation in the European Union: Towards a Common Base?" in *Tax Reform in the 21st Century*, John G. Head and Richard Krever (Alphen aan den Rijn: Wolters Kluwer, 2009), 76.

There were several subsequent editions of both conventions. The history of the OECD Model Convention started on 30 July 1963, when the Council of the OECD adopted a recommendation concerning the avoidance of double taxation and called on the governments of the member countries, when concluding or revising bilateral conventions, to conform to a "model convention for the avoidance of double taxation with respect to taxes on income and capital" that had been drawn up by the Fiscal Committee of the OECD and was annexed to that recommendation.

That model tax convention is re-examined and amended regularly. It is the subject of commentaries approved by the OECD Council.[66] The Fiscal Committee and, after 1971, its successor the Committee on Fiscal Affairs, undertook the revision of the 1963 Draft Convention and of the commentaries thereon. This resulted in the publication in 1977 of a new Model Convention and Commentaries to it.[67] Since amendments of the Model Convention from 1977 conducted in 1992, the OECD Model Convention has been updated ten times (in 1994, 1995, 1997, 2000, 2002, 2005, 2008, 2010, 2014 and 2017).[68] On the contrary, the UN Model Convention has fewer updates (1980, 2001, and the last one made in line with the OECD in 2017).[69]

Upon termination of the Soviet Union occupation (24 August 1991),[70] Ukraine concluded the vast double tax treaties with Member States of the EU in the 1990s-2000s. Professor Vdovichena in her monography states that the Ministry of Finance of Ukraine composed their own model double tax treaty to be used while negotiating with other state. Such a “Ukrainian double tax model convention” served as a guideline for negotiators from the Ukrainian side. As stated by Prof. Vdovichena, this negotiable instrument was a mere translated copy of the OECD Model Convention 1992.[71] However, while searching for this model tax treaty online, the only document available in free access is the Order of the Government of Ukraine from 12 November 1993 № 921. Under Paras. 1-2 of this Order, the Government of Ukraine requested the Ministry of Finance to prepare the model convention on double taxation prevention that would serve as a guideline for the Minister of External Affairs while conducting negotiations on the conclusion of double tax treaties between Ukraine and other states.[72] The text of the very model convention, composed by the Ministry of Finance, is not shown by the web search. Perhaps, since this document is intended to be used during negotiations, its text is not freely accessed.

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[66] "N Luxembourg 1 and Others v Skatteministeriet, Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16," EUR-Lex, accessed 18 November 2023, https://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX:62016CJ0115, Para. 3.
[67] "OECD Model Convention 2017 with Commentaries," *supra note*, 12: Para. 7 of the Introduction part.
[68] *Ibid*., Para. 11.2 of the Introduction part.
[69] "UN Model Convention 2017 with Commentaries," *supra note*, 13: Paras. 8-11 of the Introduction part.
[70] "Constitution of Ukraine № 254к/96-ВР adopted on 28 June 1996," Parliament of Ukraine, accessed 24 July 2023, https://zakon.rada.gov.ua/laws/show/254%D0%BA/96-%D0%B2%D1%80?lang=en#Text
[71] Vdovichena, *supra note*, 14: 81.
[72] "Order of the Government of Ukraine on the organisation of work on the preparation of international agreements on the avoidance of double taxation of income and property and the prevention of tax evasion from 12 November 1993 № 921," Parliament of Ukraine, accessed 24 July 2023, https://zakon.rada.gov.ua/cgi-bin/laws/main.cgi?nreg=921-93-%EF#Text.

Nevertheless, the Supreme Court of Ukraine in the *Polpharma S.A.*-case (which concerned the "permanent establishment" concept under the double tax treaty between Ukraine and Poland) reiterated the position of Prof. Vdovichena, mentioning that "the Court takes into account provisions of the Commentary to the OECD Model Convention while interpreting a double tax treaty since the latter has been signed based on the OECD Model Convention". In addition, the Supreme Court substantiated its approach by referring to Art. 31(1) of the Vienna Convention on the Law of Treaties, under which "a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose".[73] Thus, the OECD Model Convention might be considered as *travaux préparatoires* for double tax treaties concluded between Ukraine and the EU Member States.

The issue of the *Polpharma S.A. case* is that the Supreme Court did not clarify which version of the OECD Model Convention and its Commentaries exactly should have been considered. The Supreme Court referred to several provisions of the OECD Commentaries without mentioning the year of their edition. On the one hand, it could be indeed the OECD Model Convention edited in 1992 since the double tax treaty between Ukraine and Poland was concluded in 1993.[74] On the other hand, since the *Polpharma S.A. case* was rendered by the Supreme Court in 2019, upon the last update of the OECD Model Convention, it could be the edition issued by the OECD in 2017.

Which year edtion of the OECD Model Convention shall apply has become a matter in the case *N Luxembourg 1 and Others v Skatteministeriet* of the Court of Justice of the European Union (hereinafter – CJEU).[75] If the *Polfarma case* concerned the definition of a "permanent establishment" under the Polish-Ukrainian double tax treaty, the *Luxembourg case* issue was on defining a "beneficial owner" under the EU Directive 2003/49 on interest and royalty. One of the parties in *Luxembourg* stated that "the concept of beneficial owner contained in the Directive 2003/49 requires interpretation within the meaning of the OECD 1977 Model Tax Convention and the commentaries relating thereto. *A dynamic interpretation would be contrary to the principle of legal certainty*".[76] Nevertheless, the CJEU disagreed with this reasoning and did not opt for the static interpreter doctrine. The CJEU supported the doctrine of the dynamic interpreter emphasizing that "the concept of "beneficial owner", which appears in the bilateral conventions based on the OECD Model Tax Convention, and *the successive amendments of that model and of the commentaries* relating thereto *are relevant when interpreting* EU Directive 2003/49".[77]

[73] "Judgement № 826/3192/13-a from 13 June 2019 (Polpharma S.A.)," *supra note*, 14.
[74] "Double tax treaty between Ukraine and Poland № 616_168 from 12 January 1993," Ministry of Finance of Ukraine, accessed 18 October 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.
[75] "N Luxembourg 1 and Others v Skatteministeriet," *supra note*, 48.
[76] *Ibid.*, Para. 76.
[77] *Ibid.*, Para. 90.

Following the approach of the CJEU, the successive amendments shall serve as an instrument of interpretation of concluded double tax treaties between Ukraine and the EU Member States. The context of the 1990s-2000s years, when the vast of the above-mentioned bilateral agreements were drafted, did not take into account the emerging danger of tax heavens, tax conduits, treaty-shopping, and other abusive practices, aiming eventually to erose the tax base and to shift profits to other jurisdictions. Abusive tax practices became widely discussed in the international community in the 2010s when the OECD commenced its work on the Base Erosion and Profit Shifting Project (hereinafter - BEPS). In particular, it resulted in the amended OECD Model Convention in 2017.[78] Interpretation of double tax treaties based on the OECD Model Convention present in times of double tax treaties conclusion would neglect the context in which legal entities operate today. Furthemore, the text of Article 23A and Article 23B, regulating double tax relief, has not been amended by the OECD since 1992.[79] Thus, the last updated version of the OECD Model Convention 2017 and its Commentaries serve as the basis for this research.

1.2.3. Double tax relief methods

To alleviate the double taxation, the OECD Model Convention the exemption (Article 23A) and credit methods (Article 23B). Pursuant to Article 23A, where a resident of a Contracting State derives income which may be taxed in the other Contracting State, the first-mentioned State shall *exempt such income from tax*. Under Art. 23B, where a resident of a Contracting State derives income which may be taxed in the other Contracting State, the first-mentioned State shall allow, as *a deduction from the tax* on the income of that resident, an amount equal to the income tax paid in that other State. However, in doctrine, three main methods are described. There are the exemption, credit, and deduction tax reliefs:

1) Exemption method: under this method, the residence state does not tax the foreign income of its tax residents. Foreign income is said to be exempt.

2) Credit method: here, the income earned from the overseas state is taxed in the residence state. The foreign tax paid is then credited against the tax on the income charged by the residence state. Thus, the residence state gives credit for the foreign tax suffered.

3) Deduction method: under the deduction method, foreign taxes are treated as an expense of doing business. The residence state taxes the foreign income, but allows a deduction from the foreign income for any foreign taxes paid.[80]

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[78] "OECD Model Convention 2017 with Commentaries," *supra note*, 12: Para. 11.2 of the Introduction part.

[79] "Model Tax Convention on Income and on Capital: Condensed Versions 1992-2017," Organization for Economic Co-operation and Development, accessed 18 November 2023, https://www.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-september-1992_mtc_cond-1992-en

[80] Oats, *supra note*, 11: 97.

In other words, the *exemption* method prescribes that a residence state only taxes income earned in this state. Thus, instead of worldwide taxation, which is usually a prerogative for a residence state, the latter does not take into account the income earned abroad while calculating the tax base. The *credit* method allows a residence state to tax the worldwide income but with some peculiarities. The tax amount to be paid on the worldwide income in the residence state is decreased by the tax paid abroad. Thus, the tax paid abroad is deducted (credited), which results in lessening of the tax to be paid.

In essence, the difference between exemption and credit methods constitutes the amount of a tax base.[81] If the exemption method applies, the tax base equals to the income generated only in the state of tax residence. If the credit method applies, the tax base amounts to the income earned in the tax residence and in another state (there is a so-called worldwide income). The *deduction* method taxes a worldwide income; however, the tax paid abroad is deducted not from the computed tax obligation to be paid, like with the credit method, but from the tax base as an expense. Therefore, the tax base is lessened. The legal literature primarily describes peculiarities of exemption and credit methods, omitting deduction since only exemption and credit are prescribed by the OECD Model Convention.[82]

In practice, both exemption and credit methods are divided into two different systems: the "full exemption" - "exemption with progression" and "full credit" - "ordinary credit".[83] While the OECD Convention determines the basics of exemption and credit methods, states modify them according to their economic needs. These four modifications result in different amounts of the tax obligation to be paid in a residence state.[84]

The difference between the *full exemption* and *exemption with progression* is the tax rate applicable at the residence state. If the exemption with progression method applies, the tax rate in the residence state is higher while the tax base stays the same and amounts to the income earned in the residence state. The difference between the *ordinary credit* and *full credit* methods constitutes the tax amount to be deducted. The ordinary credit is applicable if the tax rate abroad is higher than the domestic tax rate. When the ordinary credit applies, it is calculated how much tax could be paid if the same amount of income earned abroad would be earned in the residence state. Then, instead of deducting the tax indeed paid abroad, a taxpayer shall deduct the tax calculated.[85] On the contrary, whether the tax rate in another state is higher than in the residence state is irrelevant while applying

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[81] Christiana Hji Panayi, *European Union Corporate* Tax Law (Cambridge University Press, 2013), 214.
[82] Institute for Austrian and International Tax Law, *supra note*, 45: 10.
[83] "Elimination of double taxation," Erasmus University Rotterdam, accessed 31 July 2023, https://pure.eur.nl/en/publications/elimination-of-double-taxation-relief-credit-vs-exemption
[84] Geoffrey Morse and David Williams, *Principles of Tax Law* (London: Sweet & Maxwell, 2004), 89.
[85] Brian J. Arnold and Michael J. Mclntyre, "Double Taxation Relief," in *International Tax Primer,* Brian J. Arnold and Michael J. Mclntyre (Alphen aan den Rijn: Wolters Kluwer, 2002), 34.

the full credit method. The tax actually paid abroad is deducted from the tax to be paid in the residence state. Thus, the full credit applies regardless of the differences in tax rates. If the tax rate abroad is not higher than the domestic tax rate, the practical difference between the full and ordinary credit methods is inexistent.[86]

The OECD Model Convention describes precisely mechanisms of the full exemption (Article 23A) and ordinary credit methods (Article 23B). Article 23A prescribes exempting income earned abroad without applying a higher tax rate at home. Article 23B allows deducting the tax paid abroad not fully but upon a certain level. Under this provision, "such deduction shall not exceed that part of the income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in that other State". Nevertheless, provisions of the OECD Model Convention have an advisable nature and serve merely as a persuasive one but still a guiding legislative tool (soft law).[87]

Pursuant to the TCU, a Ukrainian taxpayer may be granted only an ordinary credit method as a double tax relief while computing tax obligations in Ukraine. The ordinary credit method applies only if there is a double tax treaty concluded between Ukraine and another State. The issue of the operation of Ukrainian permanent establishments in a State that has no double tax treaty concluded with Ukraine remains unsolved. Further observations of double tax treaty provisions between Ukraine and the EU Member States demonstrate that they indeed prescribe a credit method for a Ukrainian taxpayer to apply. Not only does the TCU specify a credit method under these treaties as an ordinary credit method, but it also prescribes a specific bureaucratic procedure to prove the amount of tax paid abroad.

Under para. 141.4.9. of the TCU, amounts of corporate income tax paid by Ukrainian legal entities abroad are credited when they compute a taxable burden (the tax amount to be paid in Ukraine). *The amount of a tax credit* from a foreign source during a tax (reporting) period *cannot exceed the amount of tax payable in Ukraine* by such a taxpayer during such period. It means that if a tax rate abroad is higher than a domestic tax rate (18 %)[88], the lower domestic tax rate applies for the purposes of crediting. Thus, if a taxpayer earned abroad 80,000 and paid 16,000 as tax because of the 20% tax rate abroad, Ukraine will not allow to deduct the 16,000 paid. The amount of credit will be less due to the application of a domestic lower tax rate (18 %). So, Ukraine will grant as credit only 14,400 instead of the 16,000 actually paid.

Crediting is carried out on the conditions of 1) *submission of written confirmation* from the controlling authority of another state regarding the fact of payment of such tax, and 2) *existence of a*

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[86] Institute for Austrian and International Tax Law, *supra note*, 45: 5; "OECD Model Convention 2017 with Commentaries," *supra note*, 12: Page 382-383, Paras. 14-16 of the Commentaries part.
[87] Augusto Fantozzi, "Harmonization in the Tax Field," in *Tax Competition in Europe,* Wolfgan Schon (Amsterdam: IBFD, 2003), 127.
[88] "Tax Code of Ukraine," *supra note*, 5: Para. 136.1.

valid international treaty of Ukraine on the avoidance of double taxation of income. Under Para. 13.5 of the TCU, a taxpayer shall obtain from the authority of a foreign state (where income is received) a document/certificate that confirms the amount of tax paid, as well as the tax base and tax object. This document is subject to legalisation in the relevant country or in the relevant foreign diplomatic institution of Ukraine unless otherwise stipulated by the current international treaties of Ukraine. Given the Note of the Ministry of Justice of Ukraine, in case Ukraine has concluded with a state a bilateral agreement on legal aid, which cancels the requirement of legalisation of official documents, such documentary legalisation (consular legalisation or apostille certification) is not required. Translation of a document is sufficient for its further submission to the Ukrainian authorities. Pursuant to the Ministry of Justice, this simplified procedure relates to a number of the EU Member States (e.g., Bulgaria, Estonia, Latvia, Lithuania, Poland, Romania, and the Czech Republic).[89]

Thus, a Ukrainian tax resident operating abroad might take advantage only of an ordinary credit method according to the valid double tax treaty between Ukraine and the EU Member State. A Ukrainian taxpayer shall have a legalized confirmation of a tax obligation paid abroad from a foreign tax authority to be granted a double tax relief in Ukraine.

To summarise, double taxation is divided into economic and juridical, domestic and international, depending on the grounds of such a typology. This thesis concentrates on international legal (juridical) double taxation caused by the operation of a tax resident on markets located inside and outside its state of residence. Double tax relief methods such as exemption, credit, and deduction alleviate the burden imposed on a taxpayer. Neither income nor tax paid abroad is taken into account by fiscal authorities in a residence state applying the exemption method. Tax paid abroad is deducted as an expenditure from the tax base in a state of residence undertaking deduction method. Tax paid abroad is deducted from the computed tax to be paid on the worldwide income if the credit method applies. The TCU prescribes that the ordinary credit to alleviate double taxation if a double tax treaty is concluded with a foreign state.

[89] "Note of the Ministry of Justice of Ukraine on the application of international treaties of Ukraine on legal aid in the part that concerns the cancellation of the requirement for legalisation of official documents issued by the competent authorities of the Contracting Parties № 26-26/291 from 11 May 2020," Parliament of Ukraine, accessed 24 July 2023, https://zakon.rada.gov.ua/laws/show/v_291323-10#Text.

CHAPTER 2. DOUBLE TAX RELIEF MECHANISM IN PRACTICE: UKRAINE AND EU MEMBER STATES

The main interest of a taxpayer is to eliminate fully, and not only partially mitigate double taxation. Thus, the most beneficial double tax relief might be traced only through actual calculations.

This chapter observes the advantages and drawbacks of double tax relief methods from the perspective of a state and taxpayer. Additionally, this chapter invents formulas to calculate the tax amount at the residence state when the exemption and credit methods apply. Abbreviations in formulas will be marked as follows:

1) Income earned in the residence state ("**RI**"), - residence income;

2) Income earned in the source state ("**SI**"), - source income;

3) Tax rate of the residence state ("**RT**"), **-** residence tax;

4) Tax rate of the source state ("**ST**"), **-** source tax**;**

5) Tax amount that a taxpayer pays in its residence state ("**TB**"), **-** tax burden**.**

6) "**Threshold**" means the amount of the income, earned in the residence state and the source state together, that shall be exceeded by a taxpayer to apply a higher tax rate to the income earned in the residence state (relevant for the exemption with progression method).

Suppose that a Ukrainian tax resident earns 80,000 in Ukraine and 20,000 abroad (in "State B"). The corporate tax rate in Ukraine is 18%, according to Para. 136.1 of the TCU. Assumingly, the corporate tax rate in State B is 25%.[90] As an alternative, the corporate tax rate in State B is 15%[91] to demonstrate the outcome if a corporate tax rate is lower in the source state than in the residence state.

No double tax relief. Assuming there is no double tax relief between Ukraine and State B. Thus, a Ukrainian taxpayer is subject to worldwide income taxation at an 18% rate. The formula to calculate the tax obligation in the residence state should no double tax relief be applicable is suggested. The formula for taxes to be paid in the state of residence ("TB") is the following:

(RI + SI) × RT = TB.

Practical application of the formula:

[90] 25% rate is exemplary in the paragraph. However, a 25% corporate tax rate is present in such EU Member States as Belgium and France, see: "Corporate Tax Rates around the World, 2019-2023," Deloitte Highlights, accessed 18 November 2023, https://www2.deloitte.com/content/dam/Deloitte/global/Documents/Tax/dttl-tax-corporate-tax-rates-2019-2023.pdf.

[91] 15% is a corporate tax rate in Lithuania, see Art. 5(1)(1) of Lithuania Law on Corporate Income Tax, *supra note*, 25; Furthermore, the OECD considers 15% as an optimal corporate tax rate and suggests this amount for countries to follow in their tax policy in the Pillar 2 Project Proposal, see Organization for Economic Co-operation and Development. *Tax Challenges Arising from Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project* (Paris, 2021).

Table 1.1. (ST is 25%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	100,000	20,000
Tax rate	18% ("RT")	25% ("ST")
Tax burden	**18,000 ("TB")**	5,000
Overall	23,000	

Table 1.2. (ST is 15%)

	Ukraine	State B
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	100,000	20,000
Tax rate	18% ("RT")	15% ("ST")
Tax burden	**18,000 ("TB")**	3,000
Overall	21,000	

2.1. Exemption method application

The exemption method is deemed the most beneficial for a taxpayer. In this method the tax residence blurs since taxation is imposed only on the income earned at home. On the contrary, the exemption with progression enables a state to obtain at least partial "benefit" of a worldwide income of its tax resident. The difference between the exemption and exemption with progression methods is seen in the calculation below.

2.1.1. Full exemption

Under this method, the income earned abroad is not taxed in the residence state. The formula for the tax amount to be paid in the residence state ("TB") is the following:

RI × RTR = TB.

Practical application of the full exemption method:

Table 2.1. (ST is 25%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	80,000	20,000
Tax rate	18% ("RT")	25% ("ST")
Tax burden	**14,400 ("TB")**	5,000
Overall	19,400	

Table 2.2. (ST is 15%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	80,000	20,000
Tax rate	18% ("RT")	15% ("ST")
Tax burden	**14,400 ("TB")**	3,000
Overall	17,400	

The tables demonstrate that the tax burden is substantially alleviated compared to the previous example where no double tax relief is present.

2.1.2. Exemption with progression

To apply this method, the progressive tax rate shall be introduced in domestic law. Though the Ukrainian tax rate is flat and does not depend on the amount of income earned, for this example, we assume that if the worldwide income of a Ukrainian taxpayer is less than 90,000, the tax rate is 18%. Conversely, when the income is equal and above 90,000, the tax rate applicable becomes 25%.[92] Thus, 90,000 serves for the purpose of a threshold in this example.

The exemption with the progression method supposes that the tax base stays the same as in the full exemption method. The tax base in the residence state is not increased by the income earned abroad. However, the tax rate goes up. Therefore, the tax rate of 20% applies to the tax base of 80,000.

If the total income earned in the two states does not exceed the limits established by a legislator for applying a higher tax rate (for instance, the income in State B is 10,000 and the total income in two state is 90,000), the tax rate remains 18%.

The formula for the tax amount to pay in the residence state ("TB") is the following:

If SI+RI < or = the threshold, then:

RI × RTR = TB.

If SI+RI > the threshold, then:

RI × RT ↑ (increased) = TB.

Practical application of the exemption with progression method:

[92] Ukraine does not apply a progressive tax rate. However, the global tax practice is aware of countries where a progressive tax rate is applicable. For instance, the Dutch tax rate becomes 25.8% should an annual income exceed the bracket of EUR 395,000. If the income is below this level, the corporate tax rate is 15% (the information provided is valid for 2022); see "Taxes on corporate income in the Netherlands," PwC Worldwide Tax Summaries, accessed 18 November 2023, https://taxsummaries.pwc.com/netherlands/corporate/taxes-on-corporate-income.

Table 3.1. (ST is 25%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	80,000	20,000
If (RI + SI) < or = 90 000 *then*:		
Tax rate	18% ("RT")	25% ("ST")
If (RI + SI) = or > 90 000 *then*:		
Tax rate	25% ("RT ↑")	25% ("ST")
Tax burden	**20,000 ("TB")**	5,000
Overall	25,000	

Table 3.2. (ST is 15%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	80,000	20,000
If (RI + SI) < 100 000 *then*:		
Tax rate	18% ("RT")	15% ("ST")
If (RI + SI) = or > 100 000 *then*:		
Tax rate	25% ("RT ↑")	15% ("ST")
Tax burden	**20,000 ("TB")**	3,000
Overall	23,000	

Contrary to the full exemption, the exemption with the progression method puts a taxpayer even in a worse position compared to the absence of any double tax relief method in force between two states. However, the issue lies in the amount of a tax rate applicable and the brackets of the income to invoke a higher tax rate. For instance, such an amount might be equal not to 90,000, which is a rather small threshold to apply a tax rate of 25%, but around 400,000, like in the Netherlands.[93] Moreover, instead of the increased tax rate of 25%, the higher rate might be slightly less, for instance, 20%. This changed number indeed makes a substantial difference in the level of a tax burden imposed:

Table 4.1. (ST is 25%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	80,000	20,000
If (RI + SI) < 100 000 *then*:		
Tax rate	18% ("RT")	25% ("ST")
If (RI + SI) = or > 100 000 *then*:		
Tax rate	20% ("RT ↑")	25% ("ST")

[93] *Ibid.*

Tax burden	**16,000 ("TB")**	5,000
Overall		21,000

Table 4.2. (ST is 15%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	80,000	20,000
If (RI + SI) < 100 000 *then*:		
Tax rate	18% ("RT")	15% ("ST")
If (RI + SI) = or > 100 000 *then*:		
Tax rate	20% ("RT ↑")	15% ("ST")
Tax burden	**16,000 ("TB")**	3,000
Overall		19,000

Thus, a legislator shall properly consider the thresholds of a worldwide income to impose a higher tax rate in regard to the exemption with the progression method. Otherwise, it risks disincentivising a taxpayer from operating in another jurisdiction or even causing it to switch tax residence to another jurisdiction.[94]

Progressive tax rate. Though the TCU provides a progressive tax rate neither for legal entities nor for natural persons, currently, there is a legislative proposal in the Parliament of Ukraine to impose a progressive tax rate. However, it shall only concern the income of natural persons. The rates are expected to be 9%, 18%, and 25%, depending on the amount of income earned.[95] There was another bill suggesting the introduction of a progressive tax rate for individuals' incomes in 2020.[96] Some Ukrainian legal scholars also support the idea of a progressive tax rate but only for natural persons. They substantiate it with the requirement of social justice, prescribed by the Constitution of Ukraine alongside the TCU, and the ability of a natural person to pay a particular tax.[97]

Parliament does not suggest a progressive tax rate for legal entities. Perhaps, it might be attributed to the fear of losing legal entities (large taxpayers) if a tax rate gets higher than 18%. Large taxpayers, particularly multi-national corporations, tend to change the residence state if the tax rate

[94] In some cases, business is indeed reluctant to face a high tax burden even though a residence state suggests a prosperous investment climate with zero tolerance for corruption, effective work of administrative authorities, a stable economy, etc. For instance, a Swedish company, IKEA, transferred its headquarters from Sweden to the Netherlands for tax purposes, see "IKEA," Britannica, accessed 08 October 2023, https://www.britannica.com/topic/IKEA.

[95] "Legislative Proposal on Introduction of a Progressive Tax Rate № 7406 from 25 May 2022," Parliament of Ukraine, accessed 18 November 2023, https://itd.rada.gov.ua/billInfo/Bills/Card/39660.

[96] "Legislative Proposal on Introduction of a Progressive Tax Rate № 2758-1 from 06 February 2020," Parliament of Ukraine, accessed 18 November 2023, http://w1.c1.rada.gov.ua/pls/zweb2/webproc4_1?pf3511=68075.

[97] Anastasiya Klimova, "Implementation of the progressive tax rate in the Ukrainian taxation system," paper presented at the scientific conference organised by Ternopil National Economic University, Ternopil, May 2020.

becomes burdensome. To stimulate businesses stay in Ukraine,[98] a legislator should not impose a higher tax rate on a legal entity if the latter earns more than its competitors.

Nevertheless, progressive corporate tax rates are indeed present in tax legislations in a number of EU Member States. As an example, there are Austria, Germany, Luxembourg, and the Netherlands.[99] For instance, the latter applies a 25.8% tax rate to the income above EUR 395,000 and 14% for the income below this amount.[100] A first glance at the list of these states reveals that they possess stable, well-developed economies, so their markets are full of viable legal entities. Thus, they may tax corporations differently, depending on the amount of income earned worldwide, without a substantive risk that they switch their tax residence to another state.

2.1.3. Advantages of the exemption method

In essence, only the full exemption method eliminates double taxation since it does not require consideration of the income earned abroad in the residence state. Other methods merely mitigate double taxation, allowing the residence state to impose taxation on at least some percentage of the income earned outside the residence state. Furthermore, the application of this method by states would ease bureaucratic and financial burden imposed. Tax observer R. Rohatgi suggests the following advantages of the full exemption method:

1. It is the least complex administratively;
2. It avoids dealing with two tax authorities;
3. It eliminates actual double taxation.[101]

This method is deemed beneficial for a taxpayer and might be followed by some states to encourage entities' incorporation under their fiscal jurisdiction. A state aiming to exempt income earned abroad from taxation might provide this provision as a unilateral relief in its national tax legislation or in double tax treaties concluded with certain states. Additionally, it stimulates taxpayers to operate in some particular foreign jurisdictions. Since Ukraine declares its objective to integrate into the European economic agenda with the aim of gaining membership in the European Union,[102] it might be possible to consider exempting income obtained by Ukrainian taxpayers from the EU. This incentive might stimulate Ukrainian tax residents to join the EU market and integrate Ukrainian businesses into the European economic agenda.

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98 Especially given the ongoing full-scale aggression against Ukraine carried out by russia.
99 Karoline Spies and Philipp Walter Scharizer, "Chapter 9: Exemption Method with Proviso Safeguarding Progression," in *Exemption Method and Credit Method,* Georg Kofler et al. (Vienna: Vienna University Press, 2021), 13.
100 "Taxes on corporate income in the Netherlands," PwC Worldwide Tax Summaries, accessed 18 November 2023, https://taxsummaries.pwc.com/netherlands/corporate/taxes-on-corporate-income.
101 Ray Rohatgi, *Basic International Taxation. Volume 1: Principles* (London: BNA International Inc, 2005), 71.
102 "Law of Ukraine On the Principles of Domestic and Foreign Policy № 2411-VI adopted on 01 July 2010," Parliament of Ukraine, accessed 18 November 2023, https://zakon.rada.gov.ua/laws/show/2411-17?lang=en#Text, Art. 11(2).

The Lithuanian example can be taken into cognisance. Under Art. 55(1) of the Law of Lithuania on Corporate Income Tax, the income of a tax-resident company is not subject to taxation in Lithuania should it be received from activities through a permanent establishment in a foreign country that is in the European Economic Area or that has a double tax treaty with Lithuania and if the income has already been subject to taxation there.[103] This provision might be considered by a Ukrainian legislator while reforming its double taxation preclusion policy. Objectively, only a few Ukrainian taxpayers operate abroad, especially in the European Union.[104] Exempting the income generated in the EU from taxation may incentivise Ukrainian taxpayers to commence economic activity in Europe.

2.1.4. Shortcomings of the exemption method

Following tax observer R. Rohatgi's observations, the disadvantages of this method might be presented as follows:

1. It reduces the tax revenues due to the residence state;
2. It encourages the use of low-tax countries or tax heavens;
3. It requires detailed financial statements if exemption is given with progression.[105]

So, firstly, in view of being territorially small or having a limited population, some countries are reluctant to fully exempt income earned abroad by their tax residents. It can be merely for the objective inability to generate a decent amount of income in their states. Secondly, as a result of having income earned abroad exempted from taxation at home, taxpayers might shift the vast proportion of their income abroad. In particular, to countries where a tax rate is much lower than in the residence state.[106] To alleviate these issues, the exemption with progression method aims to prevent taxpayers from enjoying the benefits of lower tax brackets by ensuring that a portion of their income is earned in a foreign jurisdiction.[107] However, the exemption with progression diminishes administrative simplicity often attributed to the exemption method since the state will not grant exemption unless it is unaware of the income earned worldwide by its tax resident. Moreover, the calculation presented in this Chapter showed that the exemption with the progression method might even increase the tax burden imposed on a taxpayer depending on the amount of a tax rate to be imposed on a taxpayer in its residence state.

[103] "Law of Lithuania on Corporate Income Tax," *supra note*, 25.
[104] O.I. Duma and K.O. Zavtura, "Startup ecosystem in Europe: best practices and lessons for Ukraine," *Management and entrepreneurship in Ukraine: stages of formation and problems of development* 3, 1 (2021): 127.
[105] Rohatgi, *supra note*, 80: 71.
[106] Michael Schilcher, "Exemption Method and Community Law," in *Tax Treaty Law and EC Law,* Michael Lang, Josef Schuch, and Claus Staringer (Alphen aan den Rijn: Wolters Kluwer, 2007), 153.
[107] Institute for Austrian and International Tax Law, *supra note*, 40: 5.

To summarise, it might be recommendatory for the Ukrainian legislator to substitute the ordinary credit method with the full exemption. Since one of the declared policy objectives of Ukraine is to establish strong economic ties with the EU, a Ukrainian taxpayer should be allowed to fully exempt its income earned in the EU from taxation in Ukraine. A similar approach is maintained in Lithuania regarding the income earned by Lithuanian taxpayers in the European Economic Area through a permanent establishment. This practice can serve as an example for the Ukrainian legislator to follow during the tax reform.

2.2. Credit method application

For the credit method, the residence state calculates the tax base amounting to the income earned in two states. However, the residence state allows the deduction of taxes paid abroad from the tax obligations to be paid at home. This method is divided into the full credit and ordinary credit subtypes. The difference between them is traced only if the tax rate abroad is higher than the domestic tax rate. To demonstrate the difference, formulas and calculations are provided below. We similarly assume that a Ukrainian tax resident earns 80,000 at home and 20,000 abroad (State B). The corporate tax rate in Ukraine is 18%, while the corporate tax rate in State B is 25% or 15%. The abbreviation for formulas:

1) income earned in the residence state is "**RI**" (residence income);
2) income earned in the source state is "**SI**" (source income);
3) tax rate in the residence state is "**RT**" (residence tax);
4) tax rate in the source state is "**ST**" (source tax);
5) tax amount that a taxpayer pays in the residence state is "**TB**" (tax burden).

Further observations illustrate that the tax rate in the source state (ST) substantially impacts the amount of tax to be paid in the residence state (TB). This aspect makes the credit method different from the previous exemption method observed.

2.2.1. Full credit

This subtype of the credit method requires deducting taxes paid abroad from the tax obligations in the residence state. In comparison with the exemption example, the formula to apply the full credit method looks more complex:

((RI + SI) × RT) – (SI × ST) = TB

Practical application of the full credit method:

Table 4.1. (ST is 25%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	100,000	20,000
Tax rate	18% ("RT")	25% ("ST")
Tax burden	**13,000 ("TB")**	5,000
Overall	18,000	

Table 4.2. (ST is 15%)

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	100,000	20,000
Tax rate	18% ("RT")	15% ("ST")
Tax burden	**15,000 ("TB")**	3,000
Overall	18,000	

Given results, the full credit method benefits a taxpayer more than the full exemption in case the tax rate abroad is higher than the domestic tax rate. Conversely, the full exemption allows a taxpayer to pay less overall tax if a domestic tax rate is lower than the tax rate abroad.

However, there is no sense for a state to opt for the full credit method instead of the full exemption as it imposes an additional administrative burden on a taxpayer. The full credit requires a taxpayer to provide documents, like tax declarations, etc. Such proofs are submitted to confirm the amount of the income earned and the tax paid abroad. Also, it causes an administrative burden for a state itself given the necessity to verify tax documentation from a foreign jurisdiction.

2.2.2. Ordinary credit

This double tax relief differs from the previous subtype with the tax rate applicable to the income earned in the source state. If the tax rate in the source state is above the tax rate in the residence state, the latter applies for the purpose of deduction. Therefore, the formula for the tax burden in the residence state ("TB") encompasses two steps:

If RT < ST or RT = ST, *then*:

((RI + SI) × RT) – (SI × <u>RT</u>) = TB

If RT > ST, *then*:

((RI + SI) × RT) – (SI × <u>ST</u>) = TB

The RT and ST are marked to demonstrate the crux of the difference. Practical application of the ordinary credit method is following:

Table 5.1. (ST is 25%)

((RI + SI) × RT) – (SI × RT) = 18,000 – 3,600 = TB

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	100,000	20,000
Tax rate	18% ("RT")	25% ("ST")
Tax burden	**14,400 ("TB")**	5,000
Overall	19,400	

Table 5.2. (STR is 15%)

((RI + SI) × RT) – (SI × RT) = 18,000 – 3,000 = TP

	Ukraine	*State B*
Income earned	80,000 ("RI")	20,000 ("SI")
Tax base	100,000	20,000
Tax rate	18% ("RT")	15% ("ST")
Taxes to be paid	**15,000 ("TB")**	3,000
Overall	18,000	

Table 5.2. (full credit), with the tax rate in the source state below the tax rate in the residence state, has no difference compared to Table 4.2 (ordinary credit). The difference felt by a taxpayer occurs only in case a foreign jurisdiction taxes entities in a more "severe" way than a domestic jurisdiction. Actually, a taxpayer experiences a double burden since it is not only imposed a higher tax rate abroad but also should leave some extent of the tax paid abroad not covered by a double tax relief. Consequently, the ordinary credit method provides more incentives to a national treasury than to a tax resident. To "convert" the ordinary credit into the full credit, a taxpayer should opt for a jurisdiction with a lower corporate tax rate compared to a domestic one.

2.2.3. Advantages of the credit method

Para. 14.1.9. of the TCU prescribes the application of ordinary credit methods in relation to Ukrainian taxpayers – legal entities that operate in countries with which Ukraine concluded double tax treaties. The full credit method seems to be one of the most beneficial for a taxpayer, especially in regard to a high tax rate applicable in the source state. The full credit method does not discourage a taxpayer from pursuing their activity in jurisdictions with high tax rates but even "encourages" it, allowing deduction of the tax paid abroad to the fullest extent. However, this method remains unpopular in double-tax treaties practice among states.[108]

On the contrary, ordinary credit suggests more beneficial treatment for a resident state rather than for a taxpayer. The latter still has some part of their income taxed twice since the resident state

[108] Bendlinger, *supta note*, 20.

allows dedication by applying its domestic tax rate and not a tax rate of the source state. The difference between the full credit and ordinary credit is inconsistent only if a tax rate abroad is the same or less than the tax rate of the residence state.[109] The residence state claims its right to the precise part of a "tax pier". A less obvious advantage of a credit method is the possibility to trace states in which tax residents operate the most. This rather sociological data allows to examine the reasons why tax residents opt for particular jurisdictions to operate in and to shift some parts of their profits there. Perhaps, it may be reasoned by the geographical proximity to the residence state, or by more beneficial conditions for business conduct. The experience of states where tax residents operate the most might serve as an example of a policy to follow and implement since tax residents consider it as favourable.

2.2.4. Shortcomings of the credit method

The credit method is complex in its calculations and application. This method is ratherbureaucratic. Given Para. 14.1.9 and 13.5 of the TCU, a taxpayer shall obtain the document that confirms the amount of tax paid abroad from a foreign fiscal authority. Afterwards, this document shall be translated, legalised (consular legalisation or apostille certification done unless there is a convention on legal aid between countries that does not require it), and, eventually, submitted to the Ukrainian tax office. The procedure is long-lasting. It may end up in double taxation if a taxpayer does not succeed in obtaining needed documents on time. There is no guarantee that a tax authority from the EU Member State would operate rather quickly to provide the documental confirmation of a tax paid. Additionally, the legalisation of this document is also a time-consuming process.

As observed above, unlike the Ukrainian legislator, the Lithuanian lawmaker follows another approach and prescribes the income earned in the European Economic Area or in a country with which Lithuania has a double tax treaty to be exempted from taxation in Lithuania if a Lithuanian taxpayer possesses a permanent establishment there. Such an approach alleviates an administrative burden that might be imposed on a taxpayer who tries to prove that they indeed had paid taxes abroad.

Secondly, an administrative burden can be experienced by a taxpayer if the periods for tax declaration and tax payments differ. Some countries collect taxes in advance by way of monthly, quarterly or biannual payments. The final tax assessment takes place after the end of the year, and depending on the assessment, any excess collected taxes are refunded to the taxpayers. Such practice of collecting taxes in advance creates uncertainty around the amount of credit that the residence state is obliged to grant since there might be a significant time gap between the assessment and the final

[109] Walter Loukota, "The Credit Method and Community Law," in *Tax Treaty Law and EC Law,* Michael Lang, Josef Schuch, and Claus Staringer (Alphen aan den Rijn: Wolters Kluwer, 2007), 125.

refund. In such a situation, the Commentary on the OECD Model Convention recommends a freehanded approach, by which states are at liberty to apply their "own legislation and technique".[110] Thus, regulation of this time discrepancy is still left to the two states, leaving a taxpayer in an unsure position.

Thirdly, compared to the full exemption, the ordinary credit method does not eliminate double taxation but merely mitigates it to some extent. The residence state still takes into account income earned abroad and partially taxes it if a tax rate in the source state is higher than a domestic tax rate.[111] It discourages companies from joining the markets with high tax rates. In general, states with high tax rates possess the most developed economies. It would allow to obtain more revenues for a taxpayer by imposing higher prices for customers in those states. One of the most obvious examples is Scandinavian states. However, the ordinary credit method approach pursued in double tax treaties between Ukraine and EU Member States would discourage a Ukrainian taxpayer from pursuing a permanent establishment in these states, given the risk of a substantial extent of double taxation still remained upon application of the ordinary credit method.

To summarise, the residence state is mostly interested in the amount received by its treasury and, in essence, remains indifferent to the worldwide tax burden imposed on its taxpayer. On the contrary, a taxpayer is primarily concerned with the overall tax burden experienced in two states. Therefore, to delineate the most favourable double tax relief for the residence state treasury, the amount of tax burden (TB) will be compared. On the contrary, the overall tax burden experienced in the residence and source states is compared to delineate a favourable double tax relief from a taxpayer`s perspective. Comparison is presented based on calculations conducted above by using higher (25%) and lower (15%) tax rates than in the residence state (18%); for the current example, the latter is Ukraine. Exemption with progression is not represented in the tables below in view of the absence of a progressive tax rate in the residence state considered (Ukraine).

The calculations demonstrated that the full exemption method favours the taxpayer in case the tax rate in the source state is lower than in the residence state. Should the tax rate in the source state be higher, the full credit appears as a better option. Nevertheless, full credit is one of the most uncommon methods in the double taxation preclusion practice. The exemption with its modifications and the ordinary credit methods are followed by states more frequently.

It is suggested to follow these formulas while calculating the exemption and credit methods [according to formulations of double tax relief methods in the OECD Model Conventions]. Abbreviations in formulas:

[110] *Ibid.*
[111] Brian J. Arnold, "Double Taxation Relief," in *International Tax Primer,* (Alphen aan den Rijn: Wolters Kluwer, 2019), 65.

1) Income earned in the residence state ("**RI**");

2) Income earned in the source state ("**SI**");

3) Tax rate of the residence state ("**RT")**;

4) Tax rate of the source state ("**ST")**;

5) Tax amount that a taxpayer pays in its residence state (**"TB").**

6) **"Threshold"** means the income amount, earned in the residence state and the source state together, that shall be exceeded by a taxpayer to apply a higher tax rate to the income earned in the residence state (relevant for the exemption with progression method).

Formulas:

The full exemption:	$RI \times RTR = TB$.
The exemption with progression:	If $SI+RI <$ or $=$ the threshold, then: $RI \times RTR = TB$. If $SI+RI >$ the threshold, then: $RI \times RT \uparrow$ (increased) $= TB$.
The full credit:	$((RI + SI) \times RT) - (SI \times ST) = TB$
The ordinary credit:	If $RT < ST$ or $RT = ST$, then: $((RI + SI) \times RT) - (SI \times \underline{RT}) = TB$ If $RTR > STR$, then: $((RI + SI) \times RT) - (SI \times \underline{ST}) = TB$

Fundamentally, the difference between the methods is that the exemption methods look at income, while the credit methods look at tax.[112] Even from the very first glance, the full exemption method seems to be the easiest in application. In essence, although a state *de jure* applies the exemption with the progression method, it is still *de facto* the full exemption until the appropriate threshold is reached. Analogously, though a state *de jure* might apply the ordinary credit, a *de facto* method applicable remains the full credit if a tax rate in the source state is lower than in the residence state or is the same. Should the tax rate be higher in the source state, the ordinary credit method mechanism applies. Given these results, Chapter III examines twenty-seven double tax treaties between Ukraine and EU Member States on the subject of a double taxation preclusion method from each side.

[112] "OECD Model Convention 2017 with Commentaries," *supra note*, 12: Para. 17 Page 383 of the Commentaries part.

CHAPTER 3. DOUBLE TAXATION PRECLUSION BETWEEN UKRAINE AND EU MEMBER STATES

Ukraine has a network of double tax treaties with all twenty-seven EU Member States. The methods of double taxation preclusion differ from a treaty to treaty. Since the exemption method is deemed to benefit a taxpayer the most, this Chapter examines methods applicable to a) European tax residents that operate in Ukraine through a permanent establishment and pay a corporate income tax there; b) Ukrainian tax residents that operate in the EU through a permanent establishment and pay a corporate income tax there. The examination concerns only corporate income tax paid on the direct income generated (corporate profit) and does not cover taxes on indirect income (dividends, interest, royalty).

3.1. Exemption and credit methods in the OECD Model Convention

Ukraine and EU Member States follow the OECD Model Convention in a double tax treaty practice. The OECD Model Convention describes the full exemption and the ordinary credit methods in its texts, mentioning in the Commentaries that the exemption with progression and full credit are possible modifications. The formulation in an actual EU State-Ukraine double tax treaty either remains the same as in the OECD Model Convention (for instance, treaties with Croatia, Slovenia, etc.) or is slightly modified (for example, treaties with Belgium, Estonia).

Given the text of the OECD Model Convention:

Article 23 A. Exemption method.

1. Where a resident of a Contracting State derives income which may be taxed in the other Contracting State in accordance with the provisions of this Convention (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State), the first-mentioned State shall […] exempt such income from tax.

Article 23B. Credit method.

1. Where a resident of a Contracting State derives income which may be taxed in the other Contracting State in accordance with the provisions of this Convention (except to the extent that these provisions allow taxation by that other State solely because the income is also income derived by a resident of that State), the first-mentioned State shall allow: a) as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in that other State; […] Such deduction, in either case, shall not, however, exceed that part of the income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in that other State.

Though the title sounds general - “exemption” and “credit”, respectively - the way in which the OECD Model Convention describes them reflects the full exemption and the ordinary credit mechanisms. The modifications of the exemption (full/progression) and credit (full/ordinary) are identified in the Commentaries through practical examples and not formalistic definitions:

14. The principle of exemption may be applied by two main methods:

a) the income which may be taxed in State E is not taken into account at all by State R for the purposes of its tax; State R is not entitled to take the income so exempted into consideration when determining the tax to be imposed on the rest of the income; this method is called “full exemption”;

b) the income which may be taxed in State E is not taxed by State R, but State R retains the right to take that income into consideration when determining the tax to be imposed on the rest of the income; this method is called “exemption with progression”.[113]

16. The principle of credit may be applied by two main methods:

a) State R allows the deduction of the total amount of tax paid in the other State on income which may be taxed in that State, this method is called “full credit”;

b) the deduction given by State R for the tax paid in the other State is restricted to that part of its own tax which is appropriate to the income which may be taxed in the other State; this method is called “ordinary credit”.[114]

Following the very text of the OECD Model Convention and Commentaries, States choose the most appropriate methods for themselves.

The difference between income and profit. Though Article 23A and Article 23 B refer to "income" in its text, this term shall be used in the context of "profit". The profit implies the income remaining after deducing business expenses (bills for electricity and other facilities, materials bought for further production, services obtained from other counterparties, etc.).[115] Generally, legal entities pay a corporate income tax exactly on profit.[116] Commentaries on Article 7 identify profit as a "category of income".[117] Given Article 7 of the OECD Model Convention, the elimination of double taxation for the permanent establishment is considered in light of business profits earned. Article 7 refers directly to Article 23A and Article 23B as those addressing the issue of double taxation for a permanent establishment. Thus, even though articles in an actual double tax treaties refer to "income" of a permanent establishment, it should be considered in light of the "profit".

[113] Throughout the Commentary on Articles 23 A and 23 B, the letter "R" stands for the State of residence within the meaning of the Convention, and "E" for the State where a permanent establishment is situated.
[114] OECD Model Convention 2017 with Commentaries, *supra note*, 12: Para. 16 Page 383 of the Commentaries part.
[115] "Net Income vs. Profit: What's the Difference?," *Investopedia,* accessed 18 November 2023, https://www.investopedia.com/ask/answers/122414/net-income-same-profit.asp.
[116] "Corporate Tax: Definition, Deductions, How It Works," *Investopedia,* accessed 18 November 2023, https://www.investopedia.com/terms/c/corporatetax.asp
[117] "OECD Model Convention 2017 with Commentaries," *supra note,* 12: Para 10 Page 175 of the Commentaries part.

3.2. Exemption and credit methods in Ukraine-EU Member States double tax treaties

Austria. Ukraine concluded a double tax treaty with Austria in 1997.[118] The elimination of double taxation is regulated by Article 23 of the treaty. According to this provision, Austrian tax residents obtain in their residence state the following relief:

1. *In the case of Austria, double taxation shall be avoided as follows:*

a) Where a resident of Austria derives income which, in accordance with the provisions of this Convention, may be taxed in Ukraine, exempt such income from tax.

In essence, this provision is identical to Article 23A(1) of the OECD Model Convention. It is directly defined that the state applies the exemption method to its taxpayers. The article is formulated not in a descriptive way: it does not refer to the particular peculiarities of the exemption method or what it constitutes itself.

Though it is stated in the treaty that the income is exempted from taxation, there is no stipulation whether such exemption is full or with progression. For instance, the treaty between Belgium and Ukraine, analysed below, indeed describes the exemption as with progression. In this regard, the Austrian legislature requires analysis. Following the very text of the treaty and the way in which the full exemption is described in the OECD Convention, we presume that the method applicable in Austria is the full exemption.

Austria applies the most beneficial method to its taxpayers operating in Ukraine. On the contrary, Ukrainian taxpayers that possess a permanent establishment in Austria are approached in another way in their residence state. In accordance with the Article 23(2)(a) of the treaty:

2. In the case of Ukraine, double taxation shall be avoided as follows:

(b) Subject to the provisions of the law of Ukraine regarding the elimination of tax paid in a territory outside Ukraine (which shall not affect the general principle hereof), Austrian tax payable under the laws of Austria and in accordance with this Convention, on income from sources within Austria [...] by deduction shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Austrian tax is computed.

Such deductions in either case shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income or which may be taxed in Austria.

Article 23(2)(a), in its first part, where it is stated that "the tax paid in Austria shall be allowed as a credit in Ukraine", does not repeat Article 23B of the OECD Model Convention, but the national

[118] "Double tax treaty between Ukraine and Austria № 040_015 from 16 October 1997," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

legislative provisions (the TCU).[119] However, the formulation that the deduction shall not exceed the tax to be paid is copied indeed from Article 23B of the OECD Model Convention (and it is also repeated in the TCU). The essence is still the same, and it indicates the application of the ordinary credit method. Despite the same essence implied (application of the ordinary credit method), the drafting technique might differ in the conventional practice.

Consequently, if the tax rate in Austria is higher than in Ukraine, the latter applies the domestic tax rate to the income earned in Austria for the purposes of deduction. Assuming that at the moment of conclusion of this treaty (1997), Austria had a lower corporate tax rate than in Ukraine, that would not be a decisive factor in formulating treaty provisions differently. The tax rate is a mere number that a legislator might change in the blink of an eye. But signing the additional protocol to the treaty, stipulating that the credit method is ordinary and is not full, is a long-lasting negotiable process between two states.

Another peculiarity of the drafting technique is that the Ukrainian side refers to the national law by stating "subject to its national law that does not affect the main principle of the treaty". Austria does not do so, merely prescribing that it applies the exemption method.

To conclude, Austria mitigates double taxation for Austrian tax residents with the help of the full exemption method. On the contrary, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method.

Belgium. Ukraine concluded a double tax treaty with Belgium in 1997.[120] Belgium also applies the exemption method. But, unlike Austria, Belgium opts for the exemption with the progression subtype. The text of the Convention is formulated as follows:

2. In the case of Belgium, double taxation shall be avoided as follows:

a) Where a resident of Belgium derives income taxed in Ukraine in accordance with the provisions of this Convention, Belgium shall exempt such income from tax but may, in calculating the amount of tax on the remaining income of that resident, apply the rate of tax which would have been applicable if such income had not been exempted.

The formulation "may" (instead of "shall") imposes a non-binding bond on Belgium in regard to the application of the exemption with the progression method. However, "may" presumably means the dependence of the tax rate on the amount earned in two states. If the amount does not exceed the threshold prescribed by Belgium tax legislation, an average tax rate applies to the income earned in Belgium. Should the threshold be exceeded, the increased tax rate applies to the income earned in Belgium.

[119] "Tax Code of Ukraine," *supra note*, 5: Para. 136.1.
[120] "Double tax treaty between Ukraine and Belgium № 056_688 from 20 May 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

With regard to Ukraine, the ordinary credit method still remains. Under Article 23(1):

In the case of Ukraine, double taxation shall be avoided as follows:

a) Subject to the provisions of the law of Ukraine regarding the elimination of tax paid in a territory outside Ukraine (which shall not affect the general principle hereof), Belgian tax paid under the laws of Belgium and in accordance with this Convention, […] by deduction, shall be allowed as a credit against any Ukrainian tax computed by reference to this income.

b) […] deductions, in either case, shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in Ukraine.

To conclude, Belgium mitigates double taxation for Belgian tax residents with the help of the exemption with the progression method. Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method.

Bulgaria. Ukraine concluded a double tax treaty with Bulgaria in 1995.[121] Analogously to Austria, Bulgaria opts for the full exemption method. According to Article 24 of the treaty, that prescribes the ways of double taxation elimination:

2. Subject to the provisions of the law of Bulgaria regarding the elimination of tax paid in a territory outside Bulgaria (which shall not affect the general principle hereof), double taxation in Bulgaria shall be eliminated as follows: a) where a resident of Bulgaria derives income which, in accordance with the provisions of this Convention, may be taxed in Ukraine, Bulgaria shall exempt such income from tax;

On the contrary, Ukraine pursues the ordinary credit method in relation to its Bulgarian-operated tax residents given Article 24(1) and Article 24(3):

1. Subject to the provisions of the law of Ukraine regarding the elimination of tax paid in a territory outside Ukraine (which shall not affect the general principle hereof), Bulgarian tax paid under the laws of Bulgaria and in accordance with this Convention, […] by deduction, shall be allowed as a credit against the relative Ukrainian tax. The Bulgarian tax computed under Bulgarian laws with respect to income, the separate amounts of which do not exceed separate amounts of income taxable under Ukrainian laws, shall be recognized as a credit against the Ukrainian tax.

3. The deduction, according to paragraph 1 of this Article in either case, shall not exceed that part of the income tax, as computed before the deduction is given, which is attributable, as the case may be, to such items of income or property which may be taxed in the other State.

Ukraine seemingly introduces the same formulation while describing its method of double taxation elimination in double-tax treaties with the vast of states. To conclude, Bulgaria mitigates

[121] "Double tax treaty between Ukraine and Bulgary № 100_008 from 20 November 1995," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

double taxation for Bulgarian tax residents with the help of the full exemption method. Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method.

Croatia. Ukraine concluded a double tax treaty with Croatia in 1996.[122] Both sides apply to their tax residents, operating in another State Party, the ordinary credit method. Pursuant to Article 23(1)(a) of the treaty, which regulates the elimination of double taxation:

Where a resident of a Contracting State derives income or owns capital which may be taxed in the other Contracting State in accordance with the provisions of this Convention, the first-mentioned State shall allow:a) as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in that other State;

Such deduction, in either case, shall not, however, exceed that part of the income tax or capital tax, as computed before the deduction is given, which is attributable, as the case may be, to the income or the capital which may be taxed in that other State.

The contracting State Parties drafted Article 23 as a total analogue to Article 23B of the OECD Model Convention without modifying it. To conclude, Croatia mitigates double taxation for Croatian tax residents with the help of the ordinary credit method. Analogously, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method, too.

Cyprus. Ukraine concluded a double tax treaty with Croatia in 2012.[123] The elimination of double taxation is regulated by Article 21 of the treaty. The latter is formulated in a plain short-descriptive manner. It also totally repeats Article 23B of the OECD Model Convention. Both Contracting State Parties apply the ordinary credit method to tackle double taxation:

1. Where a resident of a Contracting State derives income which, in accordance with the provisions of this Convention, may be taxed in the other Contracting State, the first-mentioned State shall allow as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in that other State. Such deduction shall not, however, exceed that part of the income tax as computed before the deduction is given, which is attributable to the income which may be taxed in that other State.

To conclude, Cyprus mitigates double taxation for Cypriot tax residents with the help of the ordinary credit method. Similarly, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method.

[122] "Double tax treaty between Ukraine and Croatia № 191_002 from 10 September 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.
[123] "Double tax treaty between Ukraine and Cyprus № 196_016 from 08 November 2011," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

Czech Republic. Ukraine concluded a double tax treaty with Czechia in 1997.[124] Both State Parties undertake the ordinary credit method and retain the right to impose taxation on the amount exempted from taxation in another Contracting State. The elimination of double taxation is regulated by Article 23 of the treaty. Similarly, this provision repeats Article 23B of the OECD Model Convention. As stated in Article 23 of the treaty:

1. Where a resident of a Contracting State derives income or owns property which, in accordance with the provisions of this Convention, may be taxed in the other Contracting State, the first-mentioned State shall allow: a) as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in that other State;

Such deduction, in either case, shall not, however, exceed that part of the income tax or property tax, as computed before the deduction is given, which is attributable, as the case may be, to the income or the property which may be taxed in that other State.

To conclude, the Czech Republic mitigates double taxation for Czech tax residents with the help of the ordinary credit method. Similarly, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method.

Denmark. Ukraine concluded a double tax treaty with Denmark in 1997.[125] The method of double taxation preclusion is regulated by Article 24 of the treaty. Both State Parties treat their tax residents operating through a permanent establishment in another State similarly and apply the ordinary credit method. From the Ukrainian side:

a) Where a resident of Ukraine derives income which, in accordance with the provisions of this Convention, may be taxed in Denmark, Ukraine shall allow, as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in Denmark.

b) Such deduction shall not, however, exceed that part of the income tax, as computed before the deduction is given, which is attributable to the income which may be taxed in Denmark.

From the Danish side, it is formulated analogously:

a) Subject to the provisions of sub-paragraph c), where a resident of Denmark derives income which, in accordance with the provisions of this Convention, may be taxed in Ukraine (except to the extent that these provisions allow taxation by Ukraine solely because the income is also income derived by a resident of Ukraine) Denmark shall allow as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in Ukraine.

[124] "Double tax treaty between Ukraine and the Czech Republic № 203_005 from 30 June 1997," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[125] "Double tax treaty between Ukraine and Denmark № 208_669 from 05 March 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

b) Such deduction shall not, however, exceed that part of the income tax, as computed before the deduction is given, which is attributable to the income which may be taxed in Ukraine.

To conclude, Denmark mitigates double taxation for Danish tax residents with the help of the ordinary credit method. In response, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method, too.

Estonia. Ukraine concluded a double tax treaty with Estonia in 1996.[126] The method of double taxation elimination is regulated by Article 23 of the treaty. There is a remarkable difference that distinguishes double tax treaties between Ukraine and the Baltic States (Estonia, Latvia, Lithuania). Provisions on the elimination of double taxation, from the Baltic States side, contain the note on application of the ordinary credit "unless a more favourable treatment is provided in its domestic law". In that way, the Baltic State eliminate the problem of the supremacy of international treaties over domestic law in case the latter grants more beneficial regime for a taxpayer.

Pursuant to the treaty text, both sides apply an ordinary credit method. The difference only lies in formulations. The drafter from the Estonian side took the description of the credit method from the OECD Model Convention and inserted it in a double tax treaty. The drafter from the Ukrainian side took the description of the credit method partly from its national legislation (TCU) partly from the OECD Model Convention. Nevertheless, the essence (application of the ordinary credit method) remains the same and given Article 23 of the treaty:

1. In the case of Estonia, double taxation shall be eliminated as follows:

a) Where a resident of Estonia derives income which, in accordance with this Convention, may be taxed in Ukraine, unless a more favourable treatment is provided in its domestic law, Estonia shall allow: (i) as a deduction from the tax on the income of that resident, an amount equal to the income tax paid thereon in Ukraine;

Such deduction, in either case, shall not, however, exceed that part of the income tax in Estonia as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in Ukraine. […]

2. Subject to the provisions of the law of Ukraine regarding the elimination of tax payable in a territory outside Ukraine (which shall not affect the general principle hereof), Estonian tax payable under the laws of Estonia and in accordance with this Convention, […] by deduction, on income from sources within Estonia shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Estonian tax is computed.

[126] "Double tax treaty between Ukraine and Estonia № 233_687 from 10 May 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

Such deduction, in any case, shall not exceed that part of income tax or capital computed before the deduction in the case may be given, which is attributable, as the case may be, to the income which may be taxed in Estonia.

Even though, according to the double tax treaty, Estonia applies ordinary credit, its national law still requires observation. Given the treaty's wording, Estonia and Ukraine mitigate double taxation with the help of the ordinary credit method.

Finland. Ukraine concluded the double tax treaty with Finland in 1994.[127] The method of double taxation elimination is regulated by Article 23 of the treaty. Though both State Parties apply the ordinary credit method, the drafting technique differs. Finland describes the ordinary credit method as the OECD Model Convention does, whilst Ukraine describes it pursuant to the TCU alongside the OECD Model Convention. Given Article 23 of the treaty:

1. In Finland, double taxation shall be eliminated as follows:

a) Where a resident of Finland derives income which, in accordance with the provisions of this Convention, may be taxed in Ukraine, Finland shall allow: (i) as a deduction from the tax on the income of that person, an amount equal to the tax on income paid in Ukraine; […]

2. In Ukraine, double taxation shall be eliminated as follows:

a) Finnish tax payable under the laws of Finland and in accordance with the Convention, on income from sources within Finland, [..] by deduction, shall be allowed as a credit against any Ukraine tax computed by reference to the same income by reference to which the Finnish tax is computed.

3. deduction […] shall not, however, in a Contracting State exceed that part of the tax on the income, as computed before the deduction is given or the credit is allowed, which is attributable, as the case may be, to the income which may be taxed in the other Contracting State.

To conclude, Finland mitigates double taxation for Finnish tax residents with the help of the ordinary credit method. In response, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method, too.

France. Ukraine concluded a double tax treaty with France in 1997.[128] The method of double taxation elimination is regulated by Article 23 of the treaty. It is apparent that a substantial number of the EU Member States opt for the ordinary credit method. Moreover, neither of the States already analysed applies the full credit to its tax residents. France constitutes no exception to the general rule

[127] "Double tax treaty between Ukraine and Finland № 246_621 from 14 October 1994," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[128] "Double tax treaty between Ukraine and France № 250_001 from 01 November 1999," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

in this respect. Ukraine prescribes a recourse to the ordinary credit method in this treaty too. Given Article 23 of the France-Ukraine treaty:

1. In France, double taxation shall be eliminated as follows:

a) Where a resident of France derives income which, in accordance with the provisions of this Convention, may be taxed in Ukraine, France shall allow, as a deduction from the tax on the income of that person, an amount equal to the tax on income paid in Ukraine; […]

2. In Ukraine, double taxation shall be eliminated as follows:

a) French tax payable under the laws of France and in accordance with the Convention on income from sources within France, [..] by deduction, shall be allowed as a credit against any Ukraine tax computed by reference to the same income by reference to which the Finnish tax is computed.

3. […] deduction […] shall not, however, in a Contracting State exceed that part of the tax on the income, as computed before the deduction is given or the credit is allowed, which is attributable, as the case may be, to the income which may be taxed in the other Contracting State.

To conclude, France mitigates double taxation for French tax residents with the help of the ordinary credit method. In response, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method, too.

Germany. Ukraine concluded a double tax treaty with Germany in 1995.[129] Article 23 of the treaty regulates the elimination of double taxation between Contracting States. Under this treaty, Germany allows the exemption with progression method application. The text of this treaty is formulated in a manner like Belgium did in its treaty with Ukraine:

(1) Tax shall be determined in the case of a resident of the Federal Republic of Germany as follows: a) [..] there shall be exempted from German tax any item of income arising in Ukraine which, according to this Agreement, may be taxed in Ukraine. The Federal Republic of Germany, however, retains the right to take into account in the determination of its rate of tax the items of income so exempted.

As a usual practice, Ukraine applies the ordinary credit method to its tax residents:

(2) Tax shall be determined in the case of a resident of Ukraine as follows:

Subject to the provisions of the law of Ukraine regarding the elimination of double taxation of income arising in a territory outside Ukraine (which shall not affect the general principle hereof), the German tax payable under the laws of the Federal Republic of Germany and in accordance with this Agreement, on income from sources within the Federal Republic of Germany shall be allowed as a credit against any Ukrainian tax computed by reference to the income by reference to which the Ukrainian tax is computed.

[129] "Double tax treaty between Ukraine and Germany № 276_001 from 03 July 1995," *supra note*, 10.

Such deductions, in either case, shall not exceed that part of income tax or property tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in the Federal Republic of Germany.

To conclude, Germany mitigates double taxation for German tax residents with the help of the exemption with the progression method. Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method.

Greece. Ukraine concluded a double tax treaty with Greece in 2000.[130] Article 23 regulates the elimination of the double taxation procedure. Both State Parties refer to the ordinary credit method. Formulation from both sides reminds a "mirror" principle:

1. Subject to the provisions of the law of Ukraine regarding the elimination of double taxation with respect to taxes payable in a territory outside Ukraine (which shall not affect the general principle hereof), Greek tax payable under the laws of the Hellenic Republic and in accordance with this Convention, […] by deduction, on income from sources within the Hellenic Republic shall be allowed as a credit against any Ukrainian tax computed by reference to the income by reference to which the Ukrainian tax is computed.

2. Subject to the provisions of the law of the Hellenic Republic regarding the elimination of double taxation with respect to taxes payable in a territory outside the Hellenic Republic (which shall not affect the general principle hereof), Ukrainian tax payable under the laws of Ukraine and in accordance with this Convention, […] by deduction, on income from sources within Ukraine shall be allowed as a credit against the Greek tax computed by reference to the same income by reference to which the Greek tax is computed.

3. Such deductions, in either case, shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income that may be taxed in that other Contracting State.

To conclude, Greece and Ukraine mitigate double with the help of the ordinary credit method.

Hungary. Ukraine concluded a double tax treaty with Hungary in 1995.[131] Article 23 of the treaty regulates the elimination of double taxation between Contracting States. Hungary allows its tax residents to exempt fully the income earned in Ukraine. On the other hand, Ukraine still applies the ordinary credit method:

1. In Ukraine, double taxation shall be eliminated as follows:

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[130] "Double tax treaty between Ukraine and Greece № 300_050 from 06 November 2011," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[131] "Double tax treaty between Ukraine and Hungary № 348_630 from 19 May 1995," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

Subject to the provisions of the law of Ukraine regarding the allowance of a credit for tax payable in a territory outside Ukraine (which shall not affect the general principle hereof), Hungarian tax paid under the laws of Hungary and in accordance with this Convention [..] by deduction, on income from sources within Hungary shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Ukrainian tax is computed.

2. In Hungary, double taxation shall be eliminated as follows:

a) Where a resident of Hungary derives income which, in accordance with this Convention may be taxed in Ukraine, Hungary shall […] exempt such income or property from tax.

3. Such deductions allowed in a Contracting State in either case shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in the other Contracting State.

To conclude, Hungary mitigates double taxation for Hungarian tax residents with the help of the full exemption method. Meanwhile, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method.

Ireland. Ukraine concluded a double tax treaty with Ireland in 2013.[132] It is one of the latest double tax treaties signed in a row. Article 22 prescribes ways of eliminating double taxation. Both State Parties undertake the credit method in mitigating double taxation. However, Ukraine expressly specifies that it applies the ordinary credit method in the treaty, contrary to Ireland that leaves this question up to its domestic law.

Full credit is one of the most beneficial treatments suggested to a taxpayer and is applicable by States rather rarely. However, this conclusion is still doubted since the domestic legislation of Ireland shall be analysed. The Irish side refers to the provisions of its national legislation.

1. Subject to the provisions of the law of Ukraine regarding the elimination of tax payable in a territory outside Ukraine (which shall not affect the general principle hereof), Irish tax payable under the laws of Ireland and in accordance with this Convention, [..] by deduction, on income from sources within Ireland shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Irish tax is computed. Such credit shall not, however, exceed that part of the Ukrainian tax, as computed before the credit is given, which is attributable, as the case may be, to the profits, income or gains which may be taxed in Ireland.

2. Subject to the provisions of the laws of Ireland regarding the allowance of a credit against Irish tax of tax payable in a territory outside Ireland (which shall not affect the general principle hereof): a) Ukrainian tax payable under the laws of Ukraine and in accordance with this Convention, whether [..] by deduction on income from sources within Ukraine shall be allowed as a credit against

[132] "Double tax treaty between Ukraine and Ireland № 372_010 from 19 April 2013," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

any Irish tax computed by reference to the same income by reference to which Ukrainian tax is computed;

To conclude, Ireland mitigates double taxation for Irish tax residents with the help of the credit method, leaving determining its subtype up to domestic law. In response, Ukraine mitigates double taxation for Ukrainian tax residents specifically with the help of the ordinary credit method.

Italy. Ukraine concluded a double tax treaty with Italy in 1997.[133] The method of double taxation elimination is regulated by Article 24 of the treaty. Both State Parties undertake the ordinary credit method towards their taxpayers, even though State Parties describe this method in a different manner:

2. In the case of Ukraine:

(a) Subject to the provisions of the law of Ukraine regarding the elimination of tax paid in a territory outside Ukraine (which shall not affect the general principle hereof), Italian tax paid under the laws of Italy and in accordance with this Convention, […] by deduction, on income from sources within Italy shall be allowed as a credit against any Ukrainian tax computed by reference to those income. The credit so given shall not exceed the Italian tax computed with respect to incomel taxable under Ukrainian tax law.

(b) Such deductions, in either case, shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in Ukraine.

3. In the case of Italy:

(a) If a resident of Italy owns items of income which are taxable in Ukraine, Italy, in determining its income taxes specified in Article 2 of this Convention, may include in the basis upon which such taxes are imposed the said items of income unless specific provisions of this Convention otherwise provide. In such a case, Italy shall deduct from the taxes so calculated the income tax paid in Ukraine but in an amount not exceeding that proportion of the aforesaid Italian tax which such items of income bear to the entire income.

To conclude, Italy mitigates double taxation for Italian tax residents with the help of the ordinary credit method. In response, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method, too.

Latvia. Ukraine concluded a double tax treaty with Latvia in 1996.[134] The elimination of double taxation is regulated by Article 24 of the treaty. This provision resembles an analogous article

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[133] "Double tax treaty between Ukraine and Italy № 380_011 from 26 February 1997," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[134] "Double tax treaty between Ukraine and Latvia № 428_662 from 21 November 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

from the Estonia-Ukraine treaty. Analogously to Estonia, the Latvian drafter states that Latvia applies the ordinary credit method unless a more beneficial treatment is provided by its national legislation:

2. In the case of Latvia, double taxation shall be eliminated as follows:

a) Where a resident of Latvia derives income or owns capital which, in accordance with this Convention, may be taxed in Ukraine, unless a more favourable treatment is provided in its domestic law, Latvia shall allow: (1) as a deduction from the tax on the income of that resident, an amount equal to the income tax paid thereon in Ukraine; [..] Such deduction, in either case, shall not, however, exceed that part of the income tax in Latvia as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in Ukraine.

The clause on a "more favourable regime" allows the amendment only of national legislation without necessarily being obliged to sign an additional protocol to a double tax treaty. However, a drawback of such formulation for potential investors (who would like to obtain tax residence in Latvia and conduct business through a permanent establishment in another State Party as a Latvian resident) lies in rather limited access to the national legislation of Latvia. Thus, though Latvia might grant the favourable full exemption method under its treaty, an investor would still be deemed that Latvia follows the ordinary credit method in view of the double tax treaty. Furthermore, the ordinary credit is indeed considered as the most burdensome for a taxpayer. However, who is indeed eligible to decide what method is favourable: the state or the taxpayer? What if, for the latter, it is more favourable to apply the ordinary credit in view of some tax benefits it might obtain as a result of such application? Wouldn't it be reasonable to grant the right to decide which method shall be applicable to a taxpayer itself, given the possibility to choose between the treaty and domestic law regime? Moreover, what if the amendment to the law of Latvia suggests, for instance, the exemption with the progression method, which can sometimes be even more burdensome for a taxpayer compared to the ordinary credit? Although such questions arise, they are too hypothetical, so a "more favourable regime" clause still remain a "safe harbour" for a legislator.

On the contrary, from the side of Ukraine, the latter still maintains the ordinary credit method approach and does not step back from the approach undertaken in this treaty. It stems from the formulation that the ordinary credit method is applicable pursuant to Ukrainian law "which shall not affect the main principle contained in this article". Analogous clause is used by Ukraine in a number of its double tax treaties with EU Member States. However, it raises a problem if Ukraine provides a more beneficial regime (full exemption method) in its national legislation, however, it would still remain unapplicable:

1. a) Subject to the provisions of the law of Ukraine regarding the elimination of tax payable in a territory outside Ukraine (which shall not affect the general principle hereof), Latvian tax payable under the laws of Latvia and in accordance with this Convention, [..] by deduction, on income *from sources within Latvia shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Latvian tax is computed. Such deductions, in any case, shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in Latvia.*

To conclude, according to the treaty, Latvia mitigates double taxation for Latvian tax residents with the help of the ordinary credit method. However, Latvia includes a clause to the treaty under which the ordinary credit applies unless its national law provides a more favourable regime. In response, Ukraine also mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method.

Lithuania. Ukraine concluded a double tax treaty with Lithuania in 1996.[135] The elimination of double taxation is regulated by Article 24 of the treaty. The same period of the conclusion of treaties with all Baltic States (1996) may have contributed to the similar formulations used in these treaties. Analogously to previous Baltic States' practice, Lithuania retains the right to apply a different method under its national law if the latter is more favourable:

1. In Lithuania, double taxation shall be eliminated as follows:

where a resident of Lithuania derives income or owns capital which, in accordance with this Convention, may be taxed in Ukraine, unless a more favourable treatment is provided in its domestic law, Lithuania shall allow:a) as a deduction from the tax on the income of that resident, an amount equal to the income tax paid thereon in Ukraine;

Such deduction in either case shall not, however, exceed that part of the income tax in Lithuania, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in Ukraine.

However, the availability of the domestic law of Lithuania (translated into English) for analysis allows us to consider whether the Lithuanian law indeed suggests a more favourable regime (the full exemption method). As analysed above, under Art. 55(1) of the Law of Lithuania on Corporate Income Tax, the income of a tax-resident company is not subject to taxation in Lithuania should it be received from activities through a permanent establishment in a foreign country that is in the European Economic Area (hereinafter – EEA, which also includes EU Member States) or that has a double tax treaty with Lithuania and if the income has already been subject to taxation there.[136] Though Ukraine does not constitute a part of the EEA, it has a double tax treaty signed with Lithuania. Thus, notwithstanding the Lithuania-Ukraine double tax treaty, Lithuanian tax residents who operate in Ukraine are subject to the exemption method.

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[135] "Double tax treaty between Ukraine and Lithuania № 440_004 from 23 September 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.
[136] "Law of Lithuania on Corporate Income Tax," *supra note*, 25.

On the contrary, Ukraine provides in its domestic law (TCU) that it applies the ordinary credit method to taxpayers that operate in States with which Ukraine concluded a double tax treaty.[137] The application of ordinary credit is also prescribed in the Lithuania-Ukraine treaty:

2. a) Subject to the provisions of the law of Ukraine regarding the elimination of tax payable in a territory outside Ukraine (which shall not affect the general principle hereof), Lithuanian tax payable under the laws of Lithuania and in accordance with this Convention, […] by deduction, on income from sources within Lithuania shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Lithuanian tax is computed.

Such deductions, in any case, shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in Lithuania.

To conclude, under the treaty, Lithuania mitigates double taxation for Lithuanian tax residents with the help of the ordinary credit method. Nevertheless, given the analysis of the Lithuanian domestic legislation, Lithuanian taxpayers may seek a more favourable treatment, precisely, the exemption method. In response, Ukraine mitigates double taxation for Ukrainian tax residents with the help of the ordinary credit method under the treaty and the TCU.

Luxembourg. Ukraine concluded a double tax treaty with Luxembourg in 1997.[138] The elimination of double taxation is regulated by Article 24 of the treaty. Ireland maintains the most favourable method, among the four available, - the full exemption:

2. Subject to the provisions of the law of Luxembourg regarding the elimination of double taxation (which shall not affect the general principle hereof), double taxation shall be eliminated in Luxembourg as follows: a) Where a resident of Luxembourg derives income which, in accordance with the provisions of this Convention may be taxed in Ukraine, Luxembourg shall [..] exempt such income from tax.

Ukraine pursues the ordinary credit method:

1. Subject to the provisions of the law of Ukraine regarding the elimination of double taxation (which shall not affect the general principle hereof), Luxembourg tax paid under the laws of Luxembourg and in accordance with this Convention on income from sources within or chargeable capital situated in Luxembourg shall be allowed as a credit against any Ukrainian tax computed by reference to the income on which the Luxembourg tax is paid.

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[137] "Tax Code of Ukraine," *supra note*, 5: Para. 141.4.9.

[138] "Double tax treaty between Ukraine and Luxembourg № 442_002 from 06 September 1997," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

3. The deductions provided for in a Contracting State under paragraph 1 [..] of this Article, in either case, shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in the other State.

To conclude, Luxembourg mitigates double taxation for its tax residents with the help of the full exemption method. On the contrary, Ukraine mitigates double taxation for its tax residents with the help of the ordinary credit method.

Malta. Ukraine concluded a double tax treaty with Malta in 2013[139]. The elimination of double taxation is prescribed by Article 22. Both State Parties follow the ordinary credit method. The drafting technique is different in this treaty, and instead of "deductions" that shall not exceed some extent, the parties indicate that "credits" shall not exceed the threshold. Nevertheless, the essence of the method remains the same:

1. In the case of Ukraine, double taxation shall be eliminated as follows:

Subject to the provisions of the law of Ukraine regarding the elimination of tax paid in a territory outside Ukraine (which shall not affect the general principle hereof), Malta tax paid under the laws of Malta and in accordance with this Convention, [..] by deduction on income from sources within Malta shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Malta tax is computed.

2. In the case of Malta, double taxation shall be eliminated as follows:

Subject to the provisions of the law of Malta regarding the allowance of a credit against Malta tax in respect of foreign tax, where, in accordance with the provisions of this Convention, there is included in a Malta assessment income from sources within Ukraine, the Ukrainian tax on such income shall be allowed as a credit against the relative Malta tax payable thereon.

3. Such credits in either case shall not exceed that part of income tax, as computed before the credit is given, which is attributable to the income which may be taxed in that other State.

To conclude, Malta and Ukraine mitigate double taxation by the ordinary credit method.

Netherlands. Ukraine signed a double tax treaty with the Netherlands in 1995.[140] Article 24 of the treaty regulates ways to eliminate double taxation in Contracting States. While the Netherlands pursue the most beneficial approach to its taxpayers (the full exemption), Ukraine still maintains the ordinary credit method. Apparently, Ukraine has the same definition of its ordinary credit method mainly with all its counterparties:

[139] "Double tax treaty between Ukraine and Malta № 470_009-13 from 04 September 2013," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[140] "Double tax treaty between Ukraine and the Netherlands № 528_654 from 24 October 1995," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

2. Subject to the provisions of the law of the Netherlands […] Where a resident of the Netherlands derives items of income […] which according to this Convention may be taxed in Ukraine, the Netherlands shall exempt such items of income.

4. Subject to the provisions of the law of Ukraine regarding the elimination of tax payable in a territory outside Ukraine (which shall not affect the general principle hereof), Netherlands tax payable under the laws of the Netherlands and in accordance with this Convention, […] by deduction, on income from sources within the Netherlands shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Ukrainian tax and the Dutch tax are computed.

5. Deductions, as mentioned in paragraph 4 of this Article, in either case, shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in the Netherlands.

To conclude, the Netherlands mitigates double taxation for Dutch tax residents with the full exemption method. Ukraine treats its residents with the ordinary credit method.

Poland. Ukraine concluded a double tax treaty with Poland 1993.[141] Given Article 24 of the treaty, Poland fully exempts from taxation the income derived by its residents in Ukraine:

2. Subject to the provisions of the law of Poland regarding the elimination of tax payable in a territory outside Poland (which shall not affect the general principle hereof), [...] if a resident of Poland receives income which in accordance with the provisions of this Convention may be taxed in Ukraine, then Poland will exempt this income.

On the contrary, Ukraine applies the ordinary credit method for those who operate in Poland:

1. Subject to the provisions of the law of Ukraine regarding the elimination of tax payable in a territory outside Ukraine (which shall not affect the general principle hereof), Polish tax payable under the laws of Poland and in accordance with this Convention, […] by deduction, on income from sources within Poland shall be allowed as a credit against any Ukrainian tax computed by reference to the same income by reference to which the Ukrainian tax and the Polish tax are computed.

4. Deductions, as mentioned in paragraph 1 of this Article, in either case, shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in Poland.

To conclude, Poland opts for the full exemption, while Ukraine mitigates double taxation by the ordinary credit.

[141] "Double tax treaty between Ukraine and Poland № 616_168 from 12 January 1993," *supra note*, 57.

Portugal. Ukraine concluded a double tax treaty with Portugal in 2000.[142] Double taxation elimination is prescribed by Article 24 of this treaty. Both State Parties maintain the ordinary credit method:

1. Where a resident of Portugal derives income which, in accordance with the provisions of this Convention, may be taxed in Ukraine, Portugal shall allow as a deduction from the tax on the income of that resident an amount equal to the income tax paid in Ukraine. Such deduction shall not, however, exceed that part of the income tax as computed before the deduction is given, which is attributable to the income which may be taxed in Ukraine.

2. Subject to the provisions of the law of Ukraine regarding the elimination of double taxation (which shall not affect the general principle hereof), Portuguese tax paid under the laws of Portugal and in accordance with this Convention, on income from sources within Portugal shall be allowed as a credit against any Ukrainian tax computed by reference to income on which the Portuguese tax is paid.

3. The deductions provided in a Contracting State under paragraphs 1 or 2, in either case, shall not exceed that part of income tax or capital tax as computed before the deduction is given, which is attributable, as the case may be, to the income or the capital which may be taxed in that State.

The drafting technique has differences from both sides. While Ukraine still addresses a reader to its national law by stating that application of its method is "*subject to the provision of the law of Ukraine*", Portugal does not do so. Additionally, paragraph 3 of the Article is a mere repetition of paragraph 1 of the same article. It could be more logical, from the drafting perspective, just to indicate the threshold that shall not be exceeded in paragraph 3 and apply it to both Contracting States.

To conclude, Portugal undertakes the full exemption, while Ukraine grants the ordinary credit to its taxpayers.

Romania. Ukraine signed a double tax treaty with Romania in 1996.[143] Article 24 reflects the elimination of double taxation between states. Analogously, Ukraine applies the ordinary credit and refers to its national legislation to be analysed. Romania does not do so and provides that it applies the exemption with the progression method. Instead of "deduction", the Ukrainian side uses "reduction" in its formulation, which, nevertheless, does not affect the main principle:

1. In the case of Ukraine, double taxation shall be avoided as follows:

[142] "Double tax treaty between Ukraine and Portugal № 620_015 from 09 February 2002," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[143] "Double tax treaty between Ukraine and Romania № 642_002 from 29 March 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

As regards the application of the provisions of Ukrainian legislation concerning the tax exemption in respect of tax paid outside the territory of Ukraine, (which shall not be contrary to the main principles of this paragraph) Romania tax which is paid under Romanian legistation in accordance with this Convention [..] by way of deductions from income from Romania sources, the reduction shall be done by way of a credit against any Ukrainian tax computed in respect of such income in respect of which this Ukrainian tax is computed

This reduction in either case shall not, however, exceed that part of the income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in that other State.

2. *In the case of Romania, the double taxation shall be avoided as follows:*

a) when a resident of Romania derives income which, in accordance with the provisions of this Convention, is taxable in Ukraine, Romania exempts from tax this income […] and takes into account in determining the tax rate the total income derived.

To conclude, Romania mitigates double taxation given the full exemption method and Ukraine mitigates the same issue by the ordinary credit method.

Slovakia. Ukraine signed a double tax treaty with Slovakia in 1996.[144] Article 23 prescribes methods of double taxation elimination. Both sides describe their ordinary credit method applicable in a relatively similar manner:

1. In the case of a resident of Ukraine, double taxation shall be eliminated as follows:

In accordance with the provisions of the law of Ukraine regarding the elimination of tax payable in a territory outside Ukraine (which shall not affect the general principles of that paragraph), on the Slovak tax payable under the laws of the Slovak Republic and in accordance with this Convention, [..] by deduction on income which is taxable from sources in Slovakia, shall be allowed as the deduction against any Ukrainian tax computed by reference to the same income by reference to which the Ukrainian tax is computed. Such deduction in either case shall not exceed that part of income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in that other State.

2. In the case of a resident of the Slovak Republic, double taxation shall be eliminated as follows:

The Slovak Republic, when imposing taxes on its residents, may include in the tax base upon which such taxes are imposed the items of income which according to the provisions of this Convention may also be taxed in Ukraine, but shall allow as a deduction from the amount of tax computed on such a base an amount equal to the tax paid in Ukraine. Such deduction shall not,

[144] "Double tax treaty between Ukraine and Slovakia № 703_673 from 23 January 1996," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

however, exceed that part of the Slovak tax, as computed before the deduction is given, which is appropriate to the income) which, in accordance with the provisions of this Convention, may be taxed in Ukraine.

To conclude, Slovakia and Ukraine opt for the ordinary credit method.

Slovenia. Ukraine concluded a double tax treaty with Slovenia in 2003.[145] The elimination of double taxation is regulated by Article 24. As in the previous treaty, both State Parties opt for the ordinary credit method. The latter is formulated in a clear short-descriptive manner likewise provided in the OECD Model Convention:

Double taxation shall be eliminated as follows:

1. Where a resident of a Contracting State derives income or owns capital which, in accordance with the provisions of this Convention, may be taxed in the other Contracting State, the first-mentioned Contracting State shall allow

a) as a deduction from the tax on the income of that resident, an amount equal to the income tax paid in that other Contracting State;

Such deduction, in either case, shall not, however, exceed that part of the income tax, as computed before the deduction is given, which is attributable, as the case may be, to the income which may be taxed in that other Contracting State.

To conclude, both Slovenia and Ukraine apply the ordinary credit to their tax residents.

Spain. Ukraine has not concluded yet a new double tax treaty with Spain since the termination of the Soviet Union occupation (24 August, 1991). Nevertheless, a double tax treaty concluded with Spain by the Soviet Union in 1975 is valid nowadays.[146] It is a peculiarity that legislation adopted during the Soviet period still applies unless it contradicts the Constitution of Ukraine or is not supersede by newly adopted legislative acts on the same matter.[147] Though the President of Ukraine has requested the Ministry of Finance to sign a new double tax treaty with Spain,[148] the previous treaty applies until it is terminated by another signed treaty.

The treaty Spain-Soviet Union contains the provision on elimination of double taxation. It prescribes neither the elimination nor credit method but refers to the national legislation of the respective state. As analysed above, pursuant to the TCU if Ukraine has a double tax treaty in force with another State, Ukraine applies an ordinary credit method to its taxpayers who work there. Concerning double taxation preclusion in Spain, the latter's domestic legislation requires analysis.

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[145] "Double tax treaty between Ukraine and Slovenia № 705_010 from 23 April 2003," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[146] "Double tax treaty between the USSR and Spain from 01 March 1985," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

[147] "Constitution of Ukraine," *supra note*, 53: Para. 1 of the Chapter XIV.

[148] "Order № 373/2020-рп," President of Ukraine, accessed 18 November 2023, accessed 18 November 2023, https://www.president.gov.ua/documents/3732020-rp-33957.

Sweden. Ukraine signed a double tax treaty with Sweden in 1995.[149] Double taxation elimination is regulated under Article 22. Both State Parties indicate that they apply the credit method but do not specify its type, leaving application of the credit method up to provisions of domestic law:

(1) In the case of Ukraine, double taxation shall be avoided as follows:

As regards the application of the provisions of Ukraine legislation […], (which shall not be contrary to the main principles of this paragraph) Swedish tax which is paid under Swedish legislation in accordance with this Convention […] shall be done by way of a credit against any Ukrainian tax computed in respect of such income in respect of which this Ukrainian tax is computed.

(2) In the case of Sweden, double taxation shall be avoided as follows: (a) Where a resident of Sweden derives income which under the laws of Ukraine and in accordance with the provisions of this Convention may be taxed in Ukraine, Sweden shall allow - subject to the provisions of the law of Sweden concerning credit for foreign tax (as it may be amended from time to time without changing the general principle hereof) as a deduction from the tax on such income, an amount equal to the Ukrainian tax paid in respect of such income.

In Ukraine, given the TCU, the ordinary credit method shall be applicable with states that have a valid double tax treaty with Ukraine signed. Thus, it can be concluded that both State parties undertake the credit method type of which is dependent on the domestic law.

3.3. Introduction of the full exemption method in Ukraine

Since Ukraine aims to join the EU, Ukrainian policy should stimulate its taxpayers to operate therein. Consequently, it is suggested to introduce the full exemption method for Ukrainian taxpayers possessing a permanent establishment in the EU. It may diminish the tax burden imposed on a taxpayer. Firstly, it would mitigate a financial tax burden since the full exemption allows a taxpayer to pay less tax in its residence state. Secondly, it would mitigate a bureaucratic burden enabling a taxpayer not to declare income earned abroad in the residence state (unless the exemption is with progression, which is not the case discussed herein).

However, the issue is whether the exemption method becomes enforceable between Ukraine and EU Member States should the full exemption be introduced in the TCU. Ukraine stipulates in some double tax treaty with EU Member States that provisions of its domestic law "*shall not be contrary to the main principles of this [treaty]*" (for instance, with Austria, Portugal, Sweden, etc). Though Ukraine might amend the TCU, following the example of Lithuania, and provide that "the income of a tax-resident company is not subject to taxation in Ukraine should it be received from

[149] "Double tax treaty between Ukraine and Sweden № 752_001 from 15 August 1995," Ministry of Finance of Ukraine, accessed 18 November 2023, https://mof.gov.ua/en/international_agreements_of_ukraine_on_avoidance_double_taxation-543.

activities through a permanent establishment in a foreign country that is in the European Union if the income has already been subject to taxation there," this provision risks to remain inapplicable. Firstly, given the clause under which "national legislation applies non-contrary to the main principles contained in a double tax treaty." Secondly, the international law provisions prevail over domestic ones. This paragraph examines possible justifications and challenges in case Ukraine introduces the full exemption method in the TCU to benefit its taxpayers operating in the EU.

The latter is known as *pacta sunt servanda* and found its implementation in the Vienna Convention on the Law of Treaties (hereinafter - VCLT).[150] Ukraine is one of the parties of the VLCT. Article 26 and Article 27 of the VCLT prohibit a state from invoking provisions of national legislative acts to justify non-compliance with obligations undertaken pursuant to international treaties. The Law of Ukraine "On International Treaties of Ukraine" also contains a general rule under which international law prevails over domestic law.[151] Owing to Art. 19(2) of this act, "if an international treaty of Ukraine, which entered into force in accordance with the established procedure, establishes rules other than those provided for in the relevant act of Ukrainian legislation, then the rules of the international treaty shall be applied."

Nevertheless, by signing a treaty on elimination of double taxation, Ukraine unilaterally undertook obligation towards its tax residents that operate in a particular state, and not undertake obligation to its state-counterparty itself. Thus, amending the national law by stating that Ukraine applies the full exemption to its taxpayers operating in the EU would not be contrary to obligations towards another State.

It is a rather common conflict when international and domestic laws regulate the same matter differently. In the context of double tax relief, it poses a problem when a double tax treaty and the TCU prescribe different treatment of a taxpayer. Subsequently, an issue on the prevalence of one legal instrument over another appears and requires a solution.

So the issue arises when domestic law provides a more beneficial regime for a taxpayer than it is envisaged in a double tax treaty between the residence state and source state. Following the general approach, an international treaty shall still be applicable though domestic law benefits a taxpayer more compared to the former. However, this problem can be observed from another side.

The TCU presumes a taxpayer's actions to be in compliance with the tax law if several provisions in tax legislation regulate the same matter differently (see Para. 4.1.4 of the TCU). In this case, a taxpayer is allowed to opt for a norm that imposes a less burdensome regime on them and may follow it without a fear of negative consequences. Regarding the status of double tax treaties in the

[150] "Vienna Convention on the Law of Treaties," United Nations, accessed 18 November 2023, https://legal.un.org/ilc/texts/instruments/english/conventions/1_2_1986.pdf.
[151] "On International Treaties of Ukraine," Parliament of Ukraine, accessed 18 November 2023, https://zakon.rada.gov.ua/laws/show/1906-15#Text.

system of Ukrainian legislation, Article 9 of the Constitution of Ukraine provides that international treaties in force, ratified by the Parliament of Ukraine, constitute a part of the national legislation of Ukraine. Thus, the difference in treatment under the TCU and double tax treaty is covered by the presumption under Para. 4.1.4 of the TCU.

Contravention of two legal norms is a concern only of a legislator and not a concern of a taxpayer. This burden of ambiguity shall not be imposed on the later. The European Court of Human Rights (hereiafter - ECHR) pointed out in Para. 52 of the case *Rotaru v. Romania* that the law in question must be sufficiently accessible and foreseeable as to its effects, that is formulated with sufficient precision to enable the individual – if need be with appropriate advice – to regulate his/her conduct.[152] Analogously, in Para. 71 of the case *Rysovskyy v. Ukraine* the ECHR reiterated that the risk of any mistake made by the State must be borne by the State itself and the errors must not be remedied at the expense of the individuals concerned.[153] Both cases have precedential value to the Ukrainian legal system since pursuant to Art. 17 of the Law of Ukraine "On the Execution of Judgments and Application of the Case Law of the European Court of Human Rights," Ukrainian courts are obliged to apply the case law of the Court as a source of law in their proceedings.[154] It leads to the cautious conclusion that irrespective of different approaches suggested to a taxpayer to regulate its conduct by the TCU and treaty, a taxpayer may freely choose among the two ways suggested.

Another hypothethical legal issue might arise upon the accession of Ukraine to the EU. It concerns the prevalence of the EU tax legislation over the TCU and double tax treaties. As aforesaid, international treaties constitute a part of the national legislation of Ukraine. The CJEU pronounces the supremacy of the EU law over the national legislation. In *Flaminio*, the CJEU emphasized that the law stemming from the treaty [Treaty on the Functioning of the European Union], an independent source of law, could not, because of its special and original nature, be overridden by domestic legal provisions.[155] Moreover, the CJEU later also held that the *effet utile* (the useful effect) of the EU law would be weakened if individuals were prevented from relying on it before national courts.[156]

The CJEU, firstly, differentiates the EU law as another independent system of law and, secondly, declares its supremacy over the national one. In this paradigm, the issue might arise if the

[152] "Rotaru v. Romania, Application no. 28341/95," HUDOC, accessed 18 November 2023, https://hudoc.echr.coe.int/eng?i=001-58586.
[153] "Rysovskyy v. Ukraine, Application no. 29979/04," HUDOC, accessed 18 November 2023, https://hudoc.echr.coe.int/eng?i=001-107088.
[154] "Law of Ukraine On the Execution of Judgments and Application of the Case Law of the European Court of Human Rights," Parliament of Ukraine, accessed 18 November 2023, https://zakon.rada.gov.ua/laws/show/3477-15#Text.
[155] "Flaminio Costa v E.N.E.L., Case 6-64," EUR-Lex, accessed 18 November 2023, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A61964CJ0006.
[156] "Yvonne van Duyn v Home Office, Case 41-74," EUR-Lex, accessed 18 November 2023, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A61974CJ0041, para. 12; Georg W. Kofler and Michael Tumpel, "Double Taxation Conventions and European Directives in the Direct Tax Area," in in *Tax Treaty Law and EC Law,* Michael Lang, Josef Schuch, and Claus Staringer (Alphen aan den Rijn: Wolters Kluwer, 2007), 194.

EU tax law, double tax treaty, and domestic law regulate a tax issue vital for a taxpayer in different manners. In this triangle, the EU law should still prevail over a double tax treaty and domestic law.

There is a serious problem with granting more beneficial treatment for taxpayers under domestic law compared to a double tax treaty. However, the solution to this problem may be seen in double tax treaties between Ukraine and the Baltic States (Estonia, Latvia, Lithuania). In provisions devoted to the elimination of double taxation, from the side of Baltic States, there is a clause on application of ordinary credit "unless a more favourable treatment is provided in the domestic law." Without prejudice to a double tax treaty, a taxpayer may apply a more beneficial term under a national legal act. Moreover, it eliminates the need to sign an additional protocol to a double tax treaty in case the domestic legislation is amended.

Nonetheless, Ukraine does not have such a provision in double tax treaties with EU Member States. Thus, the only solution, which would follow the "legally positivistic" approach, is to sign additional protocols to double tax treaties. Additional protocols should prescribe applying the full exemption method from the Ukrainian side.

To summarise the third chapter, Ukraine has valid double tax treaties with all twenty-seven EU Member States. Ukraine applies the credit method (ordinary credit) to all its tax residents operating in the EU without exceptions to any country. On the contrary, though the credit method slightly prevails on the side of the EU Member States, the exemption method remains common too. So, there is no unanimous approach on a method applicable with regard to European taxpayers operating in Ukraine.

Some states precisely specify what type of an exemption (full/progression) or credit (full/ordinary) they apply, whilst others merely prescribe that they apply exemption or credit leaving the subtype to be defined by the their national legislation. Baltic States apply a credit method (ordinary credit) unless a more favourable double tax relief is prescribed by their national legislation. Overall, the methods applicable by EU Member States to taxpayers operating in Ukraine are the following (according to double tax treaty texts):

Exemption:	*Austria, Belgium, Bulgaria, Germany, Hungary, Luxembourg, Netherlands, Poland, Portugal, Romania.*
Credit:	*Croatia, Cyprus, Czechia, Denmark, Finland, France, Greece, Ireland, Italy, Malta, Slovakia, Slovenia, Sweden.*
National legislation reference:	*Estonia, Latvia, Lithuania, Spain.*

CONCLUSIONS

1. Given the analysis of the OECD Model Convention, legal doctrine, and Supreme Court of Ukraine case law, Ukraine undertook the OECD Model Convention as a guideline for concluding its double tax treaties with EU Member States. Thus, the OECD Model Convention and its Commentaries aid the interpretation of double tax treaties between Ukraine and EU Member States, including provisions on double tax relief. The OECD Model Convention suggests exemption and credit methods to preclude double taxation for a legal entity operating through the permanent establishment in another state. Applications of the exemption and credit methods result in the different tax base amounts computed in the residence state.

2. The Commentaries to the OECD Model Convention delineate the full exemption and exemption with progression subtypes of the exemption method. The full exemption applies in a way that a taxpayer pays tax only on an income earned in its residence state. The income obtained in the source state is not included in the tax base in the residence state. The exemption with progression works similarly to the full exemption. However, the difference pertains to the tax rate imposed on the income earned in the residence state. Suppose the income earned in the residence state and the source state exceeds a certain threshold prescribed by the national legislation. In that case, a higher tax rate applies to the income earned in the residence state instead of an ordinary one.

3. The Commentaries to the OECD Model Convention delineate the full credit and ordinary credit subtypes of the credit method. The full credit method requires computing the tax base of a legal entity with the income earned both in the residence state and the source state. The amount of tax already paid in the source state is fully deducted from the tax to be paid in the residence state. The ordinary credit operates similarly unless the tax rate in the source state is higher than in the residence state. For deduction, the tax rate applicable to the income earned in the source state is the tax rate of the residence state. Thus, the tax paid abroad is deducted only partly.

4. There is no apparent prevalence of one applicable method over another among EU Member States. Austria, Belgium, Bulgaria, Germany, Hungary, Luxembourg, Netherlands, Poland, Portugal, and Romania apply an exemption method to their tax residents who have a permanent establishment in Ukraine and pay a corporate income tax there. Croatia, Cyprus, Czechia, Denmark, Finland, France, Greece, Ireland, Italy, Malta, Slovakia, Slovenia, and Sweden undertake the credit method. Double tax treaties of Ukraine with Estonia, Latvia, Lithuania, and Spain refer a taxpayer to their national laws to determine the applicable method.

5. Belgium, Germany, and Romania directly prescribe in their double tax treaties with Ukraine that they apply the exemption with progression method to their tax residents with a permanent

establishment in Ukraine. Austria, Bulgaria, Hungary, Luxembourg, Netherlands, Poland, and Portugal provide that they exempt the income earned in Ukraine from taxation for their tax residents. However, whether the exemption is full or with progression is subject to the national laws of that State. On the contrary, Croatia, Cyprus, Czechia, Denmark, Finland, France, Greece, Italy, Malta, Slovakia, and Slovenia precisely indicate in their double tax treaties with Ukraine that they apply the ordinary credit method to their tax residents who possess a permanent establishment in Ukraine. Ireland and Sweden provide in their double tax treaties with Ukraine that they apply the credit method. However, their national laws should determine the exact full or ordinary subtype.

6. It is beneficial for tax residents from Belgium, Germany, and Romania to conduct business in Ukraine through a permanent establishment if the total income earned in one of these EU Member States and Ukraine does not exceed a threshold prescribed by their domestic law to apply a higher tax rate to the tax base. Though there is no clear indication in double tax treaties with Austria, Bulgaria, Hungary, Luxembourg, Netherlands, Poland, and Portugal that they apply the exemption with progression to their tax residents, the national laws of these states still require analysis to determine whether the exemption is full. Lithuanian tax residents would also benefit from conducting business in Ukraine through a permanent establishment since its domestic legislation allows the full exemption of the income earned by their tax resident through a permanent establishment in a State with which Lithuania has a double tax treaty. Subsequently, this list also includes Ukraine.

7. It is beneficial for tax residents from Croatia, Cyprus, Czechia, Denmark, Finland, France, Greece, Italy, Malta, Slovakia, and Slovenia to conduct business through a permanent establishment in Ukraine if the Ukrainian tax rate is the same or lower than in these respective EU Member States. In such circumstances, the tax paid in Ukraine is fully deducted. But if the tax rate in Ukraine prevails, the tax paid in Ukraine is deducted only partly, given ordinary credit method peculiarities. Though there is no clear indication in the double tax treaties of Ireland and Sweden that they apply the ordinary credit to their tax residents, the national laws of these States still require analysis to determine whether the credit is full.

8. The research has established that the full exemption is the most beneficial among the methods actually used by States. Calculations are simple, allowing taxpayers to pay tax in the residence state only on the income earned therein. Also, this method is the least bureaucratic as it does not require providing evidence of the income and tax earned abroad to national tax authorities. However, Ukraine applies the ordinary credit method to its tax residents operating in EU Member States. Contrary to the full exemption, ordinary credit is one of the most unfavourable for taxpayers. It does not allow deducting the tax paid in the source state to the fullest extent if the tax rate in the source state is less than in the residence state. Additionally, it requires a taxpayer to provide

documentary evidence regarding the income earned and tax paid abroad. It may lead to double taxation if a tax resident fails to submit the documentary to the Ukrainian tax authority within the time boundaries prescribed for the tax declaration.

RECOMMENDATION

It would be advisory to stimulate the increase of Ukrainian taxpayers' economic activities in the EU since Ukraine intends to join the Union. One of the incentives could be introducing the full exemption method for Ukrainian taxpayers with a permanent establishment in the EU. It would diminish the financial and administrative burden imposed on Ukrainian tax residents conducting business therein. Implementing the full exemption method is possible by signing additional protocols to double tax treaties concluded between Ukraine and EU Member States.

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ABSTRACT

The master thesis analyses double taxation preclusion between Ukraine and European Union Member States. Exemption and credit double taxation preclusion methods are described alongside their subtypes (full exemption, exemption with progression, full credit, ordinary credit). The analysis establishes that the full exemption method is the most beneficial for taxpayers since it allows them to pay less tax in the residence state, while the ordinary credit is the most burdensome in this regard. The thesis lists particular EU Member States that apply exemption and credit to their taxpayers operating in Ukraine through a permanent establishment. The thesis reveals that Ukraine uses the ordinary credit method for its taxpayers, possessing a permanent establishment in the EU. Subsequently, an author recommends that the Ukrainian legislator implements the full exemption method for those taxpayers who operate in the EU to incentivize their economic presence in the Union.

Key words: double taxation, exemption, credit, double tax treaties, permanent establishment.

SUMMARY

ANALYSIS OF DOUBLE TAX RELIEF PROVISIONS IN DOUBLE TAX TREATIES BETWEEN UKRAINE AND MEMBER STATES OF THE EUROPEAN UNION

The thesis **aim**s to analyze double tax relief methods applicable between Ukraine and EU Member States. To achieve this aim, the **objectives** of the research are these: 1) to identify double tax relief types and mechanisms of their work; 2) to determine the most beneficial and the most burdensome double tax relief for a taxpayer; 3) to examine which double tax relief methods are present in double tax treaties concluded between Ukraine and EU Member States; 4) to recommend the most beneficial double tax relief for Ukrainian tax policy applicable in the future.

The research is divided into **three parts**. The **first part** pertains to the causes of double taxation emergence between Ukraine and EU Member States. The author describes concepts of residence state, source state, taxing rights of such states, alongside criteria to determine the residential link and permanent establishment. It is found out that double taxation occurs when a tax resident of one state has a permanent establishment in another state and pays a corporate income tax there. While the residence state imposes taxation on the worldwide income of its tax resident (as usual), the source state, where the permanent establishment locates, taxes only income generated within its territory. Thus, a taxpayer becomes subject to double taxation.

The **second part** provides a general overview of double tax relief methods. To mitigate double taxation, the OECD Model Convention suggests exemption and credit methods for States to follow in their double tax treaty practice. Ukraine and EU Member States followed the OECD Model Convention as a guideline for the conclusion of their respective double tax treaties. This part observes subtypes of double tax reliefs (the full exemption/exemption with progression and the full credit/ordinary credit), their advantages, and disadvantages for a taxpayer. Following this, the **third part** observes methods present in double tax treaties between Ukraine and EU Member States. The research reveals that Ukraine applies the ordinary credit method to its tax residents who have a permanent establishment in the EU and pay a corporate income tax there.

As a **result**, it is concluded that the full exemption method is the most advantageous for a taxpayer since it allows them to pay less tax in the residence state, and it does not require additional bureaucratic procedures such as confirmation of the tax paid abroad. It has been recommended that Ukraine applies the full exemption method to its tax residents who operate in the EU through a permanent establishment to incentivize them and stimulate more robust economic cooperation between Ukraine and the EU.