

# How to Punish a Foreign Company without it Breaching Ukrainian Legislation



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One of the most common kinds of violation of Ukrainian currency legislation is breach of the import-export transactions procedure. Breach of this procedure is not always a consequence of a fault of a business entity, including a foreign company. It is also worth mentioning that sanctions for breach of the import-export transaction procedure may significantly complicate the activities of a foreign company and block its supplies to Ukraine.

The procedure for import-export transactions is specified in the *On the Procedure for Settlements in Foreign Currency Act of Ukraine*. This Act stipulates that the proceeds of entities which perform foreign economic activity shall be credited to their currency accounts in authorized banks within the period of debt repayment, specified in the contract, but not later than 180 days following the prepayment. In addition, the National Bank of Ukraine is entitled to introduce other terms for settlements for up to six months. During the last two years the National Bank of Ukraine has been using its right regularly by prolonging the validity of its restrictions, under which the period for settlements in foreign economic activity is reduced to 90 calendar days.

In practice, this means that if within 90 calendar days following the prepayment date the goods fail to pass customs clearance on the territory of Ukraine or are supplied in volumes different from those for which prepayment was made, special sanctions may be applied to entities which perform foreign economic activity pursuant to the *On the Procedure for Settlements in Foreign Currency Act of Ukraine*.

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The sanctions are applied by the Ministry of Economic Development and Trade of Ukraine on the basis of submission from the State Fiscal Service of Ukraine, and such sanctions provide for application of the special licensing regime to entities which perform foreign economic activity. This regime causes considerable problems for performance of foreign economic activities, because it requires obtaining approval from the Ministry of Economic Development and Trade of Ukraine for each separate foreign economic transaction.

One should pay attention to the fact that in the event of breach of terms for settlements the special sanction of individual licensing regime is also applied to the foreign

counterparty of the Ukrainian party at fault. However, there could be no fault on the part of the foreign counterparty in breach of currency legislation. Such foreign counterparty, as provided by the agreement, could have fully performed all its undertakings for supply of goods to Ukraine.

Such decision on the part of the Ministry of Economic Development and Trade of Ukraine actually blocks activities of a foreign company, because, while not being notified on the applied sanctions, its foreign economic transactions with other Ukrainian counterparties are suspended and may be resumed only upon obtaining an individual license for each separate transaction (which is very demanding and may result in



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breach of terms of supply) or cancellation/suspension of the individual licensing regime (pursuant to the effective procedure, suspension or cancellation of the individual licensing regime may take up to 30 days).

Such sanctions, due to the absence of breach legislation on the part of a foreign counterparty, are commonly misunderstood by foreign importers and, taking into account the speed of the modern trade, are deemed to be archaic. So what is the logic of the Ministry of Economic Development and Trade of Ukraine in applying the special sanctions, and why are foreign economic entities held liable without any fault on their part?

The answer to this question lies in the approaches used in legal regulation of liability of the entities which perform foreign economic activity (residents) and their counterparties (foreign entities). Foreign economic activity is treated as a very special area of business activity, where, in certain cases, sanctions might be applied to the entities without their active involvement in violating legislation. This is due to the fact that the actions of Ukrainian as well as foreign entities which perform foreign economic activities may harm the economic security of the state and, therefore, prevent the

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performance of Ukraine's international obligations.

Application of sanctions against foreign counterparties is aimed at preventing violations, which may have negative consequences for the state overall. Thus, application of the special licensing regime is an instrument of control, which helps the Ministry of Economic Development and Trade of Ukraine to identify all circumstances, under which violation of currency legislation took place, and make a decision on the further activity of such companies.

In circumstances when a breach of import-export transaction procedure by counterparty led to application of the special sanctions, all parties to a foreign economic contract are required to obtain approval from the Ministry of Economic Development and Trade of Ukraine on their foreign economic transactions and register their individual licenses. Pursuant to Regulations on Procedure for Issuing of Individual Licenses, an application for an individual license is considered within 15 business days. In addition, a state duty of 0.2% of the contract's value shall be paid.

As evidenced by court practice in 2014-2015, the efforts of the parties to a foreign economic contract, to which the Ministry of Economic Development and Trade applied its special sanctions, to appeal against the Ministry's decision in court were, in most cases, unsuccessful. Even in the absence of a fault in breach of Ukrainian currency legislation, the courts take into consideration the fact that in the event of breach of import-export transaction procedure the State Fiscal Service of Ukraine is entitled to make submissions to the Ministry of Economic Development and Trade of Ukraine pursuant to Article 37 of the *On Foreign Economic Activity Act of Ukraine*, and, respectively, the Ministry itself, on the basis of such submission, shall make its own decision on whether to apply the special sanctions.

The State Fiscal Service of Ukraine, by initiating application of the special sanctions towards the entities which perform activities, has several objectives, namely: to prevent mechanisms of illegal export of foreign currency abroad and outflow of foreign currency from Ukraine; to detect activities on legalization of pro-

ceeds acquired in an illegal manner; and to identify non-resident companies whose activities might be fictitious.

As mentioned, application of the special sanctions by the Ministry of Economic Development and Trade of Ukraine towards bona fide non-resident companies might come as a complete surprise to the latter ones and will result in additional expenses connected with, for example, payment for storage of goods at a customs warehouse. In order to minimize the risk of additional expenses incurred during cooperation with Ukrainian counterparties, the foreign companies should thoroughly track the terms for settlements under the foreign economic contract and, in case of their breach, check the list of companies towards which the special sanctions were applied (in order to identify whether the company was included in such a list). In the event that the company identifies in a timely manner that the Ministry of Economic Development and Trade of Ukraine decided to apply the special sanction in the form of the individual licensing regime towards the company, application of such a sanction might be prevented upon early reaction.

The risk of applying the individual licensing regime towards the foreign company due to breach of terms for settlements under the foreign economic transactions on the part of a Ukrainian counterparty might be fully mitigated in case of 100% prepayment for the supplied goods. This is due to the fact that in such cases sanctions will be applied to a foreign company only in the event of breach of Ukrainian currency legislation by such a foreign company itself.

Taking into consideration the difficult economic situation in Ukraine and deficit of foreign currency in Ukraine, such measures are one of the means for preventing the outflow of foreign currency abroad. However, on the other hand, in modern trade, where speed, predictability and certainty play an important role, such demanding, and in some cases completely unexpected for foreign companies, measures under Ukrainian law, will not contribute to strengthening the image of Ukraine as a suitable platform for trade and commerce.

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