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## PREREQUISITES AND CONSEQUENCES OF THE USE OF OFFSHORE JURISDICTIONS BY UKRAINIAN BUSINESSES

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Offshore zones, as legal, financial and tax entities, attract the attention of both governments and the business environment. These zones are used for a variety of purposes, including reducing the tax burden, ensuring confidentiality, privacy and asset protection, as well as facilitating business. However, the use of offshore zones is also associated with risks, which include tax abuse, tax evasion, corruption and money laundering. One of the catalysts of the “offshorization” processes on a global scale was scientific and technical progress, the wide and rapid development of modern means of communication and communication. The emergence and development of the global Internet, satellite communications, etc. have reduced the time required for communication between fairly remote parts of the world to a minimum. The listed points together created qualitatively new opportunities for the comprehensive and rapid development of the offshore sector of the world economy, which allowed it to reach a qualitatively new level. Recent years have been characterized by growing attention to transparency and the fight against tax evasion at the international level. Ukraine is implementing measures to control transactions with offshore jurisdictions and ensure transparency in taxation. The study of this topic allows to reveal the peculiarities of the legal, financial and tax environment of offshore jurisdictions, to identify the advantages and risks of their use, as well as to understand the influence of offshores on the economy and international relations.

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## ПЕРЕДУМОВИ ТА НАСЛІДКИ ВИКОРИСТАННЯ ОФШОРНИХ ЮРИСДИКЦІЙ УКРАЇНСЬКИМ БІЗНЕСОМ

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### **Ключові слова:**

офшорні юрисдикції,  
офшоризація,  
бізнес-середовище, фінанси,  
економіка, ризики

Офшорні зони, як правові, фінансові та податкові утворення, привертають увагу як держав, так і бізнес-середовища. Ці зони використовуються для різних цілей, включаючи зменшення податкового тягаря, забезпечення конфіденційності, приватності та захисту активів, а також спрощення ведення бізнесу. Проте, використання офшорних зон також пов'язане з ризиками, які включають податкові зловживання, ухилення від сплати податків, корупцію та легалізацію доходів злочинного походження. Одним з каталізаторів процесів «офшоризації» у світовому масштабі став науково-технічний прогрес, широкий і бурхливий розвиток сучасних засобів зв'язку і комунікації. Поява і розвиток глобальної мережі Інтернет, супутникового зв'язку і інше скоротили практично до мінімуму часові витрати процесу комунікації між досить віддаленими частинами світу. Перераховані моменти в сукупності створили якісно нові можливості для всебічного і стрімкого розвитку офшорного сектору світової економіки, що дозволило йому вийти на якісно новий рівень. Останні роки характеризуються зростаючою увагою до прозорості та боротьби з податковим ухиленням на міжнародному рівні. Україна впроваджує заходи з контролю операцій з офшорними юрисдикціями та забезпечення прозорості в оподаткуванні. Вивчення цієї теми дозволяє розкрити особливості юридичного, фінансового та податкового середовища офшорних юрисдикцій, виявити переваги та ризики їх використання, а також зрозуміти вплив офшорів на економіку та міжнародні відносини.

**Formulation of the problem**

Despite the attractiveness of offshore zones for the business environment, due to the reduction of the tax burden, the provision of privacy and protection of company assets, as well as the simplification of doing business, their use is also associated with risks, which include tax evasion, corruption and the legalization of proceeds of crime. Therefore, an important task for Ukraine is the implementation of constant control in operations with offshore jurisdictions, as well as ensuring a balanced approach to taxation and avoiding tax abuses in order to create a fairer and more efficient taxation system, contributing to the increase of the tax base and ensuring financial stability.

**Analysis of recent research and publications**

Considerable attention of national and foreign scientists has been devoted to the question of the essence and peculiarities of the activity of offshore jurisdictions, to the study of their impact on the country’s economy and ways of countering them. The article examines the research of James Henry “The Price of Offshore Revisited” [1], N.O. Mudrak “National mechanisms for combating tax evasion through offshore jurisdictions in OECD countries” [3], N.P. Yuzhanina, T.O. Frolova, Z.O. Lutsyshina “Evolution of offshore business” [5].

**Formulation of the goals of the article**

The main goal of the article is to consider the main prerequisites and consequences of the use of offshore jurisdictions by business in Ukraine in the pre-war period and to provide recommendations for solving the problems of de-offshorization in the future.

**Presenting main material**

In the modern world, offshore zones have become one of the most popular and effective business and investment tools. Offshore zones provide opportunities to reduce tax payments, protect privacy and provide more favorable conditions for doing business. However, the terms “offshore” and “offshore zone” do not always have a clear and unambiguous definition.

Offshore is a country or part of it with special business conditions for foreign companies. Offshores allow you to reduce the tax burden, hide the real owners of the business and protect assets. Different scientists define the concept of “offshore” differently, but in general, the following characteristics of offshore zones can be

distinguished [2, p. 6]: low rate of income tax or its absence; simplified form of reporting or its absence; hiding the real owners of the business; preferential currency and customs regime; high level of privacy and protection against raiding.

Offshore jurisdictions can be classified by acceptable fields of activity for their residents as follows (Table 1):

It is important, that this classification is conditional, as the capabilities and limitations of various offshore jurisdictions may change depending on many factors, such as the political situation, legislation, economic development, and others.

The consequence of offshoring was the opening of new opportunities for peripheral countries: largely due to this, many of them had the opportunity to assert themselves, for many of them offshore business became the basis of economic development.

Prerequisites for the use of offshore jurisdictions may be, in particular, tax burdens and the complexity of the tax system in Ukraine, the unpredictability of tax policy and insufficient transparency of financial processes. Additional factors include high bureaucratic procedures, the complexity and length of processing permit documentation, as well as insufficient protection of property rights and business contracts.

If you pay attention to the business of Vinnytsia, Dnipropetrovsk, Lviv, Odesa, and Kharkiv regions, in total, almost 300.000 enterprises work in them. The share of “offshore” companies among them differs in different regions, but not significantly: 4.7% of “offshore” companies from the total number of enterprises in Odesa region; 2.4% in Dnipropetrovsk region; 2.3% in Vinnytsia region; 2% in Kharkiv region; 1.9% in Lviv region. However, in quantitative terms, the difference is more noticeable: if in Vinnytsia there are a little more than 400 “offshore” enterprises, then in Odesa there are more than 100 of them [3].

To date, there are no accurate statistics in Ukraine that would reflect the number of offshore jurisdictions and controlled foreign companies owned by Ukrainian citizens. This creates certain difficulties in assessing the real scale of the use of such structures by Ukrainian businessmen and individual entrepreneurs, as well as in the process of assessing the consequences of the use of offshore jurisdictions by businesses in Ukraine.

However, the available data from the pre-war period allow us to analyze the problem under study (Table 2).

Thus, from the data in the table. 2 we can see that the degree of offshorization of Ukraine in the pre-war period was at a fairly high level and amounted to an average of 61%. In 2020–2021 the degree of offshoring of the

Table 1 – Classification of offshore jurisdictions

Branch	Приклади офшорних юрисдикцій
Financial services	Bahamas, Bermuda, Cayman Islands, Switzerland, British Virgin Islands, Seychelles, St. Kitts and Nevis, Dubai
Technologies and innovations	Ireland, Singapore, Hong Kong, Costa Rica, Estonia, Gibraltar, Malta
Real estate and investments	Bahamas, British Virgin Islands, Cayman Islands, Dubai, Gibraltar, Malta, Panama, Seychelles
Tourism and guest business	Bahamas, Maldives, Mauritius, Seychelles, Barbados
Production and logistics	Hong Kong, Singapore, Cayman Islands, Malta, Dubai
Medicine and health care	Malta, British Virgin Islands, Cayman Islands, Bermuda, St. Kitts and Nevis

Source: [4]

Table 2 – Direct investments from Ukraine (2016–2021)

№	Country	2016	2017	2018	2019	2020	2021
1	Virgin Islands	51.3	57.6	61.0	59.9	33.7	41.2
2	Cyprus	1401.5	1249.7	1214.5	1229.8	1431.4	1093.3
3	Latvia	70	68.4	61	72.5	73.0	81.1
4	Netherlands	11.2	10.7	12.3	11.8	11.3	3.8
5	EU	1716.8	1562.3	1485.5	1510.2	2351.1	1923.5
Share of direct foreign investments in offshore states from Ukraine		0.61	0.58	0.56	0.58	0.67	0.68

Source: [7; 8]

economy of Ukraine reached a maximum – 67% – 68%, respectively.

Since 2017, the European Union, the fiscal authorities of whose countries also bear considerable losses from offshore operations, has been keeping a “List of tax jurisdictions that do not cooperate in the field of taxation.” According to the decision of the EU Council, the black list includes American Samoa, Anguilla, Dominica, Fiji, Guam, Palau, Panama, Samoa, Seychelles, Trinidad and Tobago, the US Virgin Islands and Vanuatu. It is worth noting that the 12 offshore companies included in the EU list have a rather weak influence on the Ukrainian economy.

This conclusion can be reached after conducting an analysis of direct foreign investments from these countries into the domestic economy, because often the money taken offshore is returned back in the form of investments and the volume of foreign trade turnover.

According to the State Statistics Service, as of October 1, 2020, Panama made the largest contribution to the Ukrainian economy – 342.3 million dollars, through the 12 countries featured in the “EU black list.” Of the total amount of foreign investments of 34.727 billion dollars, that is exactly 1%. The contributions of other offshore companies from the EU list are much more modest: the Dominican Republic with 23.5 million dollars, the USA and Anguilla with 0.7 million dollars.

The most profitable trade partner of the 12 offshore jurisdictions on the EU list for Ukraine is the Seychelles, having bought Ukrainian goods worth \$5,540 million in

2020. And they sold their own for only 389.6 thousand dollars. In second place is Panama with an indicator of 2.671 million dollars. and 1.809 million dollars. accordingly.

Statistics of foreign trade with offshore jurisdictions from the EU list look better for Ukraine (Fig. 1).

Countries that are not officially offshore continue to be the leaders in withdrawing funds from Ukraine. Cyprus is a leader in foreign direct investment in Ukraine. So, as of 2020, the amount of its investments amounted to 10.3 billion dollars, the second place in terms of direct foreign investments was taken by the Netherlands – 7.56 billion dollars. The largest volume of foreign trade turnover fell on Cyprus – 50.82 billion dollars. As for exports, Great Britain is the leader – Ukraine exported \$66.7 billion worth of goods to Great Britain. [5].

We systematize the consequences of using offshore jurisdictions by businesses in Ukraine:

- decrease in GDP – the use of offshore jurisdictions can lead to a decrease in the country’s GDP. This is possible due to the withdrawal of part of the profits and assets from the economy of Ukraine, which were transferred to offshore zones. This can lead to reduced investment, reduced tax revenues and job losses;

- loss of tax revenues – the use of offshore jurisdictions allows businesses to avoid taxation in Ukraine or pay significantly lower taxes. This leads to a decrease in tax revenues to the state budget. A decrease in tax revenues may limit the government’s ability to implement social and economic programs;

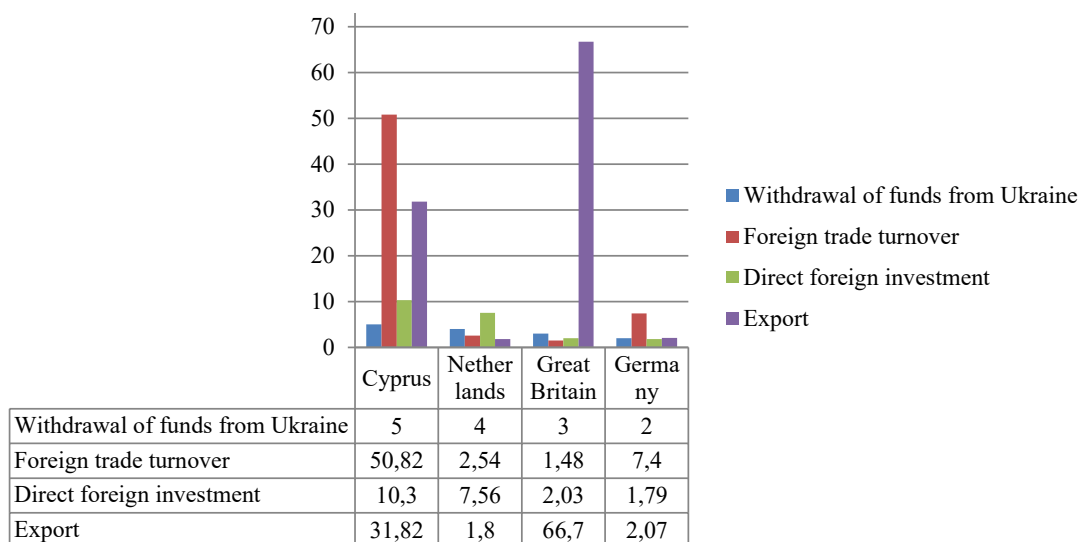


Fig. 1. External relations of Ukraine with offshore jurisdictions from the EU list for 2020 [4; 7; 8]

– a threat to financial stability – the use of offshore jurisdictions can create a threat to the country's financial stability. This can happen if businesses transfer assets to offshore zones in order to avoid risks associated with changes in the economic and political environment of Ukraine. This can undermine confidence in the national currency and banking system;

– impact on international trade – the use of offshore jurisdictions can have an impact on the volume of Ukraine's international trade. This is possible due to the creation of artificial schemes for the movement of goods between countries exclusively “on paper” without their physical transportation;

– negative image and loss of trust – the use of offshore jurisdictions can lead to a negative perception of Ukraine in the international community and a loss of trust on the part of foreign partners. This can make it difficult to do business and attract foreign investment;

– loss of control and increase in corruption – the use of offshore jurisdictions can lead to loss of control over financial flows and increase in corruption. This can create conditions for illegal operations, money laundering and terrorist financing;

– changes in legislation and international agreements – growing international pressure to combat tax evasion and money laundering leads to changes in legislation and the conclusion of international agreements limiting the use of offshore jurisdictions. This may lead to the loss of certain benefits that were provided by the use of offshore structures.

The use of offshore jurisdictions such as Belize, Panama, BVI, etc. in the field of business is often perceived with a negative connotation associated with illegal schemes or tax evasion. However, modern global and national initiatives, such as the BEPS plan and the exchange of tax information, are actively used both at the global level and in Ukraine to combat tax base erosion. This leads to significant transformations in the use of offshore businesses [1].

Ukraine is engaged in the implementation of international standards and initiatives aimed at ensuring ownership transparency and combating financial violations. These measures are aimed at increasing transparency and control in transactions with offshore jurisdictions, as well as ensuring a balanced approach to taxation and avoiding tax abuses. This makes it possible to create a fairer and more efficient taxation system in Ukraine, contributing to the increase of the tax base and ensuring financial stability [2, p. 10].

It is worth paying attention to the fact that in the modern period the Tax Code of Ukraine (TCU) already includes measures aimed at preventing tax abuse due to transactions with non-residents that are carried out from offshore jurisdictions. Provided certain value criteria are met, such transactions with related non-residents and jurisdictions with low tax rates are considered controlled and subject to transfer pricing rules (TPRs). Accordingly, Ukrainian companies are obliged to submit an annual report to the DPS on all controlled operations, to prepare documentation from the TCU, which substantiates the consistency of prices, and, if necessary, to adjust the financial result.

### Conclusion

Due to the lack of complete statistical information on the number of offshore companies owned by Ukrainian citizens, it is important to conduct research and analyze other available data sources, such as reports of international organizations, financial statements of entrepreneurs, information on the legal and tax base, as well as expert opinions and studies on this topic. In general, the implementation of measures aimed at controlling operations with offshore jurisdictions is an important stage in ensuring transparency and compliance with international standards in the field of taxation. This contributes to increasing confidence in the Ukrainian economy, attracts investments and contributes to the sustainable development of the country.

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