

US–Ukraine Policy Dialogue

Economics and Business Task Force

In June 2005, the Economics and Business Task Force made the following recommendations:

- Create a uniform public vision of economic reforms for the President and the Government of Ukraine.
- Build institutional capacity of Ukrainian Government for the implementation of radical, systematic and sustainable market economic reforms.
- Enhance property rights protection, strengthen the rule of law and reduce the tax burden.
- Increase integration in global economy.

Since that meeting, the Ukrainian government has failed to make progress on these goals. The failure to implement these recommendations has contributed to chaotic policy making. Ukraine's dysfunctional process of making economic policy has contributed to the slowdown in economic growth, as entrepreneurs have been discouraged from investing in the Ukrainian economy.

The November Task Force has developed specific economic policy recommendations for the Ukrainian government and US administration for the next 4 months based on the June statement.

Recommendations to Ukrainian Government

1. Create a New System for Formulating and Implementing Economic Policy

1.1. Issue a uniform public vision of economic reforms. The president, prime minister, and parliamentary faction leaders should issue a clear joint policy statement that the role of the Ukrainian government is to create a free, competitive market environment in which the private sector can flourish. The Ukrainian government should focus on efficiently providing public goods such as education, health care, and infrastructure.

1.2. Immediately consolidate all economic policy initiatives under one Cabinet committee in charge of economic policy chaired by the Prime Minister. The committee should have a trained, full-time staff that would prepare concept papers, draft legislation, and work with the Rada to pass legislation. After legislation has been passed, the committee should develop an implementation plan and be responsible for progress on implementation.

1.3. The public administration task force should issue policy papers on the transformation of public administration and initiate public consultations. The papers should address the creation of a completely new system of public policy decision making and implementation based on EU baselines for public management. These include designing contracting procedures and financial controls for competitive public procurement so as to stop corruption and creating a responsive, effective, democratic civil service. It also includes thoroughly evaluating government activities and programs on the basis of effectiveness and public interest and the appropriate level, national, regional, or local, for providing public services.

2. Accelerate efforts to accede to WTO and to establish a Free Trade Area with the EU by launching a public information campaign highlighting the benefits of free trade. As long as Ukraine remains outside the WTO, Ukrainian farmers and manufacturers will face discrimination on foreign markets.

3. Create a market-friendly regulatory framework for businesses and consumers

3.1 Immediately request the Verkhovna Rada to abolish the Commercial Code and amend the Civil Code to be consistent with best international examples. Businesses in Ukraine operate in an unpredictable, chaotic legal environment because Ukraine has two contradictory legal codes pertaining to business affairs: a Commercial Code, styled on Soviet-era laws, and more market-oriented yet imperfect Civil Code.

3.2. Within the next 60 days, the Government should prepare a new draft law on joint stock companies based on EU standards and work with Verkhovna Rada to pass the law.

Under the existing law, managers can easily loot companies of their property and major shareholders cheat minority shareholders.

3.3. Immediately cancel excessive regulations according to the list proposed by the Council of Entrepreneurs, bring all remaining regulations into accordance with the new law on the system of permits, and enhance the effectiveness of one-stop shop procedures. Ukraine's regulatory system imposes enormous costs on businesses and fosters corruption.

3.4 Adopt laws on the financial sector on leasing, derivatives and other financial transactions in accordance with best OECD practices.

4. Stop corruption at state-owned enterprises

4.1 Managers of state-owned enterprises suspected of fraud should be immediately place on leave, prosecuted, and punished. Some managers are looting their enterprises, stealing funds and property that belong to the people of Ukraine, costing the people of Ukraine billions of hryvnias each year.

4.2. Provide a public inventory of all property owned by the state. It should then transfer all government property, including that owned by the Presidential Secretariat and the Rada, to the State Property Fund. It should then design a program to rapidly and transparently privatize this property.

5. Righting the tax system

1) In March 2005, the Ukrainian government introduced a highly distorting value-added tax (VAT) on imports of equipment that form part of a foreign investment in Ukraine. This measure effectively imposes a 20 percent tax on foreign investments, discouraging investors and slowing economic growth. The Ukrainian government should eliminate this tax.

2) The current system of import duties and VAT refunds for exporters is broken. By not refunding VAT to exporters, the Ukrainian government steals money from businesses and prevents the expansion of exports, investment, and jobs. The Ukrainian government should speed customs clearance and refund of VAT payments to exporters.

3) The Ukrainian government should grant local authorities to levy and collect taxes, decentralizing the financing and provision of government services.

6. Facilitate the development of not-for-profit organizations in Ukraine

The not-for-profit sector plays an important role in market economies and democratic societies, providing charity, encouraging policy debates, and contributing to the public good. Ukrainian not-for-profits are not allowed to generate revenues and their sponsors are taxed heavily, limiting the

activities and development of this sector. The Ukrainian government should revise tax legislation to encourage the development of the not-for-profit sector.

Recommendations to the U.S. Government

- 1. The U.S. Congress should lift the Jackson-Vanik Amendment as it applies to Ukraine immediately.** There is no basis for applying the Jackson-Vanik amendment to Ukraine. The U.S. Administration should work closely and actively with Congress to lift the amendment as applied to Ukraine immediately.
- 2. The U.S. government should be more flexible in bilateral trade negotiations with Ukraine.** It should also encourage U.S. government agencies to work closely with Ukraine to provide finance, technical assistance, and advice on achieving market economy status.
- 3. Concentrate technical assistance to Ukraine on implementing the recommendations of the US-Ukraine Policy Dialogue.**