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INTRODUCTION

Established in 1956, the International Finance Corporation (IFC) provides investment and advisory services on a global scale. As a member of the World Bank Group, IFC assists the governments of developing countries to create an enabling business climate and increase their appeal to investors by recommending modifications to their regulatory and institutional framework.

IFC’s technical assistance program in Ukraine was launched in 1993. In 1996, under its Business Development Project, IFC began to conduct annual surveys of the SME sector in Ukraine to analyze the business environment for these firms. These surveys have been effective in promoting policy reform on private sector development issues and have been a useful tool for monitoring the progress of various reforms and changes in the business environment.

This Report summarizes the results of the 2004 survey, based on in-depth and comprehensive polling of 2,800 Ukrainian SMEs and on focus groups and expert assessments. The survey was co-funded by the Ministry of Finance of Norway and IFC.

The objectives of the survey were to define the current state of the entrepreneurial environment and its key trends and to identify administrative barriers to business. This Report is not an all-encompassing review of the problems faced by SMEs in Ukraine, nor does it represent the views of IFC or the government of Norway. Rather, it presents the views of entrepreneurs on the policy matters that affect them.

The Business Development Project would like to express its sincere gratitude to the State Committee of Ukraine for Regulatory Policy and Entrepreneurship, as well as to experts Andrey Lotish, Maksim Naumenko, Igor Priyanchik and to all those who worked on this survey.

This Report is to be published in English and Ukrainian. The project team will do their utmost to ensure that the three versions are identical; however, in the event of any discrepancy, the English version is to be considered definitive.

The Report is available, in both printed and electronic forms, at the following address:
The economic restructuring which has taken place in Ukraine over the past ten years has directly affected the development of the small and medium enterprise (SME) sector. Measures introduced by the government to facilitate the transition to a market economy have created necessary pre-conditions for private enterprise growth.

According to the State Statistics Committee, the number of SMEs is on the rise. Yet throughout its development, this sector is especially sensitive to changes in the regulatory environment. Thus, entrepreneurs' perceptions of the quality of the business climate and their assessment of the regulatory processes and procedures are important indicators for both the government and the business community, as they allow for the monitoring of changes occurring in the SME sector.

The annual studies of the business environment in Ukraine, conducted by the International Finance Corporation (IFC) with funding from the Government of Norway, allow for monitoring changes to the business environment through the eyes of Ukrainian entrepreneurs.

In 2003 the Ukrainian government facilitated a number of qualitative changes in the regulatory environment for private business:

- A clear-cut procedure for the adoption of business-related legal acts was put into place.
- A law setting forth a single window state registration procedure was enacted.
- Two out of three mandatory permits for launch of business activities were abolished.

Nevertheless, survey results and information gathered through focus groups demonstrate that certain serious grievances voiced by the business community remained unresolved in 2003. Unstable legislation, contradictions in regulatory procedures and corruption still hinder private business development in Ukraine.

80% of polled entrepreneurs believe that the current level of legislative change hinders development of their business and creates an unfavorable business environment. The year 2003 saw the adoption of more than 1,200 business-related legal acts.

Ambiguous phrasing in guidelines covering most regulatory procedures allows for significant leeway in the interpretation of normative acts and regulations, gives rise to biased decisions, and increases rent-seeking opportunities for government officials. Only 18% of survey respondents say that they do not resort to unofficial payments to “solve problems.”
What are the reasons behind such a state of affairs? What should and can government do to bring about qualitative changes in relations between entrepreneurs and authorities?

Detailed survey results, set forth below, will be helpful for finding replies to the above queries. Conclusions are accompanied by facts describing each of the procedures covered by the survey, as well as by recommendations outlining future steps aimed at improving the business environment, which may be taken by government agencies as well as by organizations promoting the SME sector development in Ukraine. Recommendations whose implementation can produce fairly immediate results are presented at the end of this section.

**SMEs’ Perception of State Authorities**

Nearly half of respondents said that their company is negatively affected by actions undertaken by state authorities.

- Most entrepreneurs believe that state officials are inconsistent in their interpretation of business-related legal acts. A mere 30% of company managers hold the view that local authorities abide by legislation adopted at the national level. An even smaller percentage of survey participants (20%) think that local authorities ensure equal business conditions for everyone.
- Only 14% of company managers believe that the justice system can protect their contractual interests or their property in business disputes.
- Unofficial payments remain widespread. Only 18% of all respondents stated that they do not resort to unofficial payments to “solve problems.”
- The survey demonstrated that only every fourth company was a member of business or trade association. Nearly 80% of the non-members believe that such membership will not benefit them.

**Recommendations**

1. Improve the system of notification of entrepreneurs about changes in business-related legislation as well as in functions and responsibilities of local authorities through use of the Internet and other resources.
2. Promote the development of business associations as organizations representing the business community by introducing a practice whereby all draft amendments to business-related legislation should be vetted by business associations prior to their adoption.
3. Consider the possibility of transferring a portion of fee-based services currently rendered by state agencies to the private sector (for example, expert assessments to obtain permits and certification of goods).

**Registration**

A number of decisions have been adopted by the government to improve the registration procedure. However, to render the procedure more efficient, a solution needs to be found to a number of technical issues, while registration-related legislation should be brought into compliance with other legal acts.

- To simplify business registration, a one-stop shop model was introduced in Ukraine in 2002-2003. Its main achievement was a nearly 50% reduction in the time required to register a business. Registration through the one-stop shop model averaged 20 working days, whereas the usual procedure required 38 days.
- Experimental one-stop shop models were not efficient enough: registration costs did not decrease, unofficial payments were still rife and companies continued to encounter difficulties in obtaining required information.
- The Law “On State Registration of Legal Entities and Individual Entrepreneurs,” enacted on 1 July 2004, introduced the following new features:
  - A “one window” principle, allowing entrepreneurs to register with all state agencies simultaneously, and
  - A single database, the “Unified State Register,” which lists all companies and entrepreneurs in Ukraine. The information contained in the register is accessible to the public as well as to state agencies.
- However, a number of issues need to be resolved before the new law can be fully implemented. Some of the provisions of the new law on registration should be brought into compliance with the Commercial and Civil Codes as well as with other legal acts.
Recommendations

1. The State Committee for Regulatory Policy and Entrepreneurship and state agencies involved in business registration should urgently agree upon procedures of the new registration process, and make sure that related legal acts and internal agency instructions are duly amended.

2. The State Committee for Regulatory Policy and Entrepreneurship, in concert with business associations representing SMEs, should ensure extensive and in-depth coverage of the new procedure by mass media and internet outlets, develop and distribute materials explicating new registration procedures so that companies are able to study them in detail.

3. The provisions of the new laws governing the registration of NGOs, financial institutions, political parties, trade unions, as well as business liquidation, issuance of free and paid-for certificates, and notarization of documents, should be closely analyzed to ensure their compliance with applicable legislation, including the Civil and Commercial Codes.

Permits

Problems flowing from the unjustifiably broad list of permits, the overall number of permit issuing bodies, and ambiguous issuance procedures render obtaining permits one of the most acute barriers to business for Ukrainian companies. The commercialization of permit issuing procedures has brought permits to the attention of state agencies, but this attention has so far not entailed any qualitative changes to the system. There is a growing need to optimize the quantitative and qualitative aspects of the system of permit issuance in Ukraine.

- The current system of permit allocation applies to all operating firms and results in a serious administrative barrier for SMEs.
- 70% of companies obliged to obtain permits in 2003 rated the procedures as either complex or very complex. This can be primarily ascribed to the cumbersome, non-transparent and often outmoded legislation which governs permit issuance.
- In 2003, less than 3% of all permit applications were turned down. This fact points to significant possibilities for introducing self-certification as a principle for issuance of a majority of permits.
- Permits are often issued for short validity periods, thus obliging entrepreneurs to secure the same permits on a regular basis.
- An analysis of applicable legislation, international practice and expert assessments by state agencies demonstrate that if Ukraine is to have an effective permit system, the current system must undergo systemic reform.

Recommendations

1. The list of activities requiring permits should be defined in unified legislation. Entrepreneurs cannot be obliged to secure permits for activities not included in this list.

2. Legislation should divide permits into two groups: the first should include permits for a concrete list of activities deemed highly hazardous to public health, safety or the environment; the second should include all other permits.

3. The second group of permits should be obtained through self-certification, a process in which state agencies do not exercise discretion in permit issuance, and applications are registered and automatically approved within a few days of submission.

4. Introduce mandatory, uniform requirements for the content of legal acts and other regulations which cover permit issuance procedures.

5. Mandate that legal acts covering permits be approved by the Cabinet of Ministers of Ukraine before they may come into force.

6. Clearly define the procedure for interaction between private sector firms authorized to issue permits, approvals, or expert assessments, and applicants, state agencies and municipal authorities involved in this process.
**Licensing**

The survey revealed a whole host of problems, related to both the legal regulation of licensing procedures and their application:

- The following aspects of licensing procedures caused most problems for surveyed companies: the need to prepare a large number of documents (38%); lengthy processing times (24%); ambiguous requirements (21%); and constantly changing licensing procedures (21%).
- More than half of surveyed firms (61%) found licensing costs burdensome in 2003.
- Licensing processing times in 2003 exceeded the timeframes set forth in applicable legislation.

**Recommendations**

1. Tighten control over license-issuing bodies’ compliance to licensing procedures.
2. Create databases that are accessible to entrepreneurs and contain information on license issuing bodies, mandatory documents, licensing conditions, costs, etc.
3. Specify criteria for the content and format of documents which must be submitted with license applications.

**Certification and Standards**

Procedures to ensure compliance with Ukrainian standards and standardization procedures are regarded by most firms as a burden and a liability rather than as a tool for boosting competitiveness. Certification and standardization are contradictory, as the state agencies involved routinely fail to furnish entrepreneurs with either exhaustive or correct information, while private entities are not actively engaged in attempts at reforming the system.

- Enacted in 2001 to bring technical regulation in Ukraine closer to EU standards, the following three laws “On Conformity Assessment,” “On Standardization” and “On the Accreditation of Certification Bodies” have yet to be fully implemented. Key lapses in implementation include:
  - Because technical guidelines to these laws have not yet been adopted, the European approach to conformity assessment, declared in the new legislation, has not been implemented.
  - Of 10,000 standards, a little more than 1,600, including about 500 in 2003, have been harmonized with those accepted internationally.
  - The process of accrediting certification bodies is extremely slow, which negatively affects the certification market.
- In 2003, 20% of surveyed firms went through conformity assessment procedures, with 88% of these firms liable for mandatory product certification. Voluntary certification is not widespread in Ukraine: only 8% of all companies chose to certify their goods and quality control systems on their own initiative.

**Recommendations**

1. The State Committee for Consumer Policies and Standards must speed up the development and adoption of technical guidelines regulating conformity assessment, in order to shorten the list of products subject to mandatory certification.
2. Technical guidelines covering conformity assessment should be minimal and limited to assuring product safety. Quality standards should be voluntary rather than mandatory.
3. The State Committee for Consumer Policies and Standards should quicken the pace of renewal and harmonization of state standards by attracting manufacturers, business and sectoral associations into the process.
4. The State Committee for Consumer Policies and Standards, as well as other agencies involved in the conformity assessment process (specifically, mandatory certification of imported goods), should review their procedures to make them more straightforward and transparent.
**Taxation**

Entrepreneurs believe that the tax system remains one of the most serious barriers to private enterprise development in Ukraine.

- Survey results demonstrate that 74% of companies in Ukraine considered the tax system either a serious or very serious hindrance to the development of their business.
- The following areas were identified as the most acute problems in taxation in 2003: high tax rates (75%); constantly changing legislation (74%); large number of taxes (72%); and frequent changes to reporting procedures (69%).
- Half of eligible companies made use of the simplified taxation system. The majority of those that did not switch claim simplified tax is economically inexpedient for their firm.
- The most difficult taxes for planning business activities in 2003 were cited as income tax, value added tax (VAT) and mandatory social security deductions.
- The shadow economy remains problematic for Ukrainian SMEs: only 16% said that companies similar to theirs did not evade taxes. Entrepreneurs estimate that every fifth enterprise does not report over 20% of its revenue to tax authorities.

**Recommendations**

1. Systematize tax legislation by adopting a Tax Code.
2. Taxation privileges should come up for review and those granted by the Cabinet of Ministers’ classified ordinances should be scrapped. Only tax privileges for investments should be preserved.
3. Ensure strict observance of the Law of Ukraine entitled “On the Taxation System,” which mandates that amendments to laws on benefits, changes in taxes and in the tax payment procedure shall be made at least six months prior to the end of the fiscal year and shall come into force at the start of the next fiscal year. The law’s application should be expanded to include tax registration and reporting, as well as normative documents that are not deemed laws.
4. It is necessary to review the way deductions to compulsory state social insurance are shared by enterprises and employees. This can be achieved by setting up an efficient non-state insurance system which would be beneficial for employees.

**Inspections**

Inspections continue to be a source of obstacles to private business development in Ukraine, a premise borne out by their number, duration and consequences. The survey results reveal that in addition to serving a controlling function, state inspections of enterprises are also used for purely fiscal purposes.

- Inspections in Ukraine continue to affect nearly all SMEs: 94% of surveyed firms were subject to on-site inspections in 2003. A similar percentage of polled businesses were inspected in 2002.
- Inspections are still a source of obstacles to private business development in Ukraine, a premise borne out by their number, duration and consequences.
- In 2003 the Tax Authorities, the Department of Fire Safety and the Sanitary Epidemiological Service led the way in terms of number of inspections carried out. This situation mirrors the state of affairs seen in 2002.
- The system of inspections does not fully perform its key function, namely preventing violations of safety standards and requirements. Instead, inspections carry out a fiscal function.
- Companies based in smaller regional capitals attract more inspections and suffer higher fines than their counterparts in large cities. This trend is not the result of differences in ratio of inspectors to number of companies.
- Entrepreneurs believe that the penalties imposed for failure to abide by regulations are nearly the same as the costs borne by a firm in complying with all legal provisions and norms.
- Two-thirds of entrepreneurs believe that the adoption of a unified Law on Inspections would be the most effective tool for regulating inspections duration and frequency.
Recommendations

1. At the legislative level, develop and adopt uniform requirements to the contents of normative acts regulating inspections procedures.

2. Mandate that all agency regulations covering inspection procedures be approved by the Cabinet of Ministers.

3. Review technical specifications and requirements of inspecting agencies to make them more straightforward and remove outmoded norms. Norms should be approved by the Cabinet of Ministers.

4. Develop and adopt a modern system for designating inspections, based on assessment of risk to public health and safety of a particular enterprise and/or sector of business.

5. Adopt, at the level of each inspecting agency, uniform regulations describing in detail procedures to be followed during inspections of business, based on model regulations developed and approved by the Cabinet of Ministers. These regulations should stipulate the rights and responsibilities of the inspector and the business being inspected, as well as clearly define the limits of the inspector’s authority.

6. Introduce, at each controlling agency, a checklist for carrying out inspections of business. During an inspection each inspector runs through the list of questions on his standardized list. Such checklists can be used to systematize and render inspections procedures more efficient, while assuring that inspectors do not overstep the bounds of their authority.

7. Consider the possibility of moving closer to European standards by abandoning the practice of allowing inspecting agencies to keep the portion of the fines they collect in order to fill budgetary gaps. Fines should be gathered centrally, while agency budgets should only be allocated from the centralized state budget.

External Financing

Seeking financing from outside sources is yet to become a universally-accepted practice in Ukraine. Although the volume of bank loans and the percentage of companies securing bank financing were on the increase in 2003, banks are not yet considered a feasible source of funds for investment projects. In addition, only 2% of those polled turned to non-banking financial institutions for credit.

- A quarter of survey respondents considering investment projects in 2003 approached banks for funds. In comparison with 2002 the share of successful SME applicants rose by 9%, to 79%.
- High interest rates precluded 35% of polled SMEs from seeking bank financing.
- Long-term loans extended for 3 to 5 years increased from 3% to 8% of total loans received, in comparison with 2002. At the same time, the portion of loans granted for a period longer than 5 years remains insignificant (less than 1%). Thus, bank funding is yet to become a feasible source of finance for investment projects in Ukraine.
- A mere 4% of Ukrainian companies intending to acquire equipment resorted to leasing to refurbish fixed assets, despite that fact that 34% of respondents needed to buy equipment in 2003.

Recommendations

1. The National Bank of Ukraine should seek out ways to increase the stability of the banking sector by influencing its basic behavioral stimuli (for example, improved corporate governance of the banking sector).

2. Develop the securities market or push through a pension system reform in a bid to create a source of long-term financing, which in turn will reduce interest rates.

3. Roll out a program to raise entrepreneurs’ awareness of the efficiency of outside sources of funds and mechanisms of securing bank loans, non-bank credits and leasing loans.
Exports

An insignificant share of Ukrainian SMEs exported their goods in 2003. The following administrative barriers hold back the development of exports: anti-dumping measures imposed on Ukrainian firms, quotas introduced by importing countries, and non-tariff restrictions\(^1\) put in place by Ukraine.

- Only 6% of operating SMEs exported their goods in 2003. A further 3% planned to export, but did not for a variety of reasons.
- The export capability of Ukrainian SMEs is limited by commercial factors: 59% of companies that either exported their products, or planned to do so, reported that they face negative effects from tough competition in foreign markets.
- Administrative barriers also hinder export development: anti-dumping measures affect 43% of exporting firm, whereas quotas imposed by importing countries are a hindrance for every third of those who export or intended to do so.
- Ukraine also erects the following non-tariff barriers for export transactions which affect 40% of exporting firms: sanitary and customs controls; licensing and certification of exported goods; and the requirement to transfer foreign exchange revenues to Ukraine within a specified period of time.

Recommendations

1. Reduce the internal non-tariff restrictions imposed on exporters. Create and implement a plan for the gradual simplification of export-related procedures and a reduction in the number of required documents.

2. Motivate the tax, customs and treasury authorities to resolve the problem of VAT reimbursement delays.

3. Consider the possibility of ensuring that Ukrainian exporters have access to databases containing information about importers.

4. Step up the work of trade departments of Ukrainian embassies and use export growth as a key indicator of their performance.

Some of the recommendations made in this report can produce results within a relatively short period of time – a year or less. Consequently, these recommendations should be regarded as guidelines for attaining short-term objectives in the field of regulatory reform. The table below lists 17 such recommendations.

---
\(^1\) Non-tariff restrictions are a combination of economic and administrative measures which lie outside the purview of customs and tariff restrictions and are aimed at regulating foreign trade. These include quotas and customs control procedures.
## 17 Steps for Reform within a Year

| Entrepreneurs’ Perception of State Authorities | • Improve notification of entrepreneurs on changes to business-related legislation, as well as in functions and responsibilities of local authorities, through use of the Internet. |
| Registration | • Agree upon registration procedures and make sure that related legal acts and internal agency instructions are duly amended. • Ensure detailed coverage of the new registration procedures by mass media outlets and through the Internet. |
| Permits | • Stipulate all activities which require permits in legislation. Activities not stipulated by the legislation do not require permits. • Introduce self-certification as a means for obtaining certain permits. • Clearly define the procedure for interaction between private sector firms authorized to issue permits, approvals and/or expert assessments, and applicants, and state agencies and municipal authorities involved in the permit process. |
| Licensing | • Create databases that are accessible to entrepreneurs and contain information on license issuing bodies, mandatory documents, licensing conditions, costs, etc. |
| Certification and Standards | • Develop and adopt technical guidelines for goods subject to mandatory certification. |
| Taxation | • Develop and adopt a Tax Code to systematize existing taxation legislation. |
| Inspections | • At the legislative level, adopt uniform requirements to the contents of normative acts regulating the inspection procedures. • Develop and adopt a modern system for designating inspections, based on assessment of risk to public health and safety of a particular enterprise and/or sector of business. • Adopt, at the level of each inspecting agency, uniform regulations describing in detail procedures to be followed during inspections of business, based on model regulations developed and approved by the Cabinet of Ministers. These regulations should stipulate the rights and responsibilities of the inspector and the business being inspected, as well as clearly define the limits of the inspector’s authority. • Eliminate the practice of remitting a percentage of fines collected to the inspecting agency imposing fines. |
| External Financing | • Roll out a program to raise entrepreneurs’ awareness of the efficiency of outside sources of funds and mechanisms of securing bank loans, non-bank credits and leasing loans. |
| Exports | • Step up the work of trade departments of Ukrainian embassies and use export growth as a key indicator of their performance. • Reduce the internal non-tariff restrictions imposed on exporters. Create and implement a plan for the gradual simplification of export-related procedures and reduction in the number of required documents. |
The total number of SMEs grew in 2003, though the year-over-year increase was slightly less than in previous years. According to the State Statistics Committee, 962,000 companies were registered in Ukraine as of the end of 2003.

**Chart 2.1**  
The Number of Registered and Operating SMEs Continued to Rise in 2003

*number of companies (thousands)*

<table>
<thead>
<tr>
<th>Year</th>
<th>Registered Companies</th>
<th>Operating Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>770</td>
<td>489</td>
</tr>
<tr>
<td>2001</td>
<td>837</td>
<td>443</td>
</tr>
<tr>
<td>2002</td>
<td>900</td>
<td>489</td>
</tr>
<tr>
<td>2003</td>
<td>962</td>
<td>520</td>
</tr>
</tbody>
</table>

Source: State Statistics Committee

Of the companies listed in Ukraine’s Unified State Register prior to 2004, 54% were active companies (required to file reports of banking transactions.) Micro and small companies accounted for the bulk of active companies.

**Chart 2.2**  
Micro and Small Companies Account for the Majority of Operating Companies

*% of acting enterprises*

<table>
<thead>
<tr>
<th>Size of Company</th>
<th>2002</th>
<th>2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro (1-10 employees)</td>
<td>71%</td>
<td>71%</td>
</tr>
<tr>
<td>Small (11-50 employees)</td>
<td>23%</td>
<td>23%</td>
</tr>
<tr>
<td>Medium (51-250 employees)</td>
<td>5%</td>
<td>5%</td>
</tr>
<tr>
<td>Large (251-1000 employees)</td>
<td>1%</td>
<td>1%</td>
</tr>
</tbody>
</table>

Source: Based on State Statistics Committee data

Despite their numbers, micro and small companies have yet to have a significant impact on the Ukrainian economy.

**Chart 2.3**  
SME Indicators in Selected CIS Countries (excluding individuals with no employees)

<table>
<thead>
<tr>
<th>Indicators</th>
<th>Ukraine¹</th>
<th>Russia²</th>
<th>Belarus³</th>
<th>Kazakhstan⁴</th>
</tr>
</thead>
<tbody>
<tr>
<td>SMEs per 1,000 residents</td>
<td>5</td>
<td>6</td>
<td>6</td>
<td>3</td>
</tr>
<tr>
<td>Population employed in SMEs (%)</td>
<td>19</td>
<td>21</td>
<td>20</td>
<td>10</td>
</tr>
<tr>
<td>SME contribution to GDP (%)</td>
<td>7</td>
<td>8</td>
<td>11</td>
<td>8</td>
</tr>
</tbody>
</table>

¹ State Statistics Committee of Ukraine: www.ukrstat.gov.ua  
² Russian SME Support Agency: www.ra.siora.ru  
³ Ministry of Statistics and Analysis of Belarus  
⁴ based on Statistics Agency of Kazakhstan data: www.stat.kz
Although SMEs represent a relatively small portion of total employment and GDP, they benefit the economy through their ability to adapt rapidly, with limited resources, to economic restructuring. SMEs also create employment and help to foster a competitive business environment. SMEs have the flexibility to meet the needs of specialized markets, often through subcontracting with larger companies. They are frequently the source of innovation and thus play an important role in a free market economy. In addition, SME owners tend to represent a segment of the population characterized by stability, an important part of democratic society.

SMEs enjoy government support in most developed countries. Support includes funding for NGOs to represent and promote the interests of SMEs and to monitor the implementation of government programs.

### Chart 2.4: Key Indicators of SME Development and Promotion in Developed Countries

<table>
<thead>
<tr>
<th>Indicator</th>
<th>USA</th>
<th>Canada</th>
<th>Japan</th>
<th>Germany</th>
<th>France</th>
<th>Italy</th>
<th>Great Britain</th>
<th>India</th>
</tr>
</thead>
<tbody>
<tr>
<td>SME Contribution to GDP</td>
<td>52%</td>
<td>43%</td>
<td>52%</td>
<td>57%</td>
<td>50%</td>
<td>55%</td>
<td>52%</td>
<td>7%</td>
</tr>
<tr>
<td>SME Contribution to Employment</td>
<td>50%</td>
<td>47%</td>
<td>70%</td>
<td>70%</td>
<td>57%</td>
<td>71%</td>
<td>56%</td>
<td>5%</td>
</tr>
<tr>
<td>SMEs as a Percentage of All Companies</td>
<td>98%</td>
<td>99.8%</td>
<td>99%</td>
<td>99%</td>
<td>98%</td>
<td>99%</td>
<td>99%</td>
<td>98%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Annual Financial Support for SMEs ($US billions):</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business Development Infrastructure</td>
</tr>
<tr>
<td>Loans</td>
</tr>
<tr>
<td>Loan Guarantees</td>
</tr>
</tbody>
</table>

| Government Procurement and Subcontracting        | National procurement system |

<table>
<thead>
<tr>
<th>Business Support Infrastructure for SMEs (number of institutions):</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Services</td>
</tr>
<tr>
<td>SME Development Centers</td>
</tr>
<tr>
<td>Information Centers</td>
</tr>
<tr>
<td>Business Incubators and Technology Centers</td>
</tr>
<tr>
<td>Export Promotion Centers</td>
</tr>
<tr>
<td>Social Centers</td>
</tr>
<tr>
<td>Promotion</td>
</tr>
</tbody>
</table>

Source: 5th All-Russian Conference of Small Businesses, March 2004
*Private sector loans
Sales Growth and Profitability

The companies surveyed were asked for their gross sales figures for 2003.

About 60% of the companies surveyed reported increased sales in 2003. The financial services sector reported the highest increase and the food and beverage services sector experienced the lowest.

With the exception of the manufacturing sector, growth in sales outstripped growth in profitability in 2003.

* 9.3% of respondents reported operating at a loss in 2003 (based on Survey data)
Analysis of the survey data showed that larger companies tended to be more profitable. This is mainly because larger companies can produce goods with higher value added and benefit from economies of scale.

**Chart 2.7 Large Enterprises Were More Profitable in 2003**

<table>
<thead>
<tr>
<th>Category</th>
<th>Profitability (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large (251-1000 employees)</td>
<td>10%</td>
</tr>
<tr>
<td>Medium (51-250 employees)</td>
<td>8%</td>
</tr>
<tr>
<td>Small (11-50 employees)</td>
<td>7%</td>
</tr>
<tr>
<td>Micro (1-10 employees)</td>
<td>7%</td>
</tr>
</tbody>
</table>
Survey respondents identify unstable legislation and corruption as key barriers hindering private business development in Ukraine.

The majority of entrepreneurs believe that civil servants are inconsistent in their interpretation of business-related legislation. Only 30% hold the view that local governments act in strict compliance with all the laws and normative acts adopted by central authorities. An even smaller percentage (20%) believes that local administrations ensure equitable business conditions for all market participants.

Only 14% of company directors believe that the judicial system is capable of upholding their contractual or property interests in commercial disputes.

Unofficial payments remain pervasive. Only 18% of companies said that they had never made unofficial payments to civil servants to "resolve issues".

Ukrainian companies are not actively involved in business associations. Only every fourth enterprise claims membership of a business or trade association. Of those who remain outside business associations, 80% hold the view that such membership will not be beneficial to their firm.

The regulatory and administrative environment is universally viewed as an important ingredient of a country's business climate. Even in developed countries, regulatory acts adopted to promote public well-being could have a negative effect on the private sector.

The regulatory burden in transition countries, like Ukraine, is compounded by government activities aimed at improving the lot of particular segments of the population. This burden undermines trust in government, lowers the efficiency of state policy and unduly lengthens the transition period.

Survey results demonstrate that relations between private business and the state in Ukraine remain imperfect. Entrepreneurs point to an unstable legislative environment and corruption as key impediments to business (see Chart 1.1 on p.6).

Given that firm owners view unstable legislation and corruption as the most serious barriers for business leads to the premise that entrepreneurs regard the administrative burden facing their firms as the result of actions taken by the authorities to improve personal rather than public well-being.

Ukrainian Companies Give a Poor Assessment of the Performance of the Legislative and Executive Branches of Power

Aproximately, every fourth respondent positively assessed the overall work of the government. However, most directors of Ukrainian companies asked to rate the performance of government agencies with regard to business development came out with a negative assessment. Respondents were chiefly dissatisfied with the Tax Administration, as well as with the legislative and executive branches of power.

As many as 80% of all Ukrainian enterprises regard frequent changes to legislation as a hindrance to business. While modification of a legal framework inherited from a command economy is a normal process of transition, numerous changes to regulations preclude entrepreneurs and politicians from developing long-term strategies, while setting the stage for inconsistent interpretation of regulations, as well as feeding corruption.
An analysis of Ukraine’s legal dynamics reveals that the most active phase of formation of Ukraine’s legal framework came to a close after 1999. Yet, the continually increasing number of legal acts enacted after 2001 demonstrates that the legal environment in the country has yet to stabilize.

The State Tax Administration and the State Customs Service issue the greatest number of business-related legal acts, after the Cabinet of Ministers, the Supreme Council and the President. This is borne out by the number of legal acts governing foreign trade, the functioning of enterprises, the industry and fuel and energy complex, as well as taxation.

The State Tax Administration and the State Customs Service issue the greatest number of business-related legal acts, after the Cabinet of Ministers, the Supreme Council and the President. This is borne out by the number of legal acts governing foreign trade, the functioning of enterprises, the industry and fuel and energy complex, as well as taxation.

When players start a game of cards they know and understand the rules, which remain unchanged for the duration of the game. The rules we have to abide with here in Ukraine are reworked during the game…. Even a qualified lawyer is unable to track the changes to legislation… Even a department at the tax office set up to assist entrepreneurs is hard-pressed to explain how the payment should be made…

Focus Group Participants

The following segments of Ukrainian legislation came under consideration: Budget/Finance, Banking, Entrepreneurship/Licensing/Certification, Taxation, Securities Market, Customs, Foreign Trade, Enterprises/Industry/Fuel and Energy Complex, Transport/Communication, and Accounting/Statistical Reporting. The Chart 3.2 sets forth the number of legal acts regulating each of these sectors, adopted by the agencies most often introducing or amending normative acts: the Cabinet of Ministers, the Rada, the President, the State Tax Administration of Ukraine, the State Customs’ Service, the State Commission for the Securities Market, and the Ministry of Health.
A quality legal act should be easy to understand by those whom it seeks to regulate, namely civil servants and firm employees. Thus, the degree to which the law allows for differing interpretations of its provisions is a measure of the quality of a law and its accompanying legal acts.

The survey showed an increase in the share of firms holding the view that state agencies have become better at interpreting legislation over the past three years. Nevertheless, not all company directors believe that civil servants correctly interpret business-related legal acts. Entrepreneurs are most dissatisfied with the way tax and customs officials treat legislation.

**Violations and Corruption Are Often Emblematic of Executive Bodies**

Instability of legislation, as mentioned above, is one of the reasons that promote inaccurate interpretation of legal acts. Unfortunately, contracting additional or more qualified staff does not always solve this problem for a firm.

**Chart 3.3 Entrepreneurs Believe that Most Civil Servants Incorrectly Interpret Legal Acts**

*To what extent are government agencies consistent and predictable in interpreting legislation?*
Survey respondents state that certain government agencies interpret legal acts appropriately. However, a majority of survey respondents believe that agency officials are often unpredictable in interpreting legislation. This prompts entrepreneurs to resort to unofficial payments to tip decisions in their favor. Chart 3.4 demonstrates that respondents who believe that civil servants do not interpret legislation in a consistent and predictable way are more likely to have paid unofficially to resolve an issue.

Unpredictable interpretation of legislation is not limited to executive bodies. Only 30% of entrepreneurs noted that local authorities in their district unerringly complied with legislation and accompanying legal acts adopted by the national government. An even smaller percentage (20%) hold the view that local administrations create equal operating conditions for all firms. One should note that attitudes of company directors to such actions of local authorities has not changed as compared to 2002.

A detailed analysis of survey results reveals regional variations in entrepreneurs’ opinion of local authorities. Chart 3.5 breaks down regional capitals into the following three groups: (1) cities where entrepreneurs came out with a positive assessment of local government; (2) cities where businessmen were split; and (3) cities where entrepreneurs negatively assessed the performance of local authorities.

Focus Group Participant

... It is believed that a tax inspector knows everything. However, this is often not the case as an accountant is often much better qualified, but the inspector tends to ignore this and still thinks that he knows better...
## Chart 3.5 Entrepreneurs in Most Regional Capitals Negatively Assess the Performance of Local Authorities

<table>
<thead>
<tr>
<th>City</th>
<th>Local authorities comply with legislation</th>
<th>Local authorities do not hinder private business development</th>
<th>Local authorities help startups</th>
<th>Local authorities create equal conditions for everybody</th>
<th>Local infrastructure promotes development</th>
<th>Local bodies supervising business are honest and never demand bribes</th>
<th>Business environment is propitious for investment</th>
<th>Business environment is better than in most regions in Ukraine</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ivano-Frankivsk</td>
<td>~</td>
<td>+</td>
<td>+</td>
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<td>~</td>
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<td>+</td>
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<tr>
<td>Uzhhorod</td>
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<td>~</td>
<td>~</td>
<td>+</td>
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<tr>
<td>Rivne</td>
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<td>+</td>
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<td>Khmelnytsky</td>
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<td>Dnipropetrovsk</td>
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<td>Vinnytsia</td>
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<td>Zhytomyr</td>
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<td>Zaporizhia</td>
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<td>Donetsk</td>
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<td>Kirovohrad</td>
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<td>Lugansk</td>
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<td>Lutsk</td>
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<td>Lviv</td>
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<td>Odesa</td>
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<td>Poltava</td>
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<td>Simferopol</td>
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<tr>
<td>Kharkiv</td>
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<tr>
<td>Chernihiv</td>
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<tr>
<td>Chernivtsi</td>
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</tr>
</tbody>
</table>

"+" – most respondents agreed with the statement  
"~" – most respondents did not agree with the statement  
"~" – respondents were split
Reasons for Emergence of Corruption

Reasons for corruptions are very well explained in the frequently cited so-called conditional equation of corruption suggested by R.Klitgaard:

"Corruption=Monopoly + Freedom of Actions – Accountability. Monopoly of a bureaucrat on services needed by a company while absence of control over the bureaucrat leads to corruption."  

According to results of the survey, major problems in relationship between business and authorities in Ukraine are corruption and factors that follow it (unstable legislation and political instability.) Thus, improved relationship of businesses and authorities is possible only after eliminating the reasons for corruption in the country.

Most Firms Do Not Believe that Ukraine’s Judicial System Will Protect Their Interests

Only 14% of company directors are confident that the judicial system will protect their contractual or property interests during business disputes. At the same time, 40% of polled entrepreneurs do not possess a clear view on this matter, which implies that few of them turn to the court system to resolve commercial disputes.
Unofficial payments are often rooted in problems which company directors encounter while dealing with officials of state agencies. Only 18% of respondents have never made unofficial payments to tip decisions in their favor.

Entrepreneurs report that unofficial payments range from 1% to 10% of annual revenues for most companies. It should be noted that small businesses allocate a larger share of their revenues to unofficial payments than do larger firms. In addition, the incidence of unofficial payments among smaller companies is higher.

**Chart 3.7**  
Many Entrepreneurs Believe the Judicial System Is Corrupt and Unable to Enforce Verdicts  
% of respondents

“How often can the judicial system be described in the following fashion while dealing with dispute resolution:”

- Honest
- Fair and Unbiased
- Fast
- Consistent and Truthful
- Capable of Enforcing Verdicts
- Affordable

**Chart 3.8**  
The Smaller the Company, the More Often It Bears the Burden of Unofficial Payments  
% of respondents

Unofficial Payments As Percentage of Company’s Revenues in 2003:
- Do Not Make Unofficial Payments
- From 1% to 10%
- From 10% to 25%
- More than 25%
Ukrainian Companies Are Not Actively Involved in Business Associations

International experience shows that business associations can successfully represent the interests of SMEs by acting as mediators between the business community and authorities. However, organization of the business community into associations remains of limited popularity in Ukraine.

Although most Ukrainian firms say that they are negatively affected by the actions of local authorities, few firms attempt to defend their interests through business associations. Survey results show that overall only every fourth company is a member of a business or trade association. However, this number grows with the size of a firm — every third medium-sized company and every second large enterprise is a member of a business association.

### Chart 3.9

**Few Companies Try to Close Ranks to Protect Their Interests**

<table>
<thead>
<tr>
<th>% of respondents</th>
<th>Not Involved in Business Associations</th>
<th>73%</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Members of Business Associations</td>
<td>24%</td>
</tr>
<tr>
<td></td>
<td>Do Not Know</td>
<td>3%</td>
</tr>
<tr>
<td></td>
<td>Trade Associations</td>
<td>9%</td>
</tr>
<tr>
<td></td>
<td>Sectoral</td>
<td>8%</td>
</tr>
<tr>
<td></td>
<td>Chambers of Commerce</td>
<td>5%</td>
</tr>
<tr>
<td></td>
<td>Other</td>
<td>2%</td>
</tr>
</tbody>
</table>

Although the share of those involved in business associations varies widely between small businesses and their larger counterparts, it should be noted that most firms give similar reasons for not joining associations. Two-thirds of respondents who chose not to join business associations believe that membership would not benefit their firm in any manner. A smaller percentage of respondents said that they were unwilling to spend either time (12%) or money (2%) on business associations.

### Chart 3.10

**Most Companies See No Benefit from Membership in Business Associations**

% of non-members

- See No Benefit: 68%
- Not Sufficient Time for Involvement: 12%
- High Dues: 2%
- Unaware of Their Existence: 18%
The reasons underlying small companies’ lukewarm attitude to membership in business associations are yet to be fully examined. It can be assumed that key reasons are rooted in the belief that business associations are not capable of assisting entrepreneurs to resolve difficulties. This passivity on the part of respondents may be caused by the fact that the tradition of active involvement of citizens in the creation of market relations in Ukraine is still in its infancy. On the other hand, business associations have yet to generate a great deal of benefits for their members if judged by their ability to save the time of company directors. Survey results demonstrate that entrepreneurs who are members of business associations spent an equal or greater portion of their time dealing with state agencies than non-members.

Survey results show that companies which have not joined business associations tend to be less involved in community improvement issues. This can be attributed to their unwillingness to assume additional taxes to improve infrastructure, remove unfair competition and to simplify the system of state registration.

**Chart 3.11 Membership in Business Associations Does Not Reduce the Regulatory "Time Tax"**

<table>
<thead>
<tr>
<th>Percentage of Time Spent</th>
<th>Member Companies</th>
<th>Non-Members</th>
</tr>
</thead>
<tbody>
<tr>
<td>More than 50%</td>
<td>10%</td>
<td>6%</td>
</tr>
<tr>
<td>25-50%</td>
<td>17%</td>
<td>12%</td>
</tr>
<tr>
<td>Up to 25%</td>
<td>70%</td>
<td>76%</td>
</tr>
<tr>
<td>Did Not Spend Any Time</td>
<td>3%</td>
<td>6%</td>
</tr>
</tbody>
</table>

**Chart 3.12 Members of Business Associations Are More Willing to Pay for Improvements to the Business Environment**

<table>
<thead>
<tr>
<th>Percentage of Respondents</th>
<th>Member Companies</th>
<th>Non-Members</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Improve Infrastructure</td>
<td>51%</td>
<td>45%</td>
</tr>
<tr>
<td>To Simplify Business Regulations</td>
<td>58%</td>
<td>52%</td>
</tr>
<tr>
<td>To Remove Practices Leading to Unfair Competition</td>
<td>65%</td>
<td>56%</td>
</tr>
</tbody>
</table>
The fact that certain companies who are not members of business associations are still prepared to assume additional costs to improve the quality of the business environment, however, bears out the premise that business associations have the potential to expand the market for their services. This, of course, rests on their ability to reach and sustain a high level of service quality.

**Recommendations**

1. Improve notification of entrepreneurs on legal changes and the functions and responsibilities of local administrations through such means as the internet (for instance, VlasnaSprava.info).

2. Promote the role of business associations as representatives of the business community by incorporating their commentary into draft legislation on business-related issues, before new acts or amendments are adopted.

3. Consider the possibility of transferring a portion of fee-based services currently rendered by state agencies to the private sector (for example, expert assessments required for permits and certification of goods).
In 2002-2003, Ukraine introduced an experimental “one-stop shop” company registration process.² On average, one-stop shop registration took 20 working days, while the standard process took 38 days.

In other respects, the experimental process did not realize significant advantages. The cost of registration did not decrease markedly, unofficial payments remained a factor, and companies continued to encounter difficulty in obtaining information.

In 2003, there was no legislation requiring state agencies to participate in one-stop shops and this was the primary reason they did not have a significant impact on the registration process generally.

Enacted 1 July 2004, the Law of Ukraine on State Registration of Legal Entities and Individual Entrepreneurs addressed this issue. The new law included the following provisions:

- Introduction of one-step registration principle, under which companies would register with all applicable state agencies simultaneously; and
- Creation of the Unified State Register, a nationwide database containing information on all registered businesses, accessible not only to state agencies but also to entrepreneurs.

In order for the new law to be effective in improving the registration process generally, however, ratification by all state agencies involved is required. Harmonization with the provisions of economic, civil and other legislation is also necessary.

One-Stop Shops As a Measure to Simplify the Registration Process

In 2002 and 2003, many municipalities throughout Ukraine implemented one-stop shops³ for company registration in an effort to simplify the process. One-stop shops both accepted applications and granted registered status. They were also intended to provide entrepreneurs with complete and accurate information about the documents and procedures for registering a business with all applicable state agencies. For an entrepreneur, registration entailed three visits to the one-stop shop: the first to learn the requirements, the second to submit an application and the third to collect the registration certificate together with confirmation that the registration had been recorded wherever required.

As of 1 January 2004, there were more than 150² one-stop shops of various types in Ukraine, but the model proved difficult to implement consistently throughout the country. One-stop shops were created on the initiative of local authorities, but the state agencies that actually delivered the services (and were not subordinate to the local authorities) often did not fully endorse the concept and were reluctant to allocate staff to it. As a result, one-stop shops varied in the services they provided, and elements such as cost, availability of information, incidence of unofficial payments and complexity of the assessment process remained much as before.

### Chart 4.1 One-Stop Shops Significantly Reduced Registration Processing Time

<table>
<thead>
<tr>
<th></th>
<th>Days Needed in 2003 for Registration/Re-Registration (without intermediaries)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Established Procedure</td>
<td>38</td>
</tr>
<tr>
<td>One-Stop Shop</td>
<td>20</td>
</tr>
</tbody>
</table>

¹ One-stop shops were implemented in many regions of Ukraine on the initiative of local authorities. These facilities took various forms, including information centres and registration offices. The processes for standard and one-stop shop registration are set out in Annex 1 Chart 1 and 2 respectively.

² See the same.

The significant success of one-stop shops was in reducing registration processing time by nearly half. Companies obtained registration in about 20 working days at one-stop shops (without an intermediary) while the standard process took 38 working days.

Apart from Processing Time, One-Stop Shops Did Not Significantly Change the Registration Process

One of the reasons for the lack of significant change was that not all of the state agencies involved in company registration participated in the one-stop shop initiative.4

Owing to the varying degree of participation by the agencies involved, many respondents who registered businesses in 2003 were required to apply to a number of agencies in addition to the one-stop shop. For them, one-stop shop registration was little different from the standard process. Along with the need to apply to several state agencies, other elements in the process were likewise unchanged, including the costs, unofficial payments and difficulties with obtaining information.

One-stop shops were designed to simplify registration in terms of process only, and did not address documentation requirements or official fees. The one-stop shop model was also intended to reduce the incidence of unofficial payments (requests to make voluntary contributions and to subscribe to various periodicals,) and thus the cost of registration, by minimizing the number of individuals with whom the entrepreneur came into contact who had control over part of the process. Owing to these impediments to uniform nationwide implementation of one-stop shops, the cost of registration did not change significantly with this initiative.

Chart 4.2
One-Stop Shops Did Not Offer Comprehensive Registration Services
% of respondents registering at one-stop shops in 2003 (without intermediaries)

Chart 4.3
One-Stop Shop Registration Did Not Cost Significantly Less
% of respondents registering or re-registering in 2003 (without intermediaries)
Of the respondents who registered according to the standard process, 40% paid more than 500 hryvnias (US$94), while approximately 32% of the respondents who opted for the one-stop shop paid more than 500 hryvnias.

One-stop shops were expected to serve as sources of comprehensive registration information. A third of respondents registering or re-registering their businesses in 2003 found it difficult to obtain complete and accurate information with respect to documentation and processing time and costs, regardless of whether they registered at one-stop shops or through the standard process.

The incidence of unofficial payments was not reduced by the one-stop shop initiative in 2003. Approximately one in three respondents registering or re-registering in 2003 reported making unofficial payments, whether they registered at one-stop shops or not.

The number of documents required for registration was identified as the single most important concern by the greatest number companies surveyed, whether they registered at one-stop shops or through the standard process.

It was not the preparation of the six to twelve separate documents that the respondents found onerous, but rather the requirement to submit numerous copies of applications, certificates and confirmations. Moreover, document format varied widely between state agencies.

---

1 See Processes 1 and 2 in Annex 1.
Companies registering through the standard process were required to go to each state agency involved to familiarize themselves with the documentation requirements. One-stop shops were intended to provide information on the requirements of all applicable agencies, thus allowing applicants to get a clear idea about the overall registration process and enabling them to develop the documents for all state agencies simultaneously.

However, the lack of legislation requiring state agencies to participate in one-stop shops made the uniform, nationwide introduction of this initiative difficult and inhibited the model from achieving its full potential.

The one-stop shops that secured the cooperation of all registration agencies performed much better than average, but most one-stop shops did not significantly simplify the registration process.

Comparative analysis of the survey data with respect to the standard registration process and one-stop shops showed that legislative measures are required in order to streamline company registration.

New Law Aims to Simplify the Registration Process

The Law of Ukraine On State Registration of Legal Entities and Individual Entrepreneurs, enacted on 1 July 2004, was based on five years of experience with the standard process, the one-stop shop model in use in a number of EU countries, and the two years of one-stop shop trial in some Ukrainian cities.

The purpose of the law was to simplify the registration process as much as possible. It provides for one-step registration, and once national registration is complete, registration with all agencies is accomplished electronically. The experimental one-stop shop registration depended on the initiative of local authorities. It is expected that once the new law is fully implemented, all agencies involved in the registration process will be required to participate in one-stop shops.

The new law also provides for a Unified State Register, a nationwide database of information on all companies and individual entrepreneurs operating in Ukraine. The information in the registry will have force in law for the purpose of contracts and in settling disputes between parties, and will permit entrepreneurs to research potential partners.

In summary, the new law eliminates all mandatory post-certificate registration processes for entrepreneurs. It reduces the entrepreneur’s interaction with state officials to a single contact, the state registrar, who accepts applications and carries out all registration and mandatory reporting functions.

This approach addresses the underlying problems, also reduces the registration processing time to four days, since entrepreneurs no longer have to apply in person to six different state agencies.

![Chart 4.6 Respondents Identified Excessive Documentation As their Key Difficulty with Registration](image_url)

<table>
<thead>
<tr>
<th>Standard Process</th>
<th>One-Stop Shop</th>
</tr>
</thead>
<tbody>
<tr>
<td>% of respondents registering or re-registering in 2003</td>
<td>49%</td>
</tr>
</tbody>
</table>

*Cabinet of Ministers Resolution No. 740 On the Procedure for State Registration of Companies (25 May 1998)*

*See Chart 3 Annex 1

*See Chart 5, Annex 1*
The new law will largely preserve the general registration requirements. However, although the number of registration documents will remain the same, the law clearly describes these documents, as well as the number of copies required, and stipulates that no additional documents are to be required by state agencies.

Change-Over to the New Registration System Presents Some Difficulties

Implementation of the new law has caused some difficulties for entrepreneurs. In the first month, long lines formed as state agencies struggled to adapt to the new system. The technology infrastructure (communications, equipment, software) to support the new process was not in place, staff had not had sufficient training, and there was a lack of coordination among the agencies involved in the registration process.

In addition, some of the provisions of the new law do not comply with the Civil and Economic Codes. The registration of public service organizations, trade unions and financial institutions has yet to be comprehensively regulated, and the issue of company dissolution has not yet been addressed. The government is working to remedy this, and amendments to the new law are currently being drafted.

*According to survey data. The overall number of days spent on registration.
**As contemplated in the new law, the registration procedures last 4 days: three for registration itself and one for issuing the certificate.
***According to survey data, the procedures remained overall unchanged. Pension funds and the tax authority require formal notification on opening a company bank account. This is considered part of the registration process.

The new law has addressed a number of matters that every district administration was interpreting in its own way. With everything set out in law, the procedures will be easier to understand and less complicated for entrepreneurs. Previously, Dnipropetrovsk district authorities would have one set of requirements and Pecherskiy District would have another … .”

Focus Group Participants

Chart 4.7 Reduction in the Duration of Registration

<table>
<thead>
<tr>
<th>Registration</th>
<th>District Office of National Registry, Four Social Agencies and Tax Authority</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Standard Process</strong> 32 Working Days*</td>
</tr>
<tr>
<td></td>
<td><strong>One-Stop Shop</strong> 19 Working Days*</td>
</tr>
<tr>
<td></td>
<td><strong>State Registrars</strong> 4 Working Days**</td>
</tr>
</tbody>
</table>

| Ministry of the Interior and Bank*** | Corporate Seal Permit 7 Working Days |
|                                       | Opening of Bank Account 2 Working Days |

<table>
<thead>
<tr>
<th>Standard Process</th>
<th>One-Stop Shop</th>
<th>State Registrars</th>
</tr>
</thead>
<tbody>
<tr>
<td>38 Working Days*</td>
<td>20 Working Days</td>
<td>11 Working Days*</td>
</tr>
</tbody>
</table>


*According to survey data, the procedures remained overall unchanged. Pension funds and the tax authority require formal notification on opening a company bank account. This is considered part of the registration process.
The New Law on State Registration

Expectations Raised by the New Law:
- Introduction of a one-stop shop model delivering simultaneous registration with all applicable state agencies
- Short processing time and clear-cut requirements
- Unified State Register in place, with information on all companies and individual entrepreneurs in Ukraine
- Access to information about companies and their officers (for example, for concluding a contract or researching partners)
- The choice of designating either an office address or a home address as the legal address of the business
- Fewer fictitious companies and fewer companies with the same name

Obstacles to Implementing the New Law:
- Requires significant investment in technology and training
- Legislative amendments and/or further legislation required to harmonize the procedures of all state agencies
- Safeguards needed against potential abuse of discretionary powers by individual registrars (Registrars accept or reject registrations, but since they effectively report to the head of the local executive committee, rejection is difficult to appeal)

Problems Reported by Respondents:
- Lack of information about the new process
- Insufficient training of staff and technical problems at offices (of particular concern in the districts)
- Regulations allow broad interpretation and individual discretion in their application, and thus permit inconsistent treatment of applicants by state agencies, which is often perceived as abuse (particularly in the regions)
- Slightly more complex procedure for the preparation of documents (company charters must comply with the new Civil and Economic Codes and must also be notarized, making the procedure more costly)
- Need to secure certificates and update registration cards annually

Even under the new law, registration alone is not enough for a company to become operational. To begin operations, every Ukrainian company must obtain at least one permit (from the Fire Department). Simplifying the registration process is only one of the necessary steps in reforming the business entry regulatory system. This initiative should be followed up by measures to simplify permit issuance and licensing.  

Recommendations

1. The State Committee for Regulatory Policy and Entrepreneurship, as well as other state agencies involved in business registration, should, as a priority matter, harmonize registration processes and ensure that the related legislation, regulations and internal procedures are duly amended.

2. The State Committee for Regulatory Policy and Entrepreneurship, in cooperation with business associations representing SMEs, should ensure extensive and in-depth dissemination of information on the new process, including through press releases and web sites and through developing and distributing printed materials that set out and explain the new registration process so that companies are able to study them in detail.

3. The provisions of the new law that govern the registration of public service organizations, financial institutions, political parties and trade unions, as well as those dealing with business dissolution, criteria for free and fee-based requests to the regulatory agency for confirmation of company information and the notarization of documents should be closely analyzed to ensure their consistency with other legislation, including the Civil and Economic Codes.
No Enterprise in Ukraine Can Operate Without Permits. The Average Cost Is 690 Hryvnyas and the Average Processing Time Is 33 Days

Ukrainian companies need permits in order to operate. Before 2003, permits issued by the Fire Department, the Sanitary and Epidemiological Service and the Labour Protection Department were mandatory in order for a company to begin operations.

The Chart below shows the most prevalent permits. The actual number of permits in Ukraine is close to 1,200. Of these, about half serve no useful purpose, according to at least one expert, and some are issued perfunctorily yet remain mandatory.

A distinguishing feature of permits for connection to an electricity grid (9% of respondents), a water supply (8%) or a gas network (5%) is that the connection approval permit is generally issued by local authorities or their designated agents, but the actual connection requires further state approvals as well as a contract.

1 The term “permit” herein means any documented decision of a state agency, local government body or other authority empowered to sanction certain actions or allow a company to operate in a line of business.


3 For example, fire safety permits are mandatory, for both purchased and leased premises, according to Article 10 of the Law of Ukraine No. 3745-XII On Fire Safety (17 December 1993).


The permits system in Ukraine applies to all companies. It is perceived as a serious administrative barrier to entrepreneurship.

As many as 70% of the companies granted permits in 2003 rated the procedures as either “complex” or “very complex”, primarily owing to Ukraine’s complicated and dated legislation governing permits.

Less than 3% of permit applications were refused in 2003, highlighting the possibility of introducing an application procedure of issuing permits.

Permits are often issued for short periods and entrepreneurs are obliged to secure them repeatedly. Permit-issuing bodies rely on the income from the permit fees and are resistant to change.

An analysis of the applicable legislation, international experience and expert assessments by state agencies demonstrates that if Ukraine is to have an effective permits system, systemic reform is needed.
Most of the companies surveyed cited Ukrainian law as the root cause of the complexity of the permits process. It is significantly different from EU law including the following elements:

- The many laws governing permits: According to some estimates, permit issuance procedures in Ukraine are regulated by 167 laws, 150 orders issued by the Cabinet of Ministers and 1,500 pieces of facilitating legislation passed by central and local governments.

- Complexity of the criteria for granting or refusing a permit and inconsistency in application: Many of the requirements that companies find hardest to meet date back to the Soviet era.
Unclear principles and rules governing the calculation of permit fees: In an overwhelming number of cases, legislation does not specify the fees. Private firms or expert centres set up by permit-issuing agencies are often available to prepare the documents needed to secure permits, including expert assessments, evaluations and condition assessment reports, surveys, inspections, tests, etc. The fees for these services vary, and are set out in a contract with the applicant.

Responsibility for permit issuance as between the levels of government is not yet allocated, as administrative reform is still in progress.

There is no clear legal framework or procedure governing the interaction of companies statutorily authorized to be involved in the permit process, applicants and all of the levels of government that issue permits.

Legislation does not clearly define the procedure for obtaining any given permit, such as the number of state agencies involved; the time and funds required, and the complete list of documents and the requirements for their preparation.

The absence of uniform rules for enacting laws governing permits allows state agencies to establish their own rules and subsequently alter them. One effect of this is that the granting of permits is often at the discretion of a single individual within those agencies. Entrepreneurs find it quite difficult to obtain information about permits, even from the state agencies responsible for granting those permits.

### Chart 5.4
Ambiguous, Inconsistent and Outdated Legislation Impedes Permit Applications

<table>
<thead>
<tr>
<th>% of respondents obtaining permits in 2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Excessive Number of Documents Required</td>
</tr>
<tr>
<td>Need to Deal with Several State Agencies</td>
</tr>
<tr>
<td>Complex Procedures and Unclear Requirements</td>
</tr>
<tr>
<td>Lengthy Processing Periods</td>
</tr>
<tr>
<td>Uncertainty in Procedures</td>
</tr>
<tr>
<td>Inaccessibility/Absence of Information</td>
</tr>
<tr>
<td>Unofficial Payments</td>
</tr>
<tr>
<td>High Cost of Document Preparation</td>
</tr>
</tbody>
</table>

### Chart 5.5
For Entrepreneurs, State Agencies Are the Principal Source of Information on Permit Procedures

<table>
<thead>
<tr>
<th>% of respondents obtaining permits in 2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>State Agencies, in the Course of Application</td>
</tr>
<tr>
<td>Laws</td>
</tr>
<tr>
<td>Acquaintances with Experience in Obtaining Permits</td>
</tr>
<tr>
<td>Advisory Services, Consultants</td>
</tr>
</tbody>
</table>
To address the problem of access to information and to make their regions more attractive to investors, some local governments have established “one-stop shops”. One-stop shops aim to enable entrepreneurs to obtain information from and submit documents to the state agencies directly involved in the process.

Less Than 3% of Permit Applications Were Refused in 2003

The aforementioned problems with the permit system had no bearing on the ratio of permits granted and refused in 2003.

The low incidence of refusal can be ascribed to the reliance of permit-issuing bodies on the income from permit fees. Moreover, permits have short validity periods and entrepreneurs must renew them repeatedly.
In the course of securing a permit, companies incur a variety of costs, both for the permit itself and for obtaining the necessary expert assessments, approvals, etc. The permit-issuing bodies that rely on the income from these fees are resistant to change in this area.

"The permits issued by fire departments are temporary in 91% of cases because companies find it impossible to comply with the requirements for permanent permits."

Civil Servant

In the course of securing a permit, companies incur a variety of costs, both for the permit itself and for obtaining the necessary expert assessments, approvals, etc.
Most of the respondents obtaining permits in 2003 rated the cost of the process as either “quite expensive” or “unacceptably expensive”. In addition to fees for the permit itself, many companies pay firms or the expert centres set up by permit-issuing agencies to prepare the application documents, including expert assessments, formal opinions, condition assessments, surveys, inspections and tests.

The existing business permits system is in need of systemic reform to attain the following objectives:

- Ensure that all required permits are necessary in the public interest.
- Create transparent and efficient permit-issuance procedures.
- Reduce the number of state agencies involved in the issuance of the same permit.
- Clearly define permit fees.
- Adapt sanitary-epidemiological, veterinary, fire safety, construction and other rules to EU and WTO standards.

**Recommendations**

1. The activities requiring permits should be statutorily defined. Entrepreneurs should only be obliged to secure permits for the activities thus defined.

2. Legislation should provide for two categories of permits; one comprising permits for activities with the potential to affect public health and safety and the environment, and the other comprising permits for operating most lines of business involving non-hazardous materials or activities.

3. A policy including the following criteria should be introduced for the second category of permits:
   - Entrepreneurs should decide for themselves whether they meet the requirements as set out in the legislation applicable to an activity.
   - Entrepreneurs should be able to pursue the activity immediately after the appropriate agencies have been duly notified.
   - The entrepreneur's compliance with legislation should be verified by an appropriate government agency. In a limited number of cases, as specified in legislation, an agency could act to bar the entrepreneur from pursuing an activity if it is found to be hazardous to public health and safety (for example, catering or trade in foodstuffs) or the environment.

4. The content of laws governing permit procedures should be statutorily defined.

5. The enactment of permit-related laws should be within the exclusive remit of the Cabinet of Ministers.

6. The legal framework should clearly define the procedure for interaction among companies authorized to take part in the permit-issuance process, applicants and state agencies or local self-governance bodies.
Licensing Procedures Are Generally Well Regulated

Licensing legislation is fairly well structured. It regulates 11 distinct groups of licenses and related licensing procedures, which vary according to the group.

Although licensing procedures are generally well regulated, a considerable portion of respondents encountered problems in 2003, including the following: excessive number of documents (38%); long processing periods (24%); unclear requirements (21%); and variable procedures (21%).

Due to the particulars of the legislation applicable in each case, the complexity and cost of licensing procedures varied by type of license:

- Only 7% of respondents obtaining retail trade licenses for alcoholic beverages and tobacco rated the process as "very complex", while 32% of respondents seeking other types of licenses assigned this rating.
- Of respondents obtaining retail trade licenses for alcoholic beverages and tobacco, 52% found the costs burdensome, compared with 41% of those seeking other types of licenses.

License processing periods in 2003 tended to exceed the deadlines set out in law.

Chart 6.1 One in Five Respondents Obtained Licenses in 2003

<table>
<thead>
<tr>
<th>% of all respondents</th>
<th>% of respondents obtaining licenses in 2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Did Not Obtain 80%</td>
<td>20%</td>
</tr>
<tr>
<td>Obtained 20%</td>
<td>26%</td>
</tr>
</tbody>
</table>

1 Law of Ukraine No. 1775-III On Licensing Certain Lines of Business (1 June 2000) is the principal licensing-related law. As of 2003, it set out the legal framework for licensing 59 kinds of business activities. However, Article 2 provides that licenses for banking, financial services, foreign trade, broadcasting, energy generation and utilization of nuclear energy, education and intellectual property activities, production and circulation of ethanol, cognac and fruit spirits, alcoholic beverages and tobacco products, and telecommunication are to be governed by special laws.
In 2003, 20% of respondents obtained licenses. Most of these licenses fell into one of two groups: (1) sale of alcoholic beverages and tobacco products, and (2) construction, passenger and luggage transportation, manufacturing and trade in pesticides and agricultural chemicals, manufacturing and trade in medications, tourism, medical services, etc.

Excessive Number of Documents, Long Processing Periods, Unclear Requirements and Variable Procedures Identified As Key Problems for All Types of Licenses

The survey showed that the type of license required had little bearing on the difficulties encountered in seeking licenses.

**Chart 6.2** Problems Are Common to All Types of Licenses

<table>
<thead>
<tr>
<th>Problem</th>
<th>% of respondents obtaining licenses in 2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Excessive Number of Documents Required</td>
<td>38%</td>
</tr>
<tr>
<td>Long Processing Period</td>
<td>24%</td>
</tr>
<tr>
<td>Unclear Requirements</td>
<td>21%</td>
</tr>
<tr>
<td>Variable Licensing Procedures</td>
<td>21%</td>
</tr>
<tr>
<td>High Cost of Preparing Documents</td>
<td>13%</td>
</tr>
</tbody>
</table>

The problem mentioned by the greatest percentage of respondents (38%) was the need to prepare a large number of licensing documents. This might seem surprising, since the complete list of documents required is set out in legislation. However, licenses for tobacco products and alcoholic beverages are issued for one outlet, and a further set of licensing documents must be prepared for each additional outlet. Companies obtaining licenses under the law “On Licensing of Certain Lines of Business” must submit additional documents, as set out by the Cabinet of Ministers for each license.

Long processing periods were noted by 24% of respondents. This perception can be attributed to the fact that some licensing authorities failed to abide by the statutory period, and also to the tendency of some respondents to include the time needed to prepare the documents in their estimation of the processing period.

Unclear requirements were cited by 21% of respondents. A similar percentage mentioned variable procedures, which may be because of legislative changes introduced in 2003. The Law “On Licensing of Certain Lines of Business” was amended six times, the law “On State Regulation of Production and Circulation of Ethanol, Cognac and Fruit Spirits, Alcoholic Beverages and Tobacco Products” was amended once, the list of license-issuing bodies approved by the Cabinet of Ministers was changed eight times, and five amendments were made to the lists of additional licensing documents approved by the Cabinet of Ministers.
Licensing Costs Were Burdensome for Half of Respondents, Depending on License Group

Of respondents obtaining licenses in 2003, 61% regarded the cost as either “burdensome” or “excessive”. Like procedure complexity, responses with respect to costs varied by license group. Of respondents obtaining licenses for the sale of alcoholic beverages and tobacco products, 82% said the cost was “excessive”, while 54% of respondents seeking other types of licenses applied that rating to costs.

The difference can be explained by the variation in fees and payment procedures. The law “On Licensing of Certain Lines of Business” provides for a one-time fee when the license is issued, and is no more than 340 UAH (US$64) in most cases. At the same time, the fee for a wholesale license for alcoholic beverages or tobacco products must be paid annually and is 50,000 UAH (US$9,412). The annual retail license for alcoholic beverages costs 4,000 UAH (US$753) and the annual retail license for tobacco products costs 2,000 UAH (US$376). The license fee is paid for each retail outlet. There was a fee increase in mid-2003 on licenses for retail or wholesale trade in alcoholic beverages and tobacco products.

A considerable portion of respondents obtaining licenses under the law “On Licensing of Certain Lines of Business” nevertheless rated the cost as “burdensome” or “excessive”. This may be because of rather high cost of the preparatory stage (collection and preparation of documents, fees charged by state agencies for documents, etc.) and unofficial payments.
Like procedure complexity and costs, responses with respect to unofficial payments depended on the license group. Overall, 20% of respondents obtaining licenses made unofficial payments, but only 8% of those obtaining licenses for the sale of alcoholic beverages or tobacco products made such payments.

At the same time, between 8% and 34% (depending on license type) of respondents seeking licenses under the law “On Licensing of Certain Lines of Business” made unofficial payments.
License Processing Periods

By law, a license for the sale of alcoholic beverages and tobacco products must be either issued or refused within 10 days of the date the documents are submitted. Yet, more than 40% of the respondents affected noted that the ten-day deadline was rarely met. This result may be cause for concern, but is mitigated by the tendency of respondents seeking retail trade licenses for alcoholic beverages and tobacco products to include in the processing period the time needed to register with local tax authorities or local government bodies in rural areas.

For other licenses, the law “On Licensing of Certain Lines of Business” provides for the following deadlines for licensing procedures:

- ten working days to consider documents submitted for obtaining a license;
- three working days to mail the notification of the decision to the applicant; and
- three working days from the date a receipt for payment of the license fee is submitted to issue the license document.

Thus, by law, licenses in this group must be processed within 16 working days, excluding mailing time. Adding about four days for mailing, a 20-day processing period does not seem out of line.
Recommendations

1. Tighten the control over the compliance of license-issuing bodies with licensing procedures;

2. Create databases, accessible to entrepreneurs, containing complete information about license-issuing bodies, mandatory documents, licensing conditions, costs, etc; and

3. Specify the content and format of the additional documents required for certain types of licenses.\(^{11}\)

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\(^{11}\) Cabinet of Ministers Order No. 756 On the Adoption of the List of Documents to be Submitted with the Licensing Application for Specific Lines of Business (4 July 2001)
Standards Reform

Until 2001, Ukraine followed the former Soviet system of standards, which contained comprehensive mandatory standards for the manufacturing sector.

In order to adapt to EU and WTO requirements, the Laws of Ukraine On Conformity Assessment, On Standardization and On the Accreditation of Conformity Assessment Bodies were introduced in 2001. The provisions of these laws were to be harmonized with EU requirements in terms of technical standards. In 2003, however, a modular approach to standardization was put in place, wherein companies could select the system of standards under which they would operate, according to their needs and resources.

Harmonization with EU standards requires that the laws governing standards include regulations stipulating adherence to EU technical specifications. This has been only partially implemented. Currently, 39 products/processes are still subject to mandatory certification under the existing system.

To date, the regulations for ten products/processes include EU-based technical specifications. Five more are at the review stage. There was some progress in this area in 2003, but not yet sufficient for widespread introduction of new standardization procedures.

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1 State Committee for Technical Regulation and Consumer Policy
2 Cabinet of Ministers Order No. 1585 On the Adoption of Technical Regulation Conformity Assessment Modules and Requirements for Awarding a National Conformity Mark Used in Conformity Assessment Technical Regulations (7 October 2003)
3 State Committee for Standardization, Metrology and Certification Decree No. 498 The List of Products Subject to Mandatory Certification (30 August 2002)
4 State Committee for Technical Regulation and Consumer Policy
SMEs Were Not Actively Involved in the Development of Standards

Only one in five respondents was subject to standardization of products or processes. In general, standards apply mostly to manufacturing, construction and trade, the fastest-growing sectors of the Ukrainian economy.

As in other CIS countries, most respondents conformed to national ("GOSTU") and CIS ("GOST") standards.

Chart 7.1  Standardization Primarily Affected Manufacturing, Trade and Construction Companies

% of respondents with products/process subject to standardization

Chart 7.2  Most Respondents Operated Under Non-ISO-Compliant GOSTU and GOST Standards

% of respondents with products/processes subject to standardization
The chart shows that three quarters of respondents subject to standardization, in key economic sectors, operated under GOSTU/GOST standards that have not been harmonized with international standards. In general, this was because the relevant ISO-compliant regulations have not been introduced through legislation, rather than because of company preference. As of June 2004, just over 1,600 national standards (less than 17%) had been harmonized with European and international standards.¹

The slow pace of harmonization was not the only problem respondents cited with respect to standardization. Of the respondents subject to standardization, 60% noted difficulties related to the procedures. The problems most frequently cited are shown in the chart below.

<table>
<thead>
<tr>
<th>Problems with Standardization</th>
<th>% of respondents with products/processes subject to standardization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unclear Specifications</td>
<td>18</td>
</tr>
<tr>
<td>Technical Conditions Are Hard to Register in the Regions</td>
<td>18</td>
</tr>
<tr>
<td>Lack of Information on Updates to Standards</td>
<td>14</td>
</tr>
<tr>
<td>Outdated Specifications</td>
<td>14</td>
</tr>
<tr>
<td>High Cost of Upgrading to Standards</td>
<td>14</td>
</tr>
</tbody>
</table>

Standards have not kept pace with technological advances and international norms, and respondents often found the requirements difficult to understand. This view is shared by every seventh surveyed respondent.

Respondents also found it difficult to obtain information on the standardization process generally, and on current standards: One in seven respondents with products/processes subject to standardization noted the lack of information on updates to standards, and more than one in three found it difficult to obtain complete and accurate standardization information from state agencies.

<table>
<thead>
<tr>
<th>Difficulty in Obtaining Complete and Accurate Information on Standardization</th>
<th>% of respondents with products/processes subject to standardization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Easy</td>
<td>62</td>
</tr>
<tr>
<td>Difficult</td>
<td>38</td>
</tr>
</tbody>
</table>

The slow pace of harmonization with international standards, the outdated specifications of existing standards and the difficulties with the current process have prompted some companies to actively develop and register their own specifications.

Of respondents with products/processes subject to standardization, 18% had developed and registered standards for their own companies in 2003, illustrating that a sizeable proportion were dissatisfied with existing standards. Nevertheless, the overwhelming majority of the respondents affected (92%) did not actively seek change through expressing their views or making proposals. Thus, while Ukraine has continued to revise standards to harmonize with international norms, few SMEs (8%) have been involved in the process.

State agencies have not actively sought the participation of companies in the development of standards, but there is also a view among business associations and individual entrepreneurs that expressing their views is unlikely to result in change. The prevalence of unclear specifications and the scale of mandatory requirements were other reasons for their disinclination to participate in the reform process.

Standardization reform should not be limited to new legislation, but should also review and update all technical specifications and streamline related procedures. In addition, the reform process should be transparent and include the participation of individual companies and the business associations of the sectors affected in each case.

Mandatory Certification

Certification is mandatory for products and processes that might pose a threat to public health and safety. In general, goods are certified “safe” if they meet the specified minimum mandatory requirements.

Of the companies surveyed, 20% produced products or engaged in activities subject to certification in 2003. Of those, 65% obtained certification because it was mandatory, 23% underwent both mandatory and voluntary certifications and 12% obtained voluntary certification only.
Of the respondents obtaining mandatory certifications in 2003, 79% required one, 14% required two and 7% required three or more. Large and medium companies were most likely to require mandatory certifications.

**Chart 7.7**

Large and Medium Companies Were Most Likely to Require Mandatory Certifications

<table>
<thead>
<tr>
<th>Company Size</th>
<th>% of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large (251-1000)</td>
<td>56%</td>
</tr>
<tr>
<td>Medium (51-250)</td>
<td>37%</td>
</tr>
<tr>
<td>Small (11-50)</td>
<td>17%</td>
</tr>
<tr>
<td>Micro (1-10)</td>
<td>12%</td>
</tr>
</tbody>
</table>

Finished goods are the products most often certified in Ukraine. In general, certification requirements are related to safety issues. Of the companies undergoing certifications in 2003, 74% complied with the minimum mandatory requirements by obtaining certification of a product sample, a production run or a batch of the product. Meeting only the minimum requirements reduces the effort required on the part of the company, but experts believe that while this is efficient, it is not sufficiently effective in ensuring public safety.

**Chart 7.8**

Types of Mandatory Certifications Obtained

<table>
<thead>
<tr>
<th>Type</th>
<th>% of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Product Sample</td>
<td>22%</td>
</tr>
<tr>
<td>Batch</td>
<td>33%</td>
</tr>
<tr>
<td>Production Run</td>
<td>19%</td>
</tr>
<tr>
<td>Production Process</td>
<td>11%</td>
</tr>
<tr>
<td>Quality Control</td>
<td>15%</td>
</tr>
</tbody>
</table>

Red Tape and Lack of Information Were the Main Problems with Mandatory Certification

New laws have created a market for certification services. Prior to 2001, only the Ukraine State System for Goods Certification (“USSGC”) was authorized to grant certifications. Currently, various types of companies can offer certification services, and each sets fees and maintains certification registers at its discretion. These companies must be accredited, in accordance with international standards, by an independent accreditation authority. In Ukraine, it is the National Accreditation Agency of Ukraine (“NAAU”).
The survey showed that legislative reform and the emergence of the certification market have not succeeded in making certification easier for businesses.

Of respondents subject to mandatory certification, 72% reported difficulties during the process. The number of documents required, processing delays and lack of information were the problems most often cited.

### Chart 7.9
**Red Tape and Lack of Information Were the Main Problems with Mandatory Certification**

<table>
<thead>
<tr>
<th>Problem</th>
<th>% of Respondents Subject to Mandatory Certification in 2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Excessive Number of Documents</td>
<td>30%</td>
</tr>
<tr>
<td>Processing Delays</td>
<td>20%</td>
</tr>
<tr>
<td>Lack of Information</td>
<td>17%</td>
</tr>
<tr>
<td>Varying Procedures</td>
<td>17%</td>
</tr>
<tr>
<td>Complex Procedures, Unclear Requirements</td>
<td>16%</td>
</tr>
</tbody>
</table>

The time required for certification varies according to the testing procedure for the product or process. Nevertheless, since mandatory certification is a requirement of the state, state agencies have a responsibility to provide complete and accurate information about the process.

Of respondents subject to mandatory certification, 17% indicated that lack of information is one of the main problems with the process and 40% noted that such information was difficult to get from state agencies.

### Chart 7.10
**40% of Respondents Found It Difficult to Obtain Information on Mandatory Certification from State Agencies**

<table>
<thead>
<tr>
<th>Difficulty Level</th>
<th>% of Respondents Subject to Mandatory Certification in 2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Difficult</td>
<td>40%</td>
</tr>
<tr>
<td>Easy</td>
<td>60%</td>
</tr>
</tbody>
</table>

Respondents subject to mandatory certification spent an average of 25 working days and approximately 4,700 hryvnya (US$885) obtaining certifications in 2003. Of these, 60% regarded the cost as burdensome or unjustifiably high, and 21% said they made unofficial payments.

"Take the garment industry, for example... If I make suits, I pay for certifications for one set of fittings, one fabric, one lining. If I want to use a second fabric, I have to start the process all over again – and I need a product line of five or six models to remain competitive."

*Focus Group Participant*
The complexity of mandatory certification stems partly from the extensive list of goods subject to certification and partly from the fact that the rules are open to interpretation. The companies surveyed believed that these requirements lacked clarity and that successful certification often depended on their negotiating skills.

"Everything depends on the personality of the employee handling the certification and on their ability to establish contacts with certifying bodies. One employee could complete everything within a day and it might take another a week... ."*  
Focus Group Participant

Respondents did not always know whether their products were subject to mandatory certification. Products are listed by name and by two sets of codes (UCIEG and SCGS). In general, customs authorities use UCIEG, while certification bodies use SCGS and companies prefer to go by the name of the product. This results in confusion, with each party interpreting the need for certification differently.

**Mandatory Certification Requirements for Imported Goods Allow Varying Interpretation**

In the course of importing a product, a company looking for the name among the products requiring certification may conclude that certification is not required. Customs officials looking up the product by UCIEG code may reach a different conclusion and may refer the company to the Chamber of Commerce and Industry for a formal ruling. Even if the code (assigned by the manufacturer) indicates that certification is not required, the code may be changed by customs authorities. They have the final say in allocating UCIEG codes for imported goods.

Unfortunately, quite a few importers do not realize that they have to submit the testing protocols used for certification in the CIS country of origin in order to validate the certification in Ukraine - until it is too late and their goods are already going through customs.

**Voluntary Certification**

Approximately one-third of all certifications sought by respondents in 2003 were voluntary, carried out in order to enhance the competitiveness of their goods.

As with mandatory certification, voluntary certification mainly applies to finished goods. Four out of five companies opting for voluntary certification certified the properties of their goods seen as important to consumers.

<table>
<thead>
<tr>
<th>Chart 7.11</th>
<th>Types of Voluntary Certifications Obtained</th>
</tr>
</thead>
<tbody>
<tr>
<td>% of companies obtaining voluntary certifications in 2003</td>
<td></td>
</tr>
</tbody>
</table>

- Products: 57%
- Production Systems: 26%
- Quality Control Systems: 18%
Nearly half of respondents seeking voluntary certification had their production and quality control systems certified, but this represents less than 3% of all companies surveyed.

Voluntary certification to enhance the competitiveness of products is not prevalent in Ukraine. In other countries, it is of vital importance to the success of a business. In Ukraine, it is generally limited to companies that (a) operate in a competitive field; (b) have reached a certain threshold of development; (c) recognize the long-term advantages; and (d) are aware of advanced management techniques.

The survey results indicate that the most positive developments in the areas of standardization and certification have taken place at the legislative level. At the local level, entrepreneurs still find the procedures complex, lengthy and costly. Procedures and requirements, particularly in the statutorily regulated field of certification, should be reviewed for consistency, transparency and availability of complete and accurate information.

**Recommendations**

1. The State Committee for Consumer Policy and Standards should expedite the development and adoption of technical requirements in order to tighten the list of goods subject to mandatory certification.

2. Mandatory certifications should be reduced to a minimum and the requirements should focus on protecting public health and safety. Certification of quality standards should be voluntary rather than mandatory.

3. The State Committee for Consumer Policy and Standards should accelerate the pace of harmonization of standards through consultations with manufacturers and business sector associations.

4. The State Committee for Consumer Policy and Standards and other agencies involved in the mandatory certification process, particularly as it relates to imported goods, should review the procedures with a view to making them more explicit and transparent.
Three Out of Four Companies Identified Taxes As a Serious Obstacle to Business Development

Of the companies surveyed, 74% rated the taxation system as a "serious" or "very serious" obstacle to business development. A further 22% considered it a "minor" obstacle.

Of the companies surveyed, 74% considered the taxation system either a "serious" or a "very serious" obstacle to business development.

The tax-related issues considered most important were unstable tax legislation (74%), the excessive number of different taxes payable (73%) and frequently-changing reporting procedures (69%).

- There were 43 amendments to tax legislation in 2003.
- Only half of eligible respondents opted for the simplified, flat tax system, while the rest did not consider it an advantage.
- Respondents found the income tax, Value Added Tax (VAT) and mandatory social security contributions the most difficult payments to calculate and predict.
- The shadow economy continues to be a significant factor in Ukraine. Only 16% of respondents said they paid taxes in full. A further 20% underreported income by more than 20%.

These responses were consistent throughout most of the 23 regional capitals, and in Kyiv and Simferopol. The exceptions were Kharkiv, Poltava and Zhytomyr, where 90% of respondents expressed dissatisfaction with the current taxation system. The Ukrainian tax system is centralized, but there are regional administrative variables (such as VAT reimbursement, tax inspections, requirements for registration with tax authorities and reporting procedures) which account for this discrepancy.
Frequently-Changing Legislation, Reporting Procedures, and the Number of Different Taxes Were Identified As the Most Significant Problems

The companies surveyed considered frequent changes to tax legislation and the reporting procedures, and the excessive number of different taxes the most significant problems with taxation in 2003.

Chart 8.2 Changing Legislation Cited As Most Serious Taxation Problem in 2003
% of respondents

- Changing Tax Legislation: 74%
- Excessive Number of Taxes: 73%
- Changing Reporting Rules: 69%
- Encourages Shadow Economy: 56%
- Disadvantage Compared to Competitors: 54%
- Complexity of Tax Calculation: 53%
- Tax Inspections: 51%
- Obtaining Information from Tax Authorities: 47%

Complaints about instability of the tax legislation (74% respondents) were explained by introduction of many amendments and changes to various legislative acts that regulate taxation in Ukraine. In 2003, there were 43 amendments to tax legislation. Of these, 36 came into force immediately, contrary to standard procedure.¹

"Tax law is in a state of flux, and as soon as a new rule is introduced, entrepreneurs must file their taxes returns according to the new procedure... ."

Focus Group Participant

Amendments in 2003:

- 14 amendments to the Law of Ukraine No. 334/94BP On Taxation of Corporate Profits (28 December 1994)
- 11 amendments to the Law of Ukraine No. 168/97/BP On the Value Added Tax (3 April 1997)
- 6 amendments to the Law of Ukraine No. 1251-XII On the Taxation System (25 June 1991)
- 2 amendments to the Decree of the Cabinet of Ministers No. 56-93 On Local Taxes and Charges (20 May 1993)
- 4 amendments to the Law of Ukraine No. 400/97-BP On the Mandatory State Pension Insurance Deduction (26 June 1997)
- 1 amendment to the Law of Ukraine No. 2272-III On Tariffs for the Mandatory State Social Insurance for Work-Related Accidents and Occupational Disease which Resulted in Disability (22 February 2001)

¹ The Law of Ukraine No. 1251-XII On the Taxation System (25 June 1991) provides that amendments to laws related to benefits, taxes and tax payments are to be made no later than six months prior to the end of the fiscal year and are to come into force at the start of the next fiscal year. However, this does not apply to other aspects of taxation legislation, including Internal Regulations and registration and reporting.
Of the companies surveyed, 73% were concerned about the excessive number of different taxes payable. In 2003, respondents paid between six and eleven different taxes, depending on company size.

The survey showed that the number of different taxes and contributions paid depended on company size: the larger the company, the higher the number payable. This is not surprising given that 37% of respondents opted for the simplified taxation option available to small business, which is deemed payment of several taxes and other payments. It should be noted that some respondents may have included their social insurance contribution in the number of taxes paid.

Income taxes, VAT and social insurance contributions proved the most complex payments to calculate.

Respondents identified income tax (23%) and VAT (22%) as the most difficult to forecast, which is not surprising in light of frequent legislative amendments affecting these taxes.

Difficulties in calculating social insurance contributions arose from ambiguity in the basis for calculating these contributions.

"The complex procedure for calculating social insurance contributions causes the most difficulty... The amount payable is a percentage of a base amount, but the composition of that base amount is unclear – and is in fact the key difficulty."

Focus Group Participant
Only Half of the Companies Eligible Opted for the Simplified Taxation System

The Ukrainian tax system in 2003 comprised 25 national and 14 local taxes and other mandatory payments. Of these, 20 national and 14 local taxes and other mandatory payments applied to companies (see Chart 11, Annex 5). In addition, companies made mandatory contributions to social programs including the Fund for the Social Protection of the Disabled, the State Employment Promotion Fund, and the Social Security Fund.

Small companies have the option of paying a flat tax, which offers the advantage of eliminating tax calculations and reporting. (See Chart 10, Annex 5)

"Since our company now pays a flat tax, we experience no tax-related problems….I believe that this simplified taxation system is quite clearly defined. Companies switch to this system not only for financial advantage, but also for the system’s simplicity. Its simplicity is a great attraction."

Focus Group Participant

Nevertheless, the survey showed that far from all companies who might benefit from paying a flat tax opted to do so. Specifically, 75% of the companies surveyed were eligible to pay the flat tax, but only half of those had done so by the end of 2003 and only a further 13% planned to do so in the future.

Chart 8.5 Only Half of Eligible Companies Opted to Pay the Flat Tax in 2003

![Chart 8.5: Only Half of Eligible Companies Opted to Pay the Flat Tax in 2003]

- **Not Eligible**: 25% of respondents
- **Eligible**: 75% of respondents
- **Paid Flat Tax**: 50% of eligible respondents
- **Did Not Pay Flat Tax, But Plan To**: 13% of eligible respondents
- **Did Not Pay Flat Tax - Content with Standard System**: 34% of eligible respondents
- **Did Not Pay Flat Tax - Advantage Outweighed by Red Tape**: 3% of eligible respondents
The Chart above shows that only half of the respondents eligible chose the simplified, flat tax system. Interestingly, 34% of eligible respondents reported that they did not pay the flat tax because they were content with the standard system, a view no doubt based on comparative financial advantage. The profit margin for companies in the retail and wholesale trade sector is a relatively small percentage of revenue. For them, the flat tax of 6% plus VAT, or about 10% of revenue, presented no advantage because the tax could be higher than revenue. Manufacturers, whose profits generally range from 30% to 40% of revenue, tended to opt for paying the flat tax because it was less than they would have paid under the standard system.

“We will not derive any financial benefit from the flat tax system because of the VAT. It is better for us to stay with the standard system because we are in the retail business.”

Focus Group Participant

Shadow Economy Remains Significant

According to 56% of respondents, tax issues contribute to the continuing significance of the shadow economy in Ukraine. One such issue is the granting of tax exemptions on a basis perceived as unjustified. Based on GDP and the 20% VAT rate, the State Taxation Administration estimates that tax revenues would have been 50 billion hryvnias in 2003 if no tax exemptions had been granted. Actual tax revenue in 2003 was 33.2 billion hryvnias. Respondents also held the opinion that the tax rates encouraged underreporting of income. According the survey results, only 16% of respondents paid taxes in full, and 43% admitted underreported their income – almost half of them by more than 20%.

Chart 8.6 Only 16% of the Respondents Paid Taxes in Full in 2003

<table>
<thead>
<tr>
<th>Revenue Status</th>
<th>% of respondents</th>
<th>% of respondents who underreported revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reported All Revenue</td>
<td>16%</td>
<td>14%</td>
</tr>
<tr>
<td>Did Not Respond</td>
<td>41%</td>
<td>8%</td>
</tr>
<tr>
<td>Underreported Revenue</td>
<td>43%</td>
<td>7%</td>
</tr>
</tbody>
</table>

Underreported Revenue:
- Up to 10%
- 11 to 20%
- 21 to 30%
- 31 to 40%
- 41 to 50%
- 51 to 60%
- More than 60%
Recommendations

1. A Taxation Code should be adopted.

2. The granting of tax exemptions should be reviewed. All exemptions granted should be made public. Only appropriate levels of exemptions for invested funds should be granted.

3. Legislative amendments should conform to the Law of Ukraine No. 1251-XII On the Taxation System (25 June 1991), which provides that amendments to laws on benefits, taxes and tax payments are to be made at least six months prior to the end of the fiscal year and are to come into force at the start of the next fiscal year. Application of this provision should be expanded to include tax registration and reporting procedures, as well as Internal Regulations, which are not laws.

4. Review the system of contribution to state social programs with respect to the portions paid by employers and employees. Examine options for a private or company insurance plans to benefit employees.
Inspections in 2003 Were Many and Frequent, and Diverted Significant Company Resources

Respondents viewed inspections as a continuing hindrance to business development owing to their quantity, duration and consequences. In 2003, 94% of the companies surveyed underwent inspections, a percentage similar to the 2002 results. Companies were inspected an average of 10 times in 2003 (14 in 2002) over an average of 13 days (17 days in 2002).

In 2003, as in 2002, the tax authorities, fire safety authorities and the Sanitary-Epidemiological Service carried out the highest number of inspections.

Inspections were not significantly effective in preventing violations. Instead, they were perceived as a revenue-generating mechanism:

- One in three respondents was fined in 2003. The average total fines paid during the year was 1,920 hryvnyas (US$358).
- The costs resulting from inspections were viewed as burdensome or unjustifiably high by 55% of respondents.
- Respondents estimated that the cost of fines paid for violations was about the same as the cost of full compliance.

Companies in regions where salaries were lower were more likely to be subject to fines resulting from inspections.

Two-thirds of respondents believed that introducing new legislation to regulate inspections would be the most effective means of reducing their frequency.

Chart 9.1  Tax and Fire Safety Authorities Inspected More Than Half of Respondents in 2003

% of respondents inspected in 2003

<table>
<thead>
<tr>
<th>Agency</th>
<th>% of respondents inspected in 2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax Inspectorate</td>
<td>61%</td>
</tr>
<tr>
<td>Fire Safety Inspectorate</td>
<td>55%</td>
</tr>
<tr>
<td>Pension Fund</td>
<td>37%</td>
</tr>
<tr>
<td>Sanitary-Epidemiological Service</td>
<td>34%</td>
</tr>
<tr>
<td>Tax Police</td>
<td>21%</td>
</tr>
<tr>
<td>Employment Fund</td>
<td>21%</td>
</tr>
<tr>
<td>Social Security Fund</td>
<td>20%</td>
</tr>
<tr>
<td>Labor Safety Authorities</td>
<td>11%</td>
</tr>
<tr>
<td>Consumer Rights Directorate</td>
<td>16%</td>
</tr>
</tbody>
</table>
More than 30 agencies are authorized to inspect companies. Tax and fire safety authorities carried out the highest number of inspections. Each inspected more than half of the companies surveyed. The most time-consuming inspections were carried out by the tax authorities, the Fire Safety Inspectorate and the Sanitary-Epidemiological Service. In aggregate, these agencies inspected 38% of respondents in 2003.

**Chart 9.2**  
**Inspections by Tax Inspectorate, Fire Safety Inspectorate and Sanitary-Epidemiological Service Were the Most Time-Consuming in 2003**  
*average number and duration of inspections per company*

<table>
<thead>
<tr>
<th>Agency</th>
<th>Average Working Days of Inspection Per Company</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tax Inspectorate</td>
<td>1.9</td>
</tr>
<tr>
<td>Fire Safety Inspectorate</td>
<td>1.9</td>
</tr>
<tr>
<td>Tax Police</td>
<td>1.7</td>
</tr>
<tr>
<td>Consumer Rights Directorate</td>
<td>1.6</td>
</tr>
<tr>
<td>Sanitary-Epidemiological Service</td>
<td>1.4</td>
</tr>
<tr>
<td>Labor Safety Authorities</td>
<td>1.4</td>
</tr>
<tr>
<td>Pension Fund</td>
<td>1.2</td>
</tr>
<tr>
<td>Employment Fund</td>
<td>1.2</td>
</tr>
<tr>
<td>Social Security Fund</td>
<td>1.1</td>
</tr>
</tbody>
</table>

**Inspections Were Not Fully Effective in Preventing Violations**

The survey showed that most companies found the regulations of state inspectors easy to understand. The Chart shows the four agencies conducting the highest number of inspections in 2003. The results were similar for the other agencies. Fewer than 20% of respondents said that they did not understand the regulations of inspecting agencies.

**Chart 9.3**  
**Entrepreneurs Understood the Regulations of Inspecting Agencies**  
*% of respondents inspected by these agencies in 2003*

The Chart shows the four agencies conducting the highest number of inspections in 2003. The results were similar for the other agencies. Fewer than 20% of respondents said that they did not understand the regulations of inspecting agencies.

Although most respondents understood the regulations, about half of them found them difficult to meet. At the same time, most respondents estimated that the cost of penalties for violations was about the same as the cost of full compliance with regulations. The Chart below illustrates these points with respect to the agencies conducting the highest number of inspections.
The results were similar for the other inspecting agencies. The survey showed that respondents had no incentive to abide by the regulations and they chose to save their resources instead.

"Sometimes it is easier to pay a fine than to comply with all the rules and regulations of inspecting agencies. It consumes much less time and resources."

Focus Group Participant

Inspections often have negative consequences in addition to fines. Nevertheless, the majority of respondents did not believe that inspectors had acted improperly. Of the respondents fined in 2003, 55% did not appeal because they did not believe they had grounds to do so. (See below for further detail.)

The survey showed that companies often knowingly violated regulations because they found compliance difficult and costly. This calls into question the effectiveness as an enforcement mechanism of the extensive inspections carried out in Ukraine.

**Inspections Perceived As a Revenue-Generating Function**

Respondents believed that inspecting agencies see inspections as a means of generating revenue from fines.

"Inspectors plan for the amount of money to be raised in fines. Sometimes they come asking us to help them reach this projection. We usually strike a compromise. We agree to pay from 1% to 2% of our revenues to avoid a full inspection that might uncover violations punishable by much steeper fines."

Focus Group Participant

There appears to be a correlation between the frequency of inspections and salary level of the region: the higher the salaries, the lower the incidence of fines.
The frequency of inspections and the incidence of penalties also depended on the revenue goals of inspecting agencies.

“The budget of Ukraine includes a line for “receipts from fines and financial penalties.” In 2003, it was projected that Ukrainian citizens, including entrepreneurs, would commit violations attracting 283,800,000 hryvnias in fines. Inspecting agencies retain 30% of the fines and penalties collected and therefore have an interest in imposing fines.”

Company size is also a factor in the incidence of inspections, with larger companies attracting more inspections.
Larger operations generally have a greater potential impact on public health and safety and it is not surprising that larger companies attract more inspections. However, the significant number of small companies inspected in 2003 suggests that inspections were not commensurate with the need to mitigate potential risk to the public. This finding led to the recommendation herein that inspections be conducted based on risk assessment.

Almost all respondents were inspected in 2003, and three out of four experienced negative consequences resulting from the inspections.

Of the respondents inspected in 2003, 37% were at least fined as a consequence. They paid an average of 1,920 hryvnyas (US$358) in fines during the year. The 2002 average was 2,758 hryvnyas (US$520). More than a quarter of respondents inspected in 2003 made unofficial payments in the course of inspections.

**Inspection Legislation Is Needed to Protect Entrepreneurs**

Most of the companies surveyed asserted their legal rights with respect to inspections, for example by keeping an Inspections Registration Book or by filing appeals.

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2 The Inspections Registration Book was introduced by Decree of the President of Ukraine No. 817/98 On Certain Measures to Deregulate Entrepreneurial Activities (23 July 1998). It was intended to regulate the frequency of inspections of SMEs.
In 2003, 71% of companies surveyed used Inspections Registration Books. Of those, 88% noted that inspectors always or nearly always filled it out for scheduled inspections, and 76% said that this was so for unscheduled inspections. 

The Inspections Registration Book is a protection for entrepreneurs, but it does not limit the number of inspections. Moreover, in some agencies, inspectors cannot be held accountable for their actions.

Inspectors of the following state agencies face punishment for illegal actions in the course of inspections: customs authorities, the Control and Revision Directorate and Police, the Temporary Disability and Accident Insurance Funds, the Inspectorate for Quality Control of Medications, and the State Inspectorate for Securities. No such accountability exists for other agencies, including the tax authorities, the fire safety authorities and the Sanitary-Epidemiological Service.

Only one in three respondents who believed they had grounds to appeal sanctions resulting from inspections actually filed appeals.
Although relatively few entrepreneurs appealed the decisions of inspecting agencies, appeals can succeed.

"The past few years have seen some positive developments in appeals of the decisions of inspecting agencies. I have represented entrepreneurs in court and can say that rulings are in favor of business people more and more often."

"Once I even won an appeal against a fine. I knew that I was right and persevered. A lot depends on your lawyer. Most people, however, shy away from disputing the decisions of inspecting agencies and are not used to arguing with the State."

*Focus Group Participants*

Large companies were more likely to appeal the decisions of inspecting agencies.

**Chart 9.10 Large Companies Appealed Sanctions More Often**

<table>
<thead>
<tr>
<th>Category</th>
<th>Did Not Appeal</th>
<th>Appealed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large (251-1000 employees)</td>
<td>37%</td>
<td>63%</td>
</tr>
<tr>
<td>Medium (51-250 employees)</td>
<td>50%</td>
<td>50%</td>
</tr>
<tr>
<td>Small (11-50 employees)</td>
<td>63%</td>
<td>37%</td>
</tr>
<tr>
<td>Micro (1-10 employees)</td>
<td>69%</td>
<td>31%</td>
</tr>
</tbody>
</table>

Inspections are governed by the Decree of the President of Ukraine No. 817/98 On Certain Measures to Deregulate Entrepreneurial Activities (23 July 1998). Section 8 of the Decree provides that inspecting agencies may adopt internal regulations for inspections, in agreement with the State Committee for Regulatory Policy and Entrepreneurship. Only two or three such documents have been introduced to date.

"In contrast to many western countries, inspecting agencies are unlikely to work in partnership with the business community in Ukraine in the near future. There are several reasons for this, the most important being prevailing attitudes. The public agency is considered to be, a priori, in a position of power, whereas the entrepreneur is viewed as a supplicant, regardless of the law. This outlook is reinforced by an inconsistent legal framework, where ambiguity allows agencies to choose the law by which they operate. They can then interpret and implement it at their discretion."  

*"Protection from Almightiness," Komp&nyon, 27/2004 (387)*

Inspection procedures are not regulated by a single, comprehensive law applicable to all inspecting agencies. As a result, procedures lack transparency and vary at the national and regional levels. In addition, there is overlap in the inspection functions of the various inspecting agencies.
Out of a variety of options, two-thirds of entrepreneurs rated legislation regulating inspections the most effective way to reduce the number of inspections.

"Inspection procedures should be made more systematic, and streamlined at the legislative level. It is evident that the functions of some agencies overlap."

Inspecting Agency Official

More than 30% of the surveyed enterprises believe that switching to the simplified taxation system can help reduce the number of inspections.

Focus group participants consider business associations to be capable of influencing the situation provided they participate more actively in representing enterprises interests and developing business promoting laws.

Recommendations

1. Incorporate uniform requirements into legislation governing inspections.
2. Mandate that all agency regulations covering inspection procedures be approved by the Cabinet of Ministers.
3. Review the standards and regulations of inspecting agencies to improve clarity and eliminate redundancy. Standards should then be adopted by parliament.
4. Correlate inspection policy and priorities to a system of assessing the risk to public health and safety of the business activity inspected.
5. Develop and introduce a uniform operating procedure for inspecting agencies that specifies the rights and responsibilities of inspectors, supervisors and entrepreneurs.
6. Itemize the specific inspection activities to be carried out by each inspecting agency, thus ensuring that inspections are appropriately limited in scope and that individual inspectors/agencies do not overstep their authority.
7. Consider eliminating the practice of remitting a percentage of fines collected to the inspecting agency imposing the fines. (This would be in line with general practice in Europe.) Projected revenue from fines should not be included in the annual state budget.
Two thirds of the companies surveyed invested new funds in their businesses in 2003. The majority of them (71%) relied exclusively on personal funds and 10% raised funds through external sources. The rest raised funds from a combination of personal and external sources.

**Chart 10.1  External Sources Are Seldom the Primary Financing Method**

- **Personal Funds**: 46%
- **Banks**: 25%
- **Partners/Investors**: 10%
- **Interest-Free Loans**: 3%
- **Non-Bank Financial Institutions**: 2%
- **Leasing**: 2%
- **State Foundations**: 1%

*Interest-Free Loans – amounts given to enterprises for their use according to agreements, which do not envisage interest payments or any other compensations for their usage*

It is evident that personal funds are currently the primary source of financing. This is likely to change as financial markets in Ukraine develop. However, the development of these markets depends on the ability of financial institutions and other investors to recover their funds, which in turn hinges on the enforcement of property rights in the country. The predominance of using personal funds for business financing is also a function of the prevalence of micro and small businesses, most of which rely chiefly on personal funds.
Banks Are the Most Prevalent Source of External Funds, and the Percentage of Companies Securing Bank Financing Increased in 2003

Although only 25% of the companies injecting new funds into their businesses in 2003 applied for bank loans, banks remained the most common providers of external financing. Most of the companies applying for bank loans in 2003 obtained the financing (79%), a 9% increase in the success rate over 2002.

Micro and Small Companies Are Financed Chiefly with Personal Funds

<table>
<thead>
<tr>
<th>Company Size</th>
<th>2003</th>
<th>2002</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro (1-10 employees)</td>
<td>77%</td>
<td>15%</td>
</tr>
<tr>
<td>Small (11-50 employees)</td>
<td>66%</td>
<td>26%</td>
</tr>
<tr>
<td>Medium (51-250 employees)</td>
<td>53%</td>
<td>34%</td>
</tr>
<tr>
<td>Large (251-1000 employees)</td>
<td>32%</td>
<td>13%</td>
</tr>
</tbody>
</table>

Increased Success Rate in Securing Bank Loans

<table>
<thead>
<tr>
<th>Company Size</th>
<th>2003</th>
<th>2002</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large (251-1000 employees)</td>
<td>97%</td>
<td>24%</td>
</tr>
<tr>
<td>Medium (51-250 employees)</td>
<td>90%</td>
<td>33%</td>
</tr>
<tr>
<td>Small (11-50 employees)</td>
<td>90%</td>
<td>33%</td>
</tr>
<tr>
<td>Micro (1-10 employees)</td>
<td>73%</td>
<td>17%</td>
</tr>
</tbody>
</table>

Small businesses experienced the greatest increase in successful loan applications, from 66% in 2002 to 92% in 2003. The smallest increase was reported by micro companies. This can be attributed to the following factors:

- Assigning a member of the staff to the process of securing a bank loan is more difficult for micro companies. The time commitment was cited as an obstacle by a greater proportion of micro companies compared with larger companies.
- Micro companies often have fewer assets (cash or fixed assets) to pledge as security.
- Micro companies tend to be younger, since companies tend to expand production over time or go out of business. Micro companies are therefore less likely to have a credit history.
"Banks are interested in getting their loans repaid and thus pay close attention to the company’s reputation and its track record in business. If a company has been operating for more than two to three years, it stands a better chance of obtaining a loan. Banks do not have a great deal of confidence in micro companies, as the staying power of these companies is uncertain and there is no guarantee that they will be able to stay in business and repay the loans... A bank usually requires funds to be deposited with the bank as security and micro-businesses are sometimes unable to fulfill this requirement..."

Focus Group Participant

Although Entrepreneurs Expressed Less Dissatisfaction with Interest Rates, Rates Remained High

The reduction in interest rates in 2003 altered the perception of this factor among the companies surveyed. The percentage of respondents citing high interest rates as a reason for not seeking bank financing declined by nearly half – from 68% in 2002 to 35% in 2003.

The average real interest rate declined from 20% in 2002 to 10% in 2003. The interest rate on foreign currency loans remained unchanged at 12%; therefore, the trend was driven by the drop in interest rates on loans in hryvnya, from 25% in 2002 to 18% in 2003, and by inflation. (Consumer prices rose by 1% in 2002 and 5% in 2003, and wholesale prices rose by 3% in 2002 and 8% in 2003.)

Not surprisingly, medium and large companies expressed a higher degree of dissatisfaction with interest rates. They are more likely than smaller companies to apply for bank financing and are thus more likely to be affected by interest rates.

The limited demand for loans (according to the National Bank of Ukraine, the total value of loans issued in hryvnya was lower than total deposits) seems to indicate that bank financing remains beyond the means of many Ukrainian companies.
Despite a Slight Shift to Longer-Term Financing, Loan Terms of Five Years or Longer Remain Atypical

As a percentage of all loans, the survey revealed a move in the direction of long-term (three to five years) financing, increasing from 3% in 2002 to 8% in 2003.

![Chart 10.5: Loan Terms Were Longer in 2003](image)

Nevertheless, it would be wrong to conclude that banks have become a viable source of long-term financing for Ukrainian companies. The survey showed that the percentage of loans with terms of more than five years remained negligible, accounting for less than 1% of bank loans.

The Non-Bank Financial Institution Market Remains Underdeveloped

Although most of the companies surveyed did not rely on external financing, banks remained the most common source of funds for those that did. The survey revealed that only about 2% of respondents had borrowed from non-bank financial institutions. Respondents cited reasons similar to those mentioned for not seeking bank financing, including:

Financing, compared to investing personal funds, reduced profits.

The requirement to deposit cash as security was viewed as a risk by both companies and lenders. Although the risks are decreasing, inflation, currency depreciation, and changes in legislation and economic policy were still seen as having the potential to affect the value of the security.

The funds from some non-bank lenders cannot be deposited in banks owing to uncertain provenance.

Apart from the difficulties encountered by all financial institutions in attracting resources, non-bank financial institutions, by definition, have the additional challenge of not being authorized to accept deposits. The funds invested in these institutions are less accessible than deposits.

The fact that (71%) of respondents relied exclusively on personal resources for financing their businesses suggests that there is a great deal of potential demand for financial services. However, realizing this potential requires that the level of risk be reduced, that more companies participate in the mainstream economy, and that financial institutions enhance their ability to attract resources.

---

1. Non-bank financial institutions provide financial services but do not have the status of a bank as defined by law. Their activities are governed by applicable legislation.
Although Leasing Companies Are Currently Underutilized, Leasing Demand Has the Potential to Triple in the Next Two or Three Years

Only 4% of respondents planning to acquire equipment in 2003 planned to do so through leasing, although 34% reported the need for new equipment during the year. Of those who had chosen leasing, three out of four successfully acquired leased equipment.

Although the incidence of leasing rose marginally over 2002, it remained a rarely-used financing option in Ukraine in 2003. The companies surveyed chiefly ascribed this to insufficient supply of leasing services, as well as to restrictive eligibility requirements and the narrow range of equipment available to be leased.

“Equipment of one or other companies is being promoted. I would like to buy equipment of this company, however, I can’t. You have to purchase only from this one … There is no partnership. For example, when I was going to buy a car, I was even told from what company to buy.”

Focus Group Participant

For the sake of comparison, leasing accounts for 15% to 30% of all investments in Europe. The survey showed that the demand for leasing has the potential to reach a similar level in Ukraine. The demand will not be fed by an increased need to acquire new equipment, but rather by the increasing number of companies opting for leasing to finance the equipment they need. In the next two to three years, the percentage of companies buying new equipment is expected to remain stable at 34%. Further acquisitions by companies that acquired equipment in 2003 will account for 59% of this. As mentioned, only 4% of companies planning to buy new equipment intended to apply for lease financing in 2003. This figure is expected to rise to 13% between 2004 and 2006.

The Ukrainian leasing market in 2003 was dominated by local banks, attracting 46% of respondents seeking lease financing. Domestic leasing companies were second at 40%. Foreign leasing companies accounted for 16%. Ukrainian leasing companies led the way in terms of number of leases written.

The preference for Ukrainian leasing companies can be explained by the more favorable terms offered by the Ukrainian companies: lower down payment, no payments in advance, marketing based on personal connections and a more flexible approach. Two out of three respondents who applied to Ukrainian leasing companies obtained the financing requested, while one out of two who applied to banks were successful and one out of three who applied to foreign leasing companies secured financing.

Banks provide customers with the advantages of ease of access and lower interest rates in comparison with other providers of lease financing. However, they are less favorable in terms of other considerations, including collateral requirements, payments in advance and purchasing imported equipment for hryvnias.

Foreign leasing companies account for a small share of the market despite their attractive interest rates and despite offering more opportunities to purchase imported equipment for hryvnias. This is primarily because of their more restrictive eligibility requirements, which translate into more applications declined. The majority of respondents who approached foreign leasing companies in 2003 were turned down. With respect to other preference factors, foreign leasing companies were seen as falling between Ukrainian leasing companies and banks.

Since respondents identified lower interest rates and the opportunity to acquire imported equipment for hryvnias as two of the key factors in selecting a leasing company, foreign companies could play a significant role as the leasing market develops.

Based on the survey, the leasing market in Ukraine is expected to range from US$300 to $500 million per year. Micro, small and medium companies will account for greatest number of lease transactions.
"Foreign leasing companies impose excessively restrictive terms, far more restrictive than banks, and offer only imported equipment."

Focus Group Participant

**Chart 10.6** Small and Medium Companies Will be the Major Market for Leasing Services

% of respondents planning to acquire equipment through leasing

<table>
<thead>
<tr>
<th>%</th>
<th>Micro (1-10 employees)</th>
<th>Small (11-50 employees)</th>
<th>Medium (51-250 employees)</th>
<th>Large (251-1000 employees)</th>
</tr>
</thead>
<tbody>
<tr>
<td>36%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>32%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>21%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>11%</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Recommendations**

1. The National Bank of Ukraine should develop the stability of the banking sector, for example by encouraging improved corporate governance in the banking field.

2. The government should institute measures to create sources of long-term financing, which would in turn reduce interest rates. Such measures could include encouraging the development of the securities market and implementing pension system reform.

3. A program should be established to raise the awareness of entrepreneurs with respect to the uses and advantages of external sources of funds and the mechanisms of securing bank loans, non-bank financing and lease financing.

4. Legislation stimulating development of leasing should be adopted. Quick tax depreciation, lower custom duties, improved mechanisms of returning a leased object in case of insolvency will make leasing more attractive as an asset renewal mechanism.
Only 6% of the companies surveyed exported goods in 2003. A further 3% planned to export but did not.

Apart from tariffs, exports in Ukraine are subject to further controls, including sanitary and customs controls, licensing and certification of exported goods, and deadlines on the repatriation of export earnings. Four out of ten respondents viewed these controls as an obstacle to exporting.

Of the respondents exporting goods, 54% reported difficulty in obtaining reimbursement for VAT. Since only half of successful litigants obtain full reimbursement of VAT, most exporters did not pursue reimbursement in court.

Export capability is limited by market factors. Of the exporting respondents, 52% found it difficult to compete in foreign markets.

More respondents favored Ukraine’s membership in the Common Economic Zone (CEZ) over membership in the World Trade Organization (WTO).

Of the companies surveyed, 6% exported their goods in 2003. A further 3% planned to export but did not. Of the companies that did export, seven out of ten exported to countries of CIS. One in three exported to Western Europe and one in fifteen exported to Asia.

More Than Half of Exporters Viewed Export Activities As Complex

Of the exporting respondents, 61% viewed the process as either “complex” or “very complex”. An even larger portion of those who intended to export in the future shared this viewpoint (83%), which raises the issue of complexity as a potential hindrance to further development of export-oriented companies in Ukraine.

Chart 11.1 Those Who Never Exported this Process Appears to be More Complex

Non-tariff controls are economic and administrative measures aimed at regulating foreign trade and include quotas, customs and sanitary control procedures.
The survey asked respondents why they regarded export procedures as complex and which factors contributed to that opinion. Their responses may be considered in two categories: compliance with non-tariff regulations and commercial impediments.

**Foreign and Domestic Export Controls**

The survey showed that the antidumping measures imposed on Ukrainian goods affected 43% of exporters surveyed. One in three respondents currently exporting or planning to export regarded the quotas of importing countries as a barrier.

Ukrainian exporters are subject to foreign non-tariff controls, but the respondents viewed domestic non-tariff controls as more significant.

Domestic customs controls were viewed as a barrier to exports by 56% of exporters.

Other controls cited as hindrances included licensing (36%), certification of goods (34%) and deadlines on the repatriation of foreign currency income from exports (44%).

Many of the exporters surveyed were of the opinion that current processes did not support an export-friendly business environment.

**Chart 11.2** A Large Number of Documents, Frequent Changes and Lengthy Procedures Are the Main Barriers to an Export-Friendly Business Environment

% of exporters surveyed

<table>
<thead>
<tr>
<th>Barriers</th>
<th>Very Serious Obstacle</th>
<th>Serious Obstacle</th>
<th>Minor Obstacle</th>
<th>Not an Obstacle</th>
</tr>
</thead>
<tbody>
<tr>
<td>Excessive Documentation</td>
<td>21%</td>
<td>43%</td>
<td>31%</td>
<td>5%</td>
</tr>
<tr>
<td>Frequently-Changing Procedures</td>
<td>23%</td>
<td>40%</td>
<td>32%</td>
<td>5%</td>
</tr>
<tr>
<td>Lengthy Procedures</td>
<td>12%</td>
<td>46%</td>
<td>34%</td>
<td>7%</td>
</tr>
<tr>
<td>Complex Procedures/ Unclear Requirements</td>
<td>8%</td>
<td>46%</td>
<td>37%</td>
<td>9%</td>
</tr>
<tr>
<td>Unofficial Payments</td>
<td>14%</td>
<td>30%</td>
<td>41%</td>
<td>15%</td>
</tr>
<tr>
<td>Inaccessibility/ Lack of Information</td>
<td>2%</td>
<td>13%</td>
<td>49%</td>
<td>17%</td>
</tr>
</tbody>
</table>
In 2003 Many Exporters Experienced Difficulty with VAT Reimbursement, but Did Not Consider Legal Action an Effective Solution

Difficulties with VAT reimbursement affected half of the exporters surveyed in 2003.

On average, the exporters surveyed recovered a little more than a half (53%) of the VAT paid. Those who reported no problems with VAT reimbursement recovered an average of 64% of the amount paid, while the rest recovered about 44%.

Most respondents (87%) who cited difficulties with VAT reimbursement did not consider legal action an effective solution.

In half of the cases where exporters were the successful litigants, they were nevertheless unable to obtain full reimbursement. The difficulty seemed to lie in the enforcement of judgments in these cases.

Consequently, many exporters hired intermediaries to recover the VAT owed. Only 22% of respondents said that they had never used an intermediary for this purpose.

Intermediary fees are about one third (31%) of the amount of VAT recovered.

Although the respondents who indicated no difficulty with VAT reimbursement recovered a larger portion of their VAT reimbursement (64%) than those using intermediaries (51%), the survey showed that many exporters were unable to recover VAT on their own.

Regardless of whether exporters hired intermediaries or pursued VAT reimbursement themselves, a portion of the reimbursable sum went unpaid.

With an intermediary, the average shortfall was 18%. Without an intermediary, it was 36%.
Most of the exporters surveyed believed that the tax, treasury and customs authorities were responsible for the delays in VAT reimbursement.

Chart 11.5  
**Tax Authorities Is the Main Cause for VAT Reimbursement Delays**

- **Tax Authorities**: 55%
- **Treasury Authorities**: 16%
- **Customs Authorities**: 11%
- **Partner Company**: 3%
- **Respondent’s Company**: 2%
Although the companies surveyed viewed export-related administrative processes and non-tariff controls as a deterrent to exporting, they considered commercial factors a more significant impediment. More than half of the exporters surveyed cited the difficulty of competing in foreign markets as an inhibiting factor, regardless of the market in question. Another commercial factor identified as an impediment to exporting was the high cost of market research, marketing, and advertising in foreign markets.

More exporters considered commercial factors (notably, competing in foreign markets) as the most significant barrier to export capability, compared with those who cited tariffs and non-tariff restrictions as the major impediments. It is not surprising therefore that more of the exporters surveyed held the opinion that Ukraine’s membership in the CEZ would benefit their businesses more than membership in the WTO.

**Exporters Favor Ukraine’s Membership in CEZ More Than WTO**

Most exporters surveyed supported Ukraine’s participation in trade and economic alliances. According to 33% of respondents, Ukraine should join both the CEZ and the WTO. A further 25% did not believe their businesses would be affected by membership in either. Only 2% were against Ukraine’s membership in either organization.

*Over the last ten years, Ukraine’s trade with Russia, Belarus and Kazakhstan combined has fallen from 53% to 30% of total trade, mostly owing to Ukraine’s increasing trade with other countries. Most of these new trading partners are WTO members, and interest in WTO membership is growing. Ukraine applied for WTO membership in 1993, and signed agreements on market access protocols for goods and services with 20 countries by the end of 2003. In applying for WTO membership, Ukraine committed to not changing its foreign trade policy. Nevertheless, along with Belarus, Kazakhstan and Russia, Ukraine has since signed an agreement on the creation of the Common Economic Zone.*
The survey showed that eastward integration through membership in the CEZ is supported by more exporters, with 60% believing that CEZ membership will benefit their businesses. WTO membership was favored by 44% of respondents. Exporters said that they focus on CIS markets because they were more able to compete in those markets than in western markets, and because customs duties are lower in CIS countries. Many cited the lack of resources to survey foreign markets and promote their goods abroad, and believed that they would generally have more difficulty in entering western markets.

**Recommendations**

1. Reduce domestic non-tariff restrictions on exports. Create and implement a plan for the gradual simplification of export-related procedures, including a reduction in the number of required documents.

2. Motivate the tax, customs and treasury authorities to resolve the problem of VAT reimbursement delays.

3. Consider the possibility of ensuring that Ukrainian exporters have access to databases containing information about importers.

4. Intensify the efforts of trade departments at Ukrainian embassies. Export growth should be considered a key indicator of their performance.
Overview

<table>
<thead>
<tr>
<th>Objective:</th>
<th>Assessment of the current business environment in Ukraine based on the 2003 operational results achieved by the companies surveyed.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reach:</td>
<td>Companies in the regional capitals of Ukraine, as well as in Kyiv and Simferopol.</td>
</tr>
<tr>
<td>Method:</td>
<td>Survey of entrepreneurs at their workplaces using structured face-to-face interviews, targeted focus group sessions, as well as personal interviews with representatives of state agencies.</td>
</tr>
<tr>
<td>Sample:</td>
<td>Multi-stage, weighted by quotas for region, company size and business sector in order to be representative of SMEs throughout Ukraine; thereafter, random selection of 2,500 participants. 300 companies-exporters were surveyed additionally.</td>
</tr>
</tbody>
</table>

Background

Preliminary data collection was conducted between 26 April and 9 June 2004 by an independent market research company with extensive experience in implementing similar surveys in Ukraine and elsewhere.

Respondents were interviewed using a questionnaire consisting of 155 complex questions with respect to regulatory processes and barriers encountered by entrepreneurs in their day-to-day operations. The questionnaire consisted of three sections: the main questionnaire (105 questions), a section for company management (43 questions) and a section for the company accountant (7 questions).

The preliminary results were tested in targeted focus group sessions in which entrepreneurs and experts commented on the reliability of the survey results. This report incorporates their views. In addition, face-to-face interviews were conducted with officials from state agencies directly involved in regulating entrepreneurial activities. These data are also included in this Report.

Sample

The sample was designed to be representative of SMEs in Ukraine.

The survey polled 2,500 SME executives from the 23 regional capitals of Ukraine, as well as Kyiv and Simferopol. All segments of the private sector in Ukraine, except agriculture, were represented. Sample selection was carried out based on:

- Company size (micro-, small, medium, large),
- Business sector,
- Company location (regional centers, Kyiv and Simferopol).

The sample pool was based on data effective 1 January 2004 furnished by the State Statistics Committee of Ukraine. The sample was weighted to normalize the statistics and to ensure adequate representation by city, business sector and company size category, thus providing a more accurate picture of the current business environment. The methodology was strictly observed at all stages of the survey, and therefore the survey results can be extrapolated to the general business population. The sampling error was 2%.

The majority of the survey participants were company managers, who were fully aware of the environment in which their companies operated. They were either directly involved in obtaining registrations, permits, licenses and certificates or they supervised the employees who were responsible. In addition, they were the decision-makers with respect to company finance and product export matters, informed with respect to the inspections carried out by regulatory agencies and well versed in taxation issues.

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*The obtained survey results are representative. The results were used for analysis of barriers to exporting business of Ukrainian enterprises.*
The sample reflects the SME sector in Ukraine, according to the internationally-accepted definition of SMEs. The State Statistics Committee defines business size differently, but these differences were taken in account and the largest companies were excluded in order to allow meaningful comparisons.¹

¹ The definitions of the categories conform to internationally-accepted standards, not the definitions in the Economic Code of Ukraine of 1 January 2004.

**Chart 12.1  Respondents by Management Level**

<table>
<thead>
<tr>
<th>Position</th>
<th>% of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Head of Unit/Chief Specialist</td>
<td>1%</td>
</tr>
<tr>
<td>Chief Accountant</td>
<td>3%</td>
</tr>
<tr>
<td>Commercial Director</td>
<td>3%</td>
</tr>
<tr>
<td>Chief Executive Officer</td>
<td>3%</td>
</tr>
<tr>
<td>Chief Financial Officer</td>
<td>2%</td>
</tr>
<tr>
<td>Deputy Director</td>
<td>3%</td>
</tr>
<tr>
<td>Director, Owner, Chairman of the Board</td>
<td>13%</td>
</tr>
</tbody>
</table>

**Chart 12.2  Respondents by Firm Size**

<table>
<thead>
<tr>
<th>Firm Size</th>
<th>% of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Micro (1-10 employees)</td>
<td>9%</td>
</tr>
<tr>
<td>Small (11-50 employees)</td>
<td>25%</td>
</tr>
<tr>
<td>Medium (51-250 employees)</td>
<td>30%</td>
</tr>
<tr>
<td>Large (251-1000 employees)</td>
<td>36%</td>
</tr>
</tbody>
</table>

**Chart 12.3  Sectors Included in the Survey**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Business Activity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>mining, machinery, materials processing, food processing, energy, chemicals, petrochemicals, pulp and paper, wood processing, communications</td>
</tr>
<tr>
<td>Construction</td>
<td>construction services</td>
</tr>
<tr>
<td>Wholesale/Retail Trade</td>
<td>retail and wholesale trade outlets</td>
</tr>
<tr>
<td>Food and Beverage Services</td>
<td>restaurants, bars, cafes, canteens</td>
</tr>
<tr>
<td>Transportation</td>
<td>freight and passenger transportation services</td>
</tr>
<tr>
<td>Financial Services</td>
<td>commercial banks, insurance companies, pension funds</td>
</tr>
<tr>
<td>Other Services</td>
<td>hotels, real estate agencies, publishers, telecommunications services, miscellaneous services</td>
</tr>
</tbody>
</table>
Companies were assigned to a sector based on their core business, as follows:

The survey sample did not include state-owned companies or those funded in whole or in part by the state (schools, municipal educational institutions, healthcare institutions, etc.) The largest category of participant consisted of limited liability companies. The rest were private companies, joint stock companies and enterprises of other forms.
### Chart 12.6  Respondents by Region

<table>
<thead>
<tr>
<th>City</th>
<th>Participants</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vinnytsia</td>
<td>77</td>
</tr>
<tr>
<td>Dnipropetrovsk</td>
<td>114</td>
</tr>
<tr>
<td>Donetsk</td>
<td>111</td>
</tr>
<tr>
<td>Zhytomyr</td>
<td>78</td>
</tr>
<tr>
<td>Zaporizhia</td>
<td>76</td>
</tr>
<tr>
<td>Ivano-Frankivsk</td>
<td>77</td>
</tr>
<tr>
<td>Kirovohrad</td>
<td>79</td>
</tr>
<tr>
<td>Kyiv</td>
<td>440</td>
</tr>
<tr>
<td>Lugansk</td>
<td>79</td>
</tr>
<tr>
<td>Lutsk</td>
<td>78</td>
</tr>
<tr>
<td>Lviv</td>
<td>90</td>
</tr>
<tr>
<td>Mykolaiv</td>
<td>80</td>
</tr>
<tr>
<td>Odesa</td>
<td>106</td>
</tr>
<tr>
<td>Poltava</td>
<td>79</td>
</tr>
<tr>
<td>Rivne</td>
<td>78</td>
</tr>
<tr>
<td>Simferopol</td>
<td>81</td>
</tr>
<tr>
<td>Sumy</td>
<td>79</td>
</tr>
<tr>
<td>Ternopil</td>
<td>76</td>
</tr>
<tr>
<td>Uzhhorod</td>
<td>79</td>
</tr>
<tr>
<td>Kharkiv</td>
<td>153</td>
</tr>
<tr>
<td>Kherson</td>
<td>78</td>
</tr>
<tr>
<td>Khmelnytsky</td>
<td>77</td>
</tr>
<tr>
<td>Cherkasy</td>
<td>79</td>
</tr>
<tr>
<td>Chernivtsi</td>
<td>78</td>
</tr>
<tr>
<td>Chernihiv</td>
<td>78</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>2500</strong></td>
</tr>
</tbody>
</table>

**Sampling error is 2%.**

### Chart 12.7  Respondents by Legal Status

- **Limited Liability Company**: 51%
- **Private Enterprise**: 31%
- **Joint Stock Company**: 8%
- **Other**: 10%

### Chart 12.8  Respondents by Gender

- **Male**: 68%
- **Female**: 32%
Annex 1

Registration

Until 1 July 2004, the registration process had remained largely unchanged for seven years. It was regulated by the Law of Ukraine On Entrepreneurship and the Cabinet of Ministers Order No. 740 (25 August 1998).

Each new company had to obtain a state registration certificate, a USRCOU code and a permit for the production of a stamp, register with four state social agencies and the tax inspectorate, and follow further procedures to open a bank account.

The standard registration process\(^1\) and the one-stop shop model process as it existed prior to the enactment of the Law of Ukraine On State Registration of Legal Entities and Individual Entrepreneurs are set out in Charts 1 and Charts 2. The new registration process is outlined in Chart 3.

---

\(^1\)Based on “How to Register a Company”, published by the Center for Commercial Law, and on the advice of experts.
One-stop shops were implemented in many regions of Ukraine, beginning in 2002. This model is the same as the standard process, except that stages 1 through 8 are completed simultaneously. Entrepreneurs submit documents to, and collect certificates and permits from, the representatives of various state agencies gathered in a single office.

**Chart 2 One-Stop Shop Registration Process, Prior to New Law**

- Company
- One-Stop Shop (Representatives of All Registering Agencies)
- State Registration Department
- Statistics Office
- Pension Fund
- Unemployment Fund
- Work-Related Accident Insurance Fund
- Temporary Disability Insurance Fund
- Tax Police, Tax Inspectorate
- Local Police Precinct
- Bank

Notes:

- **Company**
- **One-Stop Shop (Representatives of All Registering Agencies)**
- **State Registration Department**
- **Statistics Office**
- **Pension Fund**
- **Unemployment Fund**
- **Work-Related Accident Insurance Fund**
- **Temporary Disability Insurance Fund**
- **Tax Police, Tax Inspectorate**
- **Local Police Precinct**
- **Bank**
Notes:

- Enacted on 1 July 2004, the Law of Ukraine On State Registration of Legal Entities and Individual Entrepreneurs provided for implementation of one-stop shops, thus eliminating the requirement for entrepreneurs to apply in person to six different state agencies in order to register a company (Stages 2-8). The model is not yet operating efficiently, for the reasons described elsewhere in this Report.

- In addition to simplifying the initial registration process (Stage 1), the new law allows entrepreneurs to reserve a name for the future company (Stage A).

- The requirement to notify the Pension Fund in the course of opening a bank account (Stage 10) was rescinded on 12 November 2003.

- State agencies are notified of the registration of companies electronically through the Unified State Register.

- Entrepreneurs must still apply in person to state agencies to obtain the certificates needed to open a bank account.

---

**Chart 3** New Registration Process, Effective 1 July 2004

- The company works with agencies by itself
- Agencies are notified about company’s registration by e-mail through Unified State Register System
- The need to visit agencies to obtain documents for opening a bank account remains
### Stage A – Reservation of Company Name – (Chart 3 only).

- **Issuing Office:** District executive committees, city executive committees (for cities supervised by regional authorities) or regional state administration (Kyiv and Sebastopol only)

- **Effective Period:** Two months for entrepreneurs, nine months for joint stock companies

- **Documents Submitted:**
  - a) Application
  - b) Receipt for payment of registration fee
  - c) Company charter
  - d) Receipt for deposit of charter capital
  - e) Contract for purchase or lease of business premises

- **Documents Issued:**
  - a) Registration certificate
  - b) Stamp on company charter
  - c) Completed registration card

- **Processing Time:** Three working days

- **Cost:** 34 hryvnyas (US$6)

### Stage B. Opening of Temporary Bank Account to Hold Charter Capital – corporations only

#### Stage 1. Obtaining Registration Certificate – (Charts 1 and 2).

- **Documents Submitted:**
  - a) Company charter
  - b) Registration card form
  - c) Receipt for payment of registration fee
  - d) Receipt for deposit of charter capital
  - e) Contract for purchase or lease of business premises

- **Documents Issued:**
  - a) Registration certificate
  - b) Stamp on company charter
  - c) Completed registration card

- **Processing Time:** Five working days (one working day for accelerated process) from the date all documents are submitted

- **Cost:** 119 hryvnyas (US$22); accelerated process: 357 hryvnyas (US$67)

#### (Chart 3 only):

- **Issuing Office:** State Registrar, appointed by district executive committees or city executive committees supervised by regional authorities, including for Kyiv and Sevastopol.

- **Documents Submitted:**
  - a) Registration card form
  - b) General bylaw
  - c) Company charter
  - d) Receipt for payment of registration fee
  - e) Contract for purchase or lease of business premises
  - f) Receipt for deposit of charter capital
  - g) Power of Attorney (for a person acting on behalf of the principal)

- **Documents Issued:**
  - a) Registration certificate
  - b) Stamp on company charter
  - c) Two copies of completed registration card

- **Processing Time:** Three working days for registration plus one working day for issuing the certificate

- **Cost:** 170 hryvnyas (US$32)

#### Stage 2. Obtaining USRCOU Code

- **Issuing Office:** Statistics Office

- **Documents Submitted:**
  - a) Filing card form
  - b) Copy of completed registration card
  - c) Copies of passports of company principals and their identification codes

- **Deadline for Submission:** Within 10 calendar days of issuance of registration certificate

- **Documents Issued:** Certificate of inclusion in USRCOU

- **Processing Time:** Five working days (one day for accelerated process)

- **Cost:** 15 hryvnyas (US$3); accelerated process: 31 hryvnyas (US$5)
### Registration Processes in Detail

#### Stage 3. Registration with Pension Fund
- **Documents Submitted:**
  - a) Application
  - b) Copy of completed registration card
  - c) Copy of USRCOU certificate
- **Deadline for Submission:** Within 10 calendar days of issuance of registration certificate
- **Documents Issued:**
  - a) Confirmation of notification
  - b) Certificate to be submitted to bank
- **Processing Time:** Not fixed
- **Cost:** Free of charge

#### Stage 4. Registration with Unemployment Fund.
- **Issuing Office:** Employment center
- **Documents Submitted:**
  - a) Application
  - b) Copy of completed registration card
  - c) Copy of USRCOU certificate
- **Deadline for Submission:** Within 10 calendar days of issuance of registration certificate
- **Documents Issued:** Confirmation of notification
- **Processing Time:** Not fixed
- **Cost:** Free of charge

#### Stage 5. Registration with Work-Related Accident Insurance Fund
- **Documents Submitted:**
  - a) Application
  - b) Copy of the completed registration card
  - c) Copy of USRCOU certificate
- **Deadline for Submission:** Within 10 calendar days of issuance of registration certificate
- **Documents Issued:** Confirmation of notification
- **Processing Time:** 10 working days
- **Cost:** Free of charge

#### Stage 6. Registration with Temporary Disability Insurance Fund
- **Documents Submitted:** Application
- **Deadline for Submission:** Within 20 calendar days of issuance of registration certificate
- **Documents Issued:** Confirmation of notification
- **Processing Time:** Not fixed
- **Cost:** Free of charge

#### Stage 7. Registration with Tax Authorities

**7a. Tax Police:**
- **Documents Submitted:** All registration documents, passport information of the principals, directors and chief accountant

**7b. Tax Inspectorate:**
- **Documents Submitted:**
  - a) Application (Form №1-OPP)
  - b) Copy of registration certificate
  - c) Copy of USRCOU certificate
  - d) Copy of company charter, with national registry stamp
  - e) Copy of contract for purchase/lease of premises (legal address)
  - f) Copies of passports of principals, directors and accountants, along with their identification codes
  - g) Copies of Form N4-OPP if principals are corporations
- **Deadline for Submission:** Within 10 calendar days of issuance of registration certificate
- **Documents Issued:**
  - a) Certificate confirming registration as a taxpayer (Form N4-OPP)
  - b) Company charter stamped as confirmation of registration with Tax Inspectorate
- **Processing Time:** Two working days
- **Cost:** Free of charge
### Registration Processes in Detail

#### Stage 8. Obtaining Permit for Corporate Seal.
**Issuing Office:** Ministry of Internal Affairs (Local Police Precinct)

**Documents Submitted:**
- Application
- Copy of registration certificate (original to be shown when permit is issued)
- Two copies of design approved by the company
- Receipt for payment of permit fee
- Passport (to be shown when the permit is issued)

**Documents Issued:**
- Permit
- Stamped copy of seal design
- Stamp on original of registration certificate

**Processing Time:** Five working days (three days for accelerated process)

**Cost:**
- 51 hryvnyas (US$10); accelerated process: 150 hryvnyas (US$28)

#### Stage 9. Opening a Bank Account

**Documents Submitted:**
- Application (as a rule, individuals with signing authority apply in person)
- Copy of registration certificate
- Copy of company charter
- Copy tax registration certificate (Form N4-OPP)
- Signature card
- Certificate of registration with the Pension Fund
- Copy of USRCOU certificate
- Copies of confirmation of registration with social security funds
- Passports (or copies of the first and second pages and residence permit pages) for individuals with signing authority
- Certificate confirming taxpayer identification code

**Documents Issued:**
- Agreement with bank
- Counterfoil of certificate confirming registration with the Pension Fund, filled out by the bank
- Confirmation of notification of tax authorities

**Processing Time:** Ten working days

**Cost:**
- 17 hryvnyas (US$3)

#### Stage 10. Notifying Pension Fund of Bank Account

**Documents Submitted:** Counterfoil of the certificate confirming registration with the Pension Fund, filled out by the bank

**Deadline for Submission:** Within 30 calendar days of issuance of certificate by the Pension Fund for submission to the bank.

#### Stage 11. Notifying Tax Authorities of Bank Account

**Documents Submitted:** Notification form

**Documents Issued:** Stamped copy of notification form

**Deadline for Submission:** Three working days from the date the account was opened

#### Stage 12. Confirmation of Notification of Bank Account Sent by Tax Authorities to the Bank

#### Stage 13. Activation of Bank Account

---

*Depending on tax status:

**Either**

- **7c. Registration as a VAT Payer**
  - **Documents Submitted:**
    - Application (Form №1-P)
    - Receipt for payment of fee for VAT payer certificate
  - **Documents Issued:** VAT payer certificate (Form №2-P)
  - **Processing Time:** Ten working days
  - **Cost:** 17 hryvnyas (US$3)

Or

- **7d. Registration as a Flat Tax Payer (either 10% including VAT, or 6% for which registration as a VAT payer is required (see 7c))**
  - **Documents Submitted:**
    - Application
  - **Documents Issued:**
    - Confirmation of eligibility for the flat tax (6% or 10%)
  - **Processing Time:** Ten working days
  - **Cost:** Free of charge

---

*Applicable to Charts 1 and 2 only. This requirement was rescinded by the National Bank through Instruction No. 492, 12 November 2003.*
ANNEX 1

Chart 4

Agencies’ Participation in One-Stop Shops in Some Cities
(survey results)

<table>
<thead>
<tr>
<th>City</th>
<th>Number of Agencies (services)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vinnytsia</td>
<td>All (9)</td>
</tr>
<tr>
<td>Ivano-Frankivsk</td>
<td>All (9)</td>
</tr>
<tr>
<td>Kyiv</td>
<td>All (9)</td>
</tr>
<tr>
<td>Kirovohrad</td>
<td>All (9)</td>
</tr>
<tr>
<td>Lviv</td>
<td>All (9)</td>
</tr>
<tr>
<td>Rivne</td>
<td>All (9)</td>
</tr>
<tr>
<td>Odesa</td>
<td>7</td>
</tr>
<tr>
<td>Zaporizhia</td>
<td>7</td>
</tr>
<tr>
<td>Poltava</td>
<td>6</td>
</tr>
<tr>
<td>Donetsk</td>
<td>4</td>
</tr>
</tbody>
</table>

Comparison of Processing Time by Registration Process

<table>
<thead>
<tr>
<th>Registration Procedure</th>
<th>1997 - 2004</th>
<th>2002-2004</th>
<th>After 1 July 2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>District State Registration Department</td>
<td>14</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Statistics Directorate</td>
<td>4</td>
<td>4</td>
<td>4**</td>
</tr>
<tr>
<td>Pension Fund</td>
<td>7</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Work-Related Accident Insurance Fund</td>
<td>4</td>
<td>32*</td>
<td>4**</td>
</tr>
<tr>
<td>Temporary Disability Insurance Fund</td>
<td>4</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unemployment Fund</td>
<td>4</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tax Police and Tax Inspectorate</td>
<td>4</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ministry of Internal Affairs (local police precinct - permit for corporate seal)</td>
<td>7</td>
<td>7***</td>
<td></td>
</tr>
<tr>
<td>Bank</td>
<td>2</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Survey results. The overall average number of working days spent on business registration and registration with state agencies differs in aggregate from the total days for each agency, as registration with social security funds can be carried out simultaneously.
** According to the new law, registration procedures are not to take more than four days (three days for registration and one for issuing the certificate.)
*** Survey results. These two elements are shown separately for ease of comparing the differences in the three processes – the processing times for them are the same in all three registration processes. Notification of the pension fund (and the tax authorities) used to be required to open a bank account and was regarded as part of state registration. However, the requirement to notify the pension fund in the course of opening a bank account was rescinded in November 2003.
### Annex 2

#### Permits

<table>
<thead>
<tr>
<th>Chart 6</th>
<th>Key Regulatory Principles in Permit-Issuance Procedures in the EU and Ukraine</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>EU</strong></td>
<td><strong>Ukraine</strong></td>
</tr>
<tr>
<td>Permit requirements are set forth in law. Permits are mandatory only if directly stipulated by law.</td>
<td>Permit requirements are generally set forth in law. Legislation does not bar state agencies, local governments and local self-governance bodies from introducing mandatory permits and the practice is prevalent.</td>
</tr>
</tbody>
</table>
| Laws primarily define the following:  
  - materials and activities subject to permits;  
  - financial and procedural criteria;  
  - permit fees;  
  - conditions for permit cancellation;  
  - sanctions on agencies for failure to issue permits within prescribed deadlines;  
  - appeals procedure. | Most permit-related laws do not regulate procedural matters. Permit conditions related to materials, costs, documentation, etc. are stipulated in facilitating legislation enacted by the Cabinet of Ministers, state agencies and local bodies. The Administrative Procedural Code is still in draft form. |
| Legislation empowers the government to regulate certain aspects of permits issuance. Permit issuance procedures are set forth primarily in the Administrative Procedural Code. |  |
| Permit issuance procedures are always transparent because they are set forth in law and in facilitating legislation enacted by the federal government. | A sizeable portion of permit issuance procedures lack transparency, as they are passed through ordinances adopted by state agencies, local governments and self-governance bodies. |
| Special policies apply to certain businesses; for example, entrepreneurs can start work immediately after the appropriate state agency has been notified. | Such policies are not contemplated in current legislation. |
### Chart 7: Key Objectives of Permit System Reform

<table>
<thead>
<tr>
<th>Objectives</th>
<th>Solutions</th>
</tr>
</thead>
</table>
| Ensure that the requirement for each permit is necessary in the public interest | • The Verkhovna Rada should have sole authority to define the business activities subject to permits and to stipulate the permits required. State agencies and local governments should not have the authority to impose additional permits.  
• Permits not contemplated in law should be prohibited.  
• A Unified Register of Permits Issued should be implemented to keep track of all permits granted. |
| Create transparent and efficient permit issuance procedures | • State agencies and local governments should no longer be involved in regulating permit issuance. This should be the exclusive purview of the Cabinet of Ministers.  
• Uniform requirements for the content of permit-related laws should be introduced.  
• The procedure for the issuance of a particular permit, including the approvals required, should be contained in a single legislative document.  
• A simplified procedure should be introduced for permits related to non-hazardous materials and activities. |
| Reduce the number of state agencies involved in the issuance of the same permit | • If a single legislative document were to set out the procedure for the issuance of a specific permit, including all required approvals, the adoption of further laws with respect to approvals would be eliminated – a practice that has unnecessarily multiplied the number of agencies involved in issuing the same permit.  
• The enactment of laws regulating permits should be within the exclusive remit of the Cabinet of Ministers. This will prevent overlap in the competencies of state agencies. |
| Clearly define permit fees | • It should be stipulated that no fee may be charged for permits, except as provided by law.  
• If a permit fee is specified in law, it should not exceed the costs incurred by the permit-issuing body.  
• The fees charged by permit-issuing bodies for services to entrepreneurs in the preparation of applications should be set by the Cabinet of Ministers, not by state agencies.  
• Fees for similar services provided by firms established by permit-issuing bodies or by municipal and state entities should not exceed the legally-mandated fees charged by permit-issuing bodies. |
| Adapt sanitary-epidemiological, veterinary, fire safety, construction and other rules to EU and WTO standards | • The Cabinet of Ministers should assume the regulatory authority to ensure compliance with the rules within time limits set forth in law. Permits should be issued when compliance with the rules is verified. |
### Annex 3

#### Licenses

<table>
<thead>
<tr>
<th>Chart 8</th>
<th>Legal Aspects of the Procedures for Issuing the Most Common Licenses</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Types of Licenses</strong></td>
<td></td>
</tr>
<tr>
<td>Trade in alcoholic beverages and tobacco products</td>
<td>Construction, passenger and luggage transportation by road, manufacturing of and trade in pesticides and agricultural chemicals, production of and trade in medications, tourism, medical services, etc.</td>
</tr>
<tr>
<td><strong>Laws Governing Licensing Procedures</strong></td>
<td></td>
</tr>
<tr>
<td>The prerequisite for a license and the licensing procedures are set out in Law of Ukraine No. 1775-ІІІ On Licensing of Certain Lines of Business (1 June 2000).</td>
<td>The prerequisite for a license and the licensing procedures are set out in Law of Ukraine No. 481/95 BP On State Regulation of Production and Circulation of Ethanol, Cognac and Fruit Spirits, Alcoholic Beverages and Tobacco Products (19 December 1995).</td>
</tr>
<tr>
<td><strong>License-Issuing Bodies</strong></td>
<td></td>
</tr>
<tr>
<td>Wholesale licenses for alcoholic beverages and tobacco products are issued by local executive bodies in regional capitals, Kyiv and Simferopol, and the Autonomous Republic of Crimea, under the authority of the Cabinet of Ministers. Retail trade licenses for alcoholic beverages and tobacco products are issued by executive bodies in regional capitals, Kyiv and Simferopol, and the Autonomous Republic of Crimea, under the authority of the Cabinet of Ministers and subject to mandatory registration with a branch of the state taxation service and with local self-governance bodies in rural areas.</td>
<td>Licenses are issued by executive bodies or by duly authorized local government bodies, as approved by the Cabinet of Ministers.</td>
</tr>
<tr>
<td><strong>Documents</strong></td>
<td></td>
</tr>
<tr>
<td>To obtain a license, a company must submit an application and a copy of the state registration certificate for the company, authenticated by a notary or by the agency that issued the certificate.</td>
<td>The complete list of documents required is set out in On Licensing of Certain Lines of Business and includes an application and a copy of the state registration certificate for the company or a copy of the certificate confirming registration in the Unified Register of Enterprises and Organizations. Depending on the type of license, further documents are required according to the list approved by the Cabinet of Ministers.</td>
</tr>
</tbody>
</table>
### Chart 8 (Continued)

#### Processing Periods

By law, the license is to be issued or refused within ten (10) calendar days from the date the documents are submitted.

The law “On Licensing of Certain Lines of Business” provides for the following deadlines: ten (10) working days to consider the application; three working days to notify the applicant of the decision; and three working days from the date a receipt for payment of the license fee is submitted to issue the license document.

#### License Fees

The annual fee for a wholesale license for alcoholic beverages or tobacco products is 50,000 hryvnyas (US$9,412).

The annual fee for a retail license for alcoholic beverages or tobacco products is 4,000 hryvnyas (US$753); or 500 hryvnyas (US$94) in villages and settlements; per outlet, and paid quarterly in equal installments.

The annual fee for a retail license for tobacco products is 2,000 hryvnyas (US$376); or 250 hryvnyas (US$47) in villages and settlements; per outlet, and paid quarterly in equal installments.

The license fee is set by the Cabinet of Ministers and is currently the equivalent of 20 non-taxable minimum incomes (340 hryvnyas or US$64) if the license is issued by a central executive body, or 15 untaxed minimal incomes (255 hryvnyas or US$48) if the license is granted by a local executive body.

#### License Validity Period

Wholesale licenses for alcoholic beverages and tobacco products are valid for five years.

Retail trade licenses for alcoholic beverages and tobacco products are valid for one year.

Most licenses are valid for three years, with the exception of licenses for radio communications (10 years), telephone communications (15 years), and operation of commercial TV, radio and wire broadcasting networks (5 years).
## Annex 4

### Certification and Standards

<table>
<thead>
<tr>
<th>Terms</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Certification</strong>:</td>
<td>A procedure whereby products (processes, services, personnel) are confirmed as complying with statutory requirements (standards, technical requirements, etc.) It can be effected by means of a Declaration or by Independent Certification.</td>
</tr>
<tr>
<td><strong>Certification by Declaration</strong>:</td>
<td>A type of Certification. A company declares that a product (process, service) complies with statutory requirements, whereupon a Certification by Declaration document is issued.</td>
</tr>
<tr>
<td><strong>Independent Certification</strong>:</td>
<td>A type of Certification. Generally, an independent third party assesses compliance with statutory requirements, whereupon a Certificate is issued.</td>
</tr>
<tr>
<td><strong>Certificate</strong>:</td>
<td>A document attesting to compliance with statutory requirements.</td>
</tr>
<tr>
<td><strong>Mandatory Certification</strong>:</td>
<td>The requirement to certify certain types of goods that might be a danger to public health and safety.</td>
</tr>
<tr>
<td><strong>Certification in a Non-Statutorily Regulated Field</strong>:</td>
<td>Voluntary certification.</td>
</tr>
<tr>
<td><strong>Certification Body</strong>:</td>
<td>A testing laboratory or a certification agency.</td>
</tr>
<tr>
<td><strong>Technical Regulation</strong>:</td>
<td>The legally-mandated requirements for a product subject to Mandatory Certification, including safety requirements, labeling guidelines, conditions for sale, etc.</td>
</tr>
<tr>
<td><strong>Accreditation</strong>:</td>
<td>Official acknowledgement that a Certification Body is authorized to conduct tests and issue Certificates.</td>
</tr>
</tbody>
</table>
Chart 9 Certification of Goods

State Committee for Consumer Policy and Standards of Ukraine
- Develops standards and stipulates the goods that are subject to certification
- Controls entry into the market of accredited certification bodies
- Sets certification rules and supervises their implementation
- Maintains the UkrSEPRO register (register of mostly state-owned certification bodies)
- Oversees certification bodies and manufacturers

National Accreditation Agency of Ukraine
- Carries out accreditation of certification bodies
- Supervises certification bodies
- Hears appeals

Assesses test results for compliance.
1. Product Sample
2. Testing Laboratory
3. Test Results
4. Certification Body
5. Certificate
6. Manufacturer
7. Certified Products
8. Market
9. Consumer

Obtains licenses and permits to operate in the market
Reduces liability by confirming safety of goods
Gains competitive advantage through perceived superiority of goods
Raises consumer awareness of the value of goods that are certified safe

Quality is improved
Competition is promoted
Assured of product safety
Able to make informed choice between products.
The Simplified taxation for small business was introduced under the Decree of the President of Ukraine No.727/9 On the Simplified Taxation System for Small Businesses (3 July 1998).

A company is eligible if it employs less than 50 people and its annual revenue from the sale of goods or services does not exceed 1 million hryvnyas (US$187,000).

An eligible company has the following simplified taxation (flat tax) options:

- 6% of revenue from the sale of goods or services, excluding excise duty, plus VAT; or
- 10% of revenue from the sale of goods or services, excluding the excise duty but including VAT.

The flat tax is deemed payment of the following taxes and charges:

- Income tax
- VAT (only for those paying the 10% flat tax)
- Land tax
- Charge for the special use of natural resources
- Contribution to the fund established to mitigate the Chernobyl disaster
- Contribution to the State Innovation Fund
- Contribution to social insurance programs
- Contribution to road construction and maintenance
- Municipal tax
- Occasional trade tax (up to four transactions per year)
- Contribution to state Pension Fund
- Fees for permits to open a retail outlet or service business
- Contribution to the Fund for the Social Protection of the Disabled
- Contribution to the State Employment Promotion Fund
- Trade Mark fees
### Chart 11

Taxes and Other Mandatory Payments Applicable to Companies in 2003

<table>
<thead>
<tr>
<th>State Taxes and Other Payments</th>
<th>Local Taxes and Other Payments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value Added Tax</td>
<td>Advertising tax</td>
</tr>
<tr>
<td>Excise duty</td>
<td>Municipal tax</td>
</tr>
<tr>
<td>Corporate income tax</td>
<td>Car parking fees</td>
</tr>
<tr>
<td>Customs duty</td>
<td>Open-air market fee</td>
</tr>
<tr>
<td>Government fees</td>
<td>Horse racing fee</td>
</tr>
<tr>
<td>Land tax</td>
<td>Charge for the use of local public symbols for commercial purposes</td>
</tr>
<tr>
<td>Real estate tax (The payment mechanism is not yet in place)</td>
<td>Filming charge</td>
</tr>
<tr>
<td>Tax on vehicles and other self-propelled mechanisms</td>
<td>Auction, tender or lottery charges</td>
</tr>
<tr>
<td>Charge for special use of natural resources</td>
<td>Fees for permits to locate trade outlets and service companies</td>
</tr>
<tr>
<td>Charge for state-funded prospecting</td>
<td>Fee levied on motorists travelling through border areas (Rescinded in April 2003)</td>
</tr>
<tr>
<td>Environmental pollution charge</td>
<td></td>
</tr>
<tr>
<td>State Social Insurance contribution (Replaced by Pension Fund contribution)</td>
<td></td>
</tr>
<tr>
<td>Trade mark fees for certain lines of entrepreneurial activities</td>
<td></td>
</tr>
<tr>
<td>Fixed agricultural tax</td>
<td></td>
</tr>
<tr>
<td>Charges to finance the development of winemaking, gardening and hop cultivation</td>
<td></td>
</tr>
<tr>
<td>Flat border-crossing charge</td>
<td></td>
</tr>
<tr>
<td>Contribution to the Fund for Guaranteeing Deposits of Individual Citizens* (the Fund is not included in the State Budget of Ukraine)</td>
<td></td>
</tr>
<tr>
<td>Electricity and heat surcharge</td>
<td></td>
</tr>
<tr>
<td>Rental payments (oil and gas companies)</td>
<td></td>
</tr>
</tbody>
</table>