UKRAINE

TRADE SUMMARY

The U.S. goods trade surplus with Ukraine was $401 million in 2009, shifting from a deficit of $472 million in 2008. U.S. goods exports in 2009 were $890 million, down 52.4 percent from the previous year. Corresponding U.S. imports from Ukraine were $489 million, down 79.1 percent. Ukraine is currently the 75th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Ukraine was $910 million in 2008 (latest data available), down from $991 in 2007.

United States-Ukraine Trade and Investment Cooperation Agreement

The United States and Ukraine signed a new Trade and Investment Cooperation Agreement (TICA) on April 1, 2008, establishing a forum for discussion of bilateral trade and investment relations. The TICA mandates a joint United States-Ukraine Council on Trade and Investment, which addresses a wide range of trade and investment issues including market access, intellectual property, labor, and environmental issues. The Council seeks to increase commercial and investment opportunities by identifying and working to remove impediments to trade and investment flows between the United States and Ukraine. The Council met for the second time on October 14, 2009.

IMPORT POLICIES

Ukraine continues to maintain licensing requirements and fees on certain imports. Ukraine imposes several duties and taxes on imported goods: customs/import tariffs, value added tax (VAT), and excise duties. Additionally, imports into Ukraine are subject to customs processing fees, a unified fee on vehicles crossing Ukraine's borders, and port fees.

Customs/Import Tariffs

Imports from the United States are subject to Ukraine's MFN applied rate which fell to an average of 4.95 percent after its accession to the World Trade Organization (WTO) in 2008. For agricultural goods, the average applied tariff rate is now 13 percent (down from 13.8 percent before WTO accession). For industrial goods the average applied rate is now 3.71 percent (down from 4.4 percent before WTO accession). Ukraine applies preferential tariff rates to imports from its 12 FTA partners and certain Commonwealth of Independent States (CIS) countries. Most MFN customs tariffs are levied at *ad valorem* rates, and only 1.5 percent of tariff lines (down from 5.97 percent prior to WTO accession) are subject to specific or combined rates of duty. These specific and combined rates apply primarily to agricultural goods that are also produced in Ukraine, such as grains, poultry products, sugar, and vegetables such as carrots and potatoes.

In 2009, the Ukrainian State Customs Service (SCS) began to assign higher customs values to U.S. food and agricultural imports than was declared in the import documentation. There are concerns on how the Ukraine State Customs Service is determining and/or calculating the new values. For some shipments, it is alleged that the result has been a customs valuation 100 percent higher than what was declared in the import documentation. Importers who have sought to appeal the assigned customs valuation have been instructed by SCS to have the government from the country of the product's origin provide verification. These practices have made importing U.S. meat products, in particular, expensive and have impeded trade in these products. The United States government has raised its concerns about the valuation practices and is continuing to seek information on the reasons for the changes and the methodology used to determine the customs values.

On February 20, 2009, President Yushchenko signed into law a bill that imposed a temporary 13 percent increase in customs duties for a large number of imported goods. The increases went into effect on March 6, 2009 and expired on September 7, 2009. The tariffs affected by the law were increased to well above Ukraine's WTO bound rates, *i.e.*, the rate that generally cannot be exceeded under WTO rules, and the WTO's Balance of Payments Committee rejected Ukraine's argument that the tariff was justified by a trade imbalance crisis. The U.S. government signaled its concern over this measure, which adversely affected a significant number of U.S. exports, and continues to monitor the situation due to concerns that similar increases could be repeated through future legislation.

Excise Duties

Ukraine applies excise duties to a limited set of goods imported into Ukraine, such as alcoholic beverages, non-filter cigarettes, motor vehicles, and petroleum products. Excise duty rates range from 10 percent to 300 percent of the declared customs value. High excise duties hinder U.S. exports of wine and grape spirits and automobiles to Ukraine. Although VAT and excise tax exemptions for locally-produced vehicles were eliminated in 2005, excise taxes on imported automobiles remain high, especially for those with larger engines, ranging from 0.02 euro/cc for automobiles with smaller engines to 3.50 euro/cc for those with larger engines. Although import tariffs on automobiles were significantly reduced as part of the commitments Ukraine made for WTO accession, the government has introduced a new registration fee that is considerably higher for used cars and therefore discourages imports of foreign used cars.

Import Licenses

Import licenses are required for some goods. The list of goods covered by the licensing regime and the license terms are decided annually by the Cabinet of Ministers. In 2009, the list included pesticides, alcohol products, sugar and sugar syrup, prepared food products containing cocoa, optical media production inputs, some industrial chemical products and equipment containing them, official foreign postage stamps, excise marks, officially stamped/headed paper, checks and securities, some goods that contain sensitive encryption technologies, and ozone-depleting substances.

While the licenses themselves are granted automatically to applicants, some products require a separate licensing approval, which may or may not be automatic, from the relevant administrative agency before receiving the necessary import license from the Ministry of Economy. The Ukrainian State Committee for Veterinary Service established a procedure of import approvals that amounts to non-automatic licensing. The procedure is prescribed in the Law on Veterinary Medicine and covers all commodities subject to veterinary control. Approval is needed even for cases in which a bilateral veterinary certificate is issued by the country of origin. In 2008, the Ministry of Environment significantly tightened procedures for obtaining its approval to import goods that are potentially ozone-depleting. The stricter procedures delayed shipments and significantly increased business costs for importers of a wide range of goods, including aerosols, refrigerators, mascara, lipstick, toothpaste, and coffee makers.

For some goods, product certification is a prerequisite for an import license. Importers can request that a foreign facility be certified as in compliance with Ukraine's technical regulations that apply to imports. The U.S. distilled spirits industry reports that this option usually involves a burdensome and costly inspection visit by Ukrainian government officials. If approved, the supplier receives a certificate of conformity valid for two to three years and avoids the burden of certifying each shipment and mandatory laboratory testing upon arrival in Ukraine.

GOVERNMENT PROCUREMENT

Ukraine is not yet a signatory to the WTO Agreement on Government Procurement (GPA), but committed to initiate negotiations for GPA membership within two years of its WTO accession. Ukraine is reportedly preparing its initial offer to begin the process of GPA accession. It became an observer to the WTO Committee on Government Procurement in February 2009.

Ukraine's 2000 law "On Procurement of Goods, Works, and Services Using State Funds" was originally largely in line with international practice. However, amendments in 2004 to 2006 opened the system to widespread corruption and moved it away from international norms. Authority to carry out central oversight and policy development for the government procurement system was taken from the Ministry of Economy, and its policy and oversight functions were dispersed across several bodies, weakening oversight and policy making, and creating conflicts of interest and overlapping functions.

In March 2008, Parliament, responding to widespread complaints of the corruption and dysfunctional nature of the Ukrainian procurement system, repealed the 2000 law, as amended. In its place, the Cabinet of Ministers issued a decree establishing temporary provisions for government procurement. The decree eliminated the Tender Chamber of Ukraine, a nongovernmental organization, which had had the authority to monitor the procurement process and had become the center of the procurement system's corruption and lack of transparency. In addition, the decree made the Ministry of Economy the central oversight and policy body for the procurement system. The Constitutional Court subsequently ruled the temporary provisions unconstitutional on technical grounds, leaving Ukraine without a functioning government procurement system. On October 17, 2008, the Cabinet of Ministers issued a new decree, which closely tracked the previous temporary provisions. The constitutionality of the October 17 decree is not yet clear even though it was intended to address the constitutional issue raised by the Court.

A new draft procurement law passed a first reading on May 20, 2008. However, while the draft law awaited a second reading, amendments were introduced that, if enacted, would put in place a weak procurement regime that could once again open the system to conflicts of interest and corruption. The amendments include: establishment of an inter-ministerial commission that resembles the former Tender Chamber; weakening and dispersing policy and oversight functions; establishment of a defective and insufficiently independent bid protest mechanism; and expanding the number of exclusions from the application of the law. The Ministry of Economy, with support from the World Bank and the European Commission, has prepared an alternate draft procurement law based on the version that passed the first reading. This draft is generally in line with international standards and is advocated by the donor community.

The Cabinet of Ministers' decree currently in force requires that all government procurement of goods and services valued at more than UAH 100,000 (approximately $16,500) and public works valued at more than UAH 300,000 (approximately $50,000) must be procured through competitive tenders. Open international tenders are used where procurement is financed by an entity outside of Ukraine.

Ukraine's procurement rules generally do not restrict foreign enterprises from participating in government procurement, but in practice foreign companies claim that they are rarely able to compete on an equal footing with domestic companies. Foreign companies generally win only a tiny fraction of the total tenders. Among the problems faced by foreign firms are: (1) lack of public notice of tender rules and requirements; (2) non-transparent preferences in tender awards; (3) imposition of conditions that were not part of the original tender requirements; and (4) ineffective grievance and dispute resolution mechanisms, which often allow a losing bidder to block the tender after the contract has been awarded.

EXPORT BARRIERS

Exports of some categories of products are subject to registration by the Ministry of Economy. Products that must be registered prior to export from Ukraine include precious metals and stones, rolled metal products exported to the United States, scrap metal, printer's ink, optical polycarbonates for laser reading systems, optical disc manufacturing equipment, and paper with watermarks. The government has eliminated most export duties, with the notable exception of duties on natural gas, livestock, raw hides, some oil seeds, and scrap metal. As part of the commitments Ukraine made for WTO accession, Ukraine agreed to reductions of a number of these duties and elimination of others.

Export Restrictions on Grains and Sunflower Oil/Seeds

Ukraine is the sixth largest wheat exporter in the world, and has in the past resorted to grain export restrictions in reaction to poor harvests. The supply of products deemed "socially important" (*e.g.*, vegetable oil, bread, and sugar) is controlled by the government.

Live Cattle, Sheep, Hides, and Skins

Export duties remain in place on live cattle, sheep, hides, and skins. However, trade of these products has been negligible. Ukraine continues a staged reduction of these duties. Export duties on live calves, cows, and sheep will fall to 10 percent in 2016. Export duties on raw hides will fall to 20 percent in 2018.

Scrap Metal

Between January 2003 and WTO accession in May 2008, Ukraine imposed an export duty of 30 euro/metric ton on ferrous steel scrap and had, in effect, a ban on exports of nonferrous metals. The ferrous scrap export duty contributed to a decline in scrap exports from Ukraine, when global demand and prices for steel scrap were rising. Ukrainian metallurgical producers benefited from scrap inputs at prices lower than world levels. As part of its March 2006 bilateral WTO Market Access Agreement with the United States, Ukraine agreed to significantly lower these export duties. Upon WTO accession, duties fell to 25 euro/metric ton for ferrous metals and to 30 percent *ad valorem* (with minimum, specific rates for some products) for nonferrous metals. Laws passed in 2006 and 2007 as part of the accession process provide for staged duty reductions to 10 euros/metric ton over a period of 6 years (2008 – 2014) for ferrous metals and reductions to 15 percent *ad valorem* over a period of 5 years (2008 – 2013) for nonferrous metals.

Sunflower Seed, Flaxseed, and Linseed

Sunflower seed, flaxseed, and linseed have been subject to an export duty since June 2001. The export duty on sunflower seed was lowered from 17 percent to 14 percent in 2008. The duties are subject to a one percent decrease annually until duties reach 10 percent. The duty was 13 percent as of January 1, 2010.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Ukraine was listed on the Watch List in the 2009 Special 301 report. Key concerns cited in the report included widespread retail piracy, the transshipment of pirated and counterfeit goods, Internet piracy, and government use of illegal software. The Ukrainian government meets regularly with U.S. Government officials and with U.S. and domestic industry representatives to monitor the progress of enforcement efforts through the United States-Ukraine IPR Enforcement Cooperation Group.

SERVICES BARRIERS

Audiovisual Services

A local content requirement exists for radio and television broadcasting, although it has not been stringently enforced in most cases. In November 2009, Ukrainian customs authorities stated that it had changed its rules for customs valuation for audiovisual products. Rather than assessing duties on the underlying carrier medium, they will assess valuation on projected royalties. To further complicate matters, Ukrainian customs officials stated that this new "ruling" is supposedly retroactive three years with serious penalties applied to those situations where valuation was based on the carrier medium.

Financial Services

The United States continues to monitor Ukraine's actions in particular with regard to electronic payments services. A ruling by the Ukrainian Anti-Monopoly Committee modified the National Bank of Ukraine's June 19, 2008 rules that required any bank that wished to bid on cash management contracts for state employee salaries to join the National System of Mass Electronic Payment (NSMEP). NSMEP operates as a domestic electronic payments system in Ukraine, competing against foreign service suppliers. Under the modified ruling, banks are still required to become members of NSMEP, but there is no provision to force them to issue payment cards exclusively through that system. However, parliament is considering new legislation that would require all banks to join NSMEP and use that service exclusively for electronic payment transactions. This would force banks wishing to bid on government cash management contracts to base their bids on NSMEP-branded cards, thus shutting out foreign service suppliers.

INVESTMENT BARRIERS

The government is working to streamline regulations and eliminate duplicative and confusing laws regarding investment and business. The State Center for Foreign Investment Promotion (known as InvestUkraine) is charged with helping attract foreign investment to the country. The Council of Investors, an advisory body to the Cabinet of Ministers, includes representatives from foreign and domestic companies and advises the government on efforts to improve the business and investment climate.

The United States has a bilateral investment treaty (BIT) with Ukraine, which took effect in 1996. The BIT guarantees U.S. investors non-discriminatory treatment, the right to make financial transfers freely and without delay, international legal standards for expropriation and compensation, and access to international arbitration. Despite the BIT, there are several longstanding investment disputes faced by several U.S. companies. These disputes mainly date from the early 1990s and the initial opening of the Ukrainian economy to foreign investors. In most cases, however, there has been little progress toward resolution under subsequent Ukrainian governments despite advocacy by the United States. In 2009, U.S. investors filed for international arbitration in a contract dispute involving poultry imports.

An agreement signed in December 2009 ended a longstanding, dispute that had prevented the U.S. Overseas Private Investment Corporation (OPIC) from operating in Ukraine. This agreement will enable OPIC to provide financing and political risk insurance to American companies operating in Ukraine.

Taxation

Companies report that Ukraine's taxation system is a major obstacle for U.S. investors doing business in Ukraine, and a World Bank study released in September 2009 ranked Ukraine 180th out of the 181 countries surveyed in terms of the ease of paying taxes. Ukraine maintains a corporate profit tax (25 percent), a personal income tax (flat rate of 15 percent), a Value Added Tax (20 percent), and a payroll tax (variable, between 33.2 percent and 49.6 percent) that funds pension and social insurance programs. An average Ukrainian business has to pay 99 separate taxes and its profits are taxed at an overall rate of 58.4 percent. Many analysts single out the payroll tax as being exceptionally high and the main reason why shadow wage payments remain common in Ukraine.

In recent years, delays in the payment of VAT refunds to exporters have also been a problem. Industry reports that the government of Ukraine has been holding back the payment of VAT refunds for extended periods of time, for which it has been heavily criticized. The government stated its intention to introduce a comprehensive electronic system to ensure speedy refunds in the future, but no action has yet been taken in this direction. Ukraine's inability to refund VAT in a timely manner remains a problem, and delays in reimbursement have become an important cost factor for many foreign companies. Improvements to the system would have an important, positive impact on the investment climate.

Privatization

The State Property Fund oversees the privatization process in Ukraine. Privatization rules generally apply to both foreign and domestic investors, and, in theory, a relatively level playing field exists. Observers claim, however, that a common abuse of privatization laws is the adjustment of the terms of a privatization contest to fit the characteristics of a certain, pre-selected bidder. Few major, new privatizations have been conducted since the privatization rush of 2004. In 2005, Ukraine revoked the privatization of the Krivorizhstal steel factory, which had been sold to a group of domestic investors for $800 million, and subsequently sold it in a fair and transparent tender to Mittal Steel for $4.8 billion, in what is generally viewed as Ukraine’s most transparent major privatization to date. Since then, Ukraine has taken no further steps to reverse previous privatizations.

No major privatizations took place in 2009, largely due to constant political wrangling over the privatization process. The government has identified Ukrtelekom (the state telecommunications company), the Kryvorizhskyy Ore Mining and Processing Plant, and Turboatom (a producer of turbines for power plants), as priorities for privatization, but none have moved forward. Other attempts at privatization in recent years were often marked by controversy. In 2009, the Odessa Portside Plant, one of Ukraine’s largest chemical producers, was to be sold at an auction between three bidders. However, the Ukrainian government subsequently nullified the results of the auction, claiming that the bidders had colluded to bring down the price, and withdrew the facility from the privatization process. The government has also announced its intention to privatize approximately 120 of the 140 coal mines still owned by the government. There are concerns that a few Ukrainian and Russian firms are trying to acquire these mines without going through a fair, transparent privatization process.

Ukraine maintains a moratorium on the sale of agricultural farmland. This provision blocks private investors from purchasing some of the 33 million hectares of arable land in Ukraine and constitutes a serious obstacle to the development of the agricultural sector. While there have been some efforts to adopt new legislation necessary to open the land market, the ban on the sale of agricultural land is set to continue until January 1, 2012, when it comes up for renewal.

Corporate Hijacking

Ukraine continues to have problems with corporate hijacking activities. Some researchers claim that thousands of Ukrainian enterprises have suffered hijacking attempts in the last several years. These hijackers frequently purchase a small stake in a company, and then take advantage of what appears to be a combination of deficient legislation, corrupt courts, and a weak regulatory system to gain control of the company to the detriment of rightful shareholders. This development harms investors, including U.S.

companies and shareholders, and has damaged the image of Ukraine among foreign investors. The Ukrainian government has recognized the seriousness of this problem and has taken some steps to address it. In September 2008, Parliament passed a new law "On Joint Stock Companies," a major step to improve corporate governance and help stop corporate hijacking.