

UKRAINE

TRADE SUMMARY

The U.S. goods trade balance with Ukraine went from a trade deficit of \$884 million in 2006 to a trade surplus of \$121 million in 2007. U.S. goods exports in 2007 were \$1.3 billion, up 77.4 percent from the previous year. Corresponding U.S. imports from Ukraine were \$1.2 billion, down 25.6 percent. Ukraine is currently the 65th largest export market for U.S. goods.

The stock of U.S. foreign direct investment in Ukraine was \$505 million in 2006 (latest data available).

WTO Accession

Ukraine has completed the process of negotiating terms of accession to the World Trade Organization (WTO). On March 6, 2006, the United States and Ukraine signed a WTO bilateral market access Agreement. Later that month, the United States terminated the application of the Jackson-Vanik amendment to the Trade Act of 1974 to Ukraine, providing Ukraine permanent normal trade relations (PNTR) status. Ukraine made significant progress during 2007 in adopting legislation and regulations needed for compliance with WTO requirements. It also completed its bilateral market access negotiations with all other interested WTO Members. Members of Ukraine's WTO accession Working Party, including the United States, completed the multilateral Working Party process for Ukraine's WTO accession in January 2008.¹

IMPORT POLICIES

Ukraine continues to maintain fees and 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

Ukraine's tariff schedule provides for three rates of import duty: full rates, Most Favored Nation (MFN) rates, and preferential rates. The full rate of import duty can be from 2 times to 10 times higher than the MFN rate. It currently is applied to a very small number of goods from 81 countries. In 2007, the number of goods still subject to the higher rates was sharply reduced. When it becomes a WTO Member, Ukraine would apply the MFN rate to all goods originating from WTO Members, in accordance with Article I of the GATT 1994, so the number of countries whose goods are subject to full duties will decline sharply. Preferential rates are applied to imports from countries with which Ukraine has a Free Trade Agreement (FTA) or other preferential trade agreement. Ukraine has an FTA with a number of CIS countries. Imports from the United States are subject to the MFN rate.

¹ The WTO General Council approved the terms of Ukraine's accession on February 5, 2008. Ukraine will become a Member of the WTO 30 days after it submits its instrument of acceptance of the accession package to the WTO Secretariat, which is expected to occur in mid-2008.

Import duties are calculated in accordance with the law “On the Customs Tariff of Ukraine.” Their levels currently undergo annual changes already provided for in the Customs Tariff Law, and Ukraine will implement additional tariff liberalizations as a result of its negotiations on WTO accession when it joins the WTO. The customs tariff schedule comprises more than 11,000 tariff lines. Most customs tariffs are levied at *ad valorem* rates, but 672 tariff line items (5.97 percent) are subject to specific or combined rates of duty. These specific and combined rates apply to approximately one-third of tariff lines for agricultural goods, primarily those that are also produced in Ukraine. These protected goods include grains, poultry products, sugar, and vegetables such as carrots and potatoes. For agricultural goods, the average applied tariff rate is 13.8 percent (down from 19.7 percent in 2005). The number of tariffs lines subject to combined rates of duty will be sharply reduced when Ukraine implements its WTO accession tariff commitments and the average applied tariff rate will drop to below 12 percent. By contrast, for industrial goods the average applied rate is 4.4 percent (down from 8.3 percent).

High import tariffs on goods such as poultry act as a barrier to U.S. exports. As a result of the March 2006 WTO bilateral Market Access Agreement with the United States, tariffs on poultry and many other goods will be reduced significantly when Ukraine becomes a Member of the WTO.

Excise Duties

Ukraine applies excise duties to a limited set of goods imported into Ukraine, such as alcoholic beverages, nonfilter cigarettes, motor vehicles, and petroleum products. Discriminatory excise duties still hinder U.S. exports of wine and grape spirits and automobiles to Ukraine. The excise duty rate on imported wine and grape spirits is 12 times and 13 times higher, respectively, than on domestically-produced products, and this difference is likely to remain at that level until Ukraine becomes a Member of the WTO and excise rates on imported and domestic goods are unified. Although VAT and excise tax exemptions for locally-produced vehicles were eliminated on March 29, 2005, excise taxes on automobiles remain high, ranging from 0.02 euros/cc for automobiles with smaller engines to 3.50 euros/cc for those with larger engines. The import tariff on fully assembled automobiles was raised from 15 percent to 25 percent during 2005 to compensate local producers for the loss of VAT and excise privileges. This increase has negatively impacted importers of fully assembled automobiles. Application of a lower tariff rate on “semi-knocked down” vehicles further discourages imports of fully assembled automobiles.

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 2007, the list included pesticides, alcohol products, 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 prior approval, which may or may not be automatic, from the relevant administrative agency before receiving the necessary import license from the Ministry of Economy. In the WTO accession negotiations, the United States has sought assurances from Ukraine that it will not impose restrictive import licensing requirements without adequate WTO justification, (*e.g.*, on imports of mass-market, commercially-traded goods containing encryption that are covered by the Information Technology Agreement). In 2007, beef, pork, and poultry (fresh, chilled, or frozen) and related live animals became subject to import licensing without prior approval. Copper sulphate, optical polycarbonates for production

of discs for laser-reading systems, cane and beet sugar, and chemically pure sucrose in solid form became subject to import licensing without prior approval.

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 2 years to 3 years and avoids the burden of certifying each shipment and mandatory laboratory testing upon arrival in Ukraine.

STANDARDS, TESTING, LABELING, AND CERTIFICATION

For a number of years, U.S. investors have regarded Ukraine's product certification system and standards regime as a significant obstacle to trade and investment. Recently, Ukraine has passed several new laws and governmental decrees aimed at bringing Ukrainian practices in this area into line with the WTO Agreement on Technical Barriers to Trade. As of October 2007, more than 4,000 of Ukraine's standards were harmonized with international standards, and approximately 8,000 remained to be harmonized.

Standardization and Certification

Mandatory certification is required in Ukraine for many products. The State Committee for Technical Regulation and Consumer Policy (DerzhSpozhyvStandard) is the standardization and certification body in Ukraine. DerzhSpozhyvStandard has a network of 114 accredited product certifying bodies, including 60 accredited certifying bodies for quality management systems, as well as about 780 testing laboratories throughout Ukraine, 170 of which are accredited by the National Accreditation Agency as complying with international standards. Appropriate resources, such as modern analytical equipment and reactants, are not available in most laboratories. DerzhSpozhyvStandard's system includes 27 territorial departments for consumer protection and 28 state centers for standardization, systematizing weights and measures, and certification. Depending on the type of product, testing, and applicable certification scheme, the certification process can take from 3 days to 1 month.

Ukraine has both private certification bodies, which operate on a profit-making basis and are more common in the area of technical regulations compliance, and certification bodies affiliated with state agencies, which are more common in ensuring compliance with sanitary and phytosanitary measures. Some certification agencies do much of their work with little or no coordination with other Ukrainian bodies performing similar tests. Many products require multiple certificates from different agencies, with local, regional, and municipal authorities often requesting additional documentation beyond that required by central bodies. According to industry sources, numerous burdensome certification and licensing procedures for equipment impede access to the Ukrainian market. Experts allege that government officials responsible for issuing licenses often require businesses to provide documents that are not mandatory deliberately conceal information in order to confuse a potential licensee, or delay issuing documents in order to induce licensees to offer a bribe.

These issues are being addressed during Ukraine's WTO accession negotiations, and, as recently as September 13, 2007, Ukraine has reduced the number of products subject to mandatory certification. When it becomes a WTO Member, Ukraine will be obliged to apply such mandatory requirements only in conformity with WTO provisions on technical regulations,

including ensuring that such measures are not more trade restrictive than necessary to fulfill a legitimate objective, and reliance on available scientific and technical information. A May amendment to the law “On Standards, Technical Regulations, and Conformity Assessment Procedures” helped to guarantee precedence of international over regional standards and introduced provisions related to conformity assessment recognition, although further amendments may be needed to ensure that Ukraine’s authorities will accept the results of conformity assessment procedures performed in the United States. Ukraine’s National Accreditation Agency is taking steps to become a member of the International Laboratory Accreditation Cooperation (ILAC), anticipated in 2009. Once an ILAC member, Ukraine should significantly increase the acceptance of test results of laboratories accredited with, and notified by, ILAC member bodies.

Sanitary and Phytosanitary (SPS) Measures

Ukraine applies a range of SPS measures that restrict imports of a number of U.S. agricultural products, among them, pork, beef, and poultry. Industry has repeatedly complained that Ukraine’s certification and approval process is lengthy, duplicative, and expensive. Over the past several years, Ukraine has passed amendments to several laws and regulations, most importantly to the law “On Veterinary Medicine” and the law “Quality and Safety of Food Products and Food Raw Materials,” to bring its legislative and regulatory framework into compliance with requirements of the WTO SPS Agreement. The following potentially trade distorting issues are subjects of discussion between the United States and Ukraine as part of the negotiations on Ukraine’s accession to the WTO:

Overlapping State Authorities: Ukraine has maintained a complex and nontransparent oversight system for human and animal health measures that involves overlapping authority by the Veterinary Service, Sanitary Service, and DerzhSpozhyv Standard. Amendments to the law on “On Standards, Technical Regulations, and Conformity Assessment Procedures,” passed in May, made some progress but failed to solve entirely the problem of overlapping authority. Additional legislative or regulatory amendments are needed. Further legislation has been enacted in 2007 that strengthens the legal separation of authority over testing for SPS and Technical Barriers to Trade (TBT) issues.

Beef, Beef Products, and Pork: A bilateral agreement with Ukraine negotiated at the same time as the March 2006 WTO bilateral Market Access Agreement, addresses the terms of U.S. exports of beef, beef products, and pork to Ukraine. As agreed, Ukraine has allowed the entry of certified U.S. beef and pork that meets veterinary certificate requirements. The United States continues to monitor ongoing trade.

In the past, Ukraine blocked the importation of beef and beef products due to concerns over the use of growth promoting hormones as well as Bovine Spongiform Encephalopathy (BSE). The United States is working with Ukraine to ensure that any requirements imposed by Ukraine are consistent with World Organization for Animal Health guidelines. Ukraine’s law “On Veterinary Medicine” was amended in November 2006 in order to address this issue, and in 2007 additional regulatory amendments were enacted to address concerns over maximum residue levels, animal identification requirements, and the definition of contaminants.

U.S. pork exports to Ukraine have been hampered by regulations concerning trichinae. The United States is working with Ukraine to align Ukrainian standards for trichinae with international norms.

Biotechnology: Ukraine has not established an approval process for agricultural biotechnology products. The absence of an approval process has resulted in unpredictable sales conditions for corn products, soybeans, and meal. The United States is working with Ukraine to establish procedures governing biotechnology that are supported by science-based risk assessment principles and guidelines, including those of the WTO SPS and TBT Agreements, the Codex Alimentarius, and the International Plant Protection Convention (IPPC). In May, Parliament passed a new law establishing a framework for the creation, testing, and use of products of biotechnology. Implementing regulations for the law are under development and scheduled to take effect prior to Ukraine's WTO accession.

Fish Shelf life: In Ukraine's WTO accession talks, Ukraine committed to make changes to its technical regulation on shelf life for fish such as salmon, sardines, and roe to bring it into conformity with the CODEX Alimentarius guidelines on the labeling of prepackaged food products.

GOVERNMENT PROCUREMENT

Ukraine is not yet a signatory to the WTO Agreement on Government Procurement (GPA), but committed to become an observer to the GPA when it becomes a WTO Member, and to initiate negotiations for membership within 2 years after that. Ukraine's total government procurement stood at \$4.11 billion for April through December of 2006.

All government procurement of goods and services valued at more than \$10,000 and public works valued at more than \$80,000 must be procured through competitive tenders. Open international tenders must be used when procurement is financed by any entity outside of Ukraine. The Tender Chamber of Ukraine publishes information on government procurement in the "State Procurement Bulletin."

Ukraine's recent amendments of the law "On Procurement of Goods, Works, and Services Using State Funds" have moved it away from international norms. A recent study on Ukraine by the Atlantic Council of the United States concluded that "government procurement is one of the most corrupt spheres of state activity." Amendments to the procurement law in March 2006 transferred the authority to coordinate government procurement from the Ministry of Economy to the Antimonopoly Committee of Ukraine, a body with no particular expertise in regulating public procurement. The amendments also dispersed policy and oversight functions across several bodies, including the Antimonopoly Committee, the Accounting Chamber of Ukraine (reporting to Parliament), the State Control and Audit Unit (under the Ministry of Finance), and the Tender Chamber of Ukraine. The amendments have been criticized for creating an overlap in authority of various regulatory agencies and decreasing the transparency of the system.

The 2006 amendments granted the Tender Chamber of Ukraine, purportedly a nongovernmental organization, the authority to monitor the procurement process, and to undertake key operational functions that are inherently governmental. The Tender Chamber has exclusive authority to maintain a catalog of bidders, consider claims of tender participants, and select suppliers to be awarded contracts. It also requires a UAH 7000 (\$1,400) fee for bidders to be registered in the catalogue, in contravention of the international practice of free listing for all interested parties. The Tender Chamber has faced widespread criticism as contributing to the procurement system's corruption and lack of transparency.

Only the European Consulting Agency, a Ukrainian private enterprise with links to the Tender Chamber has been allowed to operate a website announcing tenders. Several observers have

charged that this relationship fosters corruption and decreases transparency. In addition, the 2006 amendments introduced burdensome and lengthy procurement procedures, and required all tender proposals to be secured by collateral, limiting the number of tender participants and increasing the cost of participation. For some procurement, the Tender Chamber assesses fees of 4 percent of the value of the procurement, which is extremely high by international norms.

Under the December 2006 amendments to the law, procurement rules do not apply to some tenders of special public sectors, such as defense, postal and telecommunications services, and railways.

The procurement law does 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 (0.01 percent during the first nine months of 2006). Among the problems faced by foreign firms are: (1) the lack of public notice of tender rules and requirements; (2) covert preferences in tender awards; (3) the 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. March 2007 amendments to the law eliminated preferences that favor domestic bidders in tenders below certain values. However, some regulations still exclude foreign bidders; for example, some firms report that there is a practice in health sector procurement of only accepting bids from Ukrainian resellers or Ukrainian producers of pharmaceuticals.

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, textile products exported to the United States, scrap metal, printer's ink, and paper with watermarks. The government has eliminated most export duties, with the prominent exceptions of natural gas, livestock, raw hides, some oil seeds, and scrap metal. In the context of its WTO accession negotiations, Ukraine has negotiated reductions in a number of these duties and the elimination of others.

Export Restrictions on Grains

Ukraine is the sixth largest wheat exporter in the world. The United States continues to express its concern about the export restrictions that Ukraine imposed on food and feed grain exports beginning in September 2006. Ukraine readjusted the export restrictions in July, imposing highly-restrictive quotas that served as a near export ban on each grain type covered (wheat, barley, corn, and rye). Ukraine plans to introduce somewhat more liberal quotas in January, 2008, allowing more grain to be exported until April 2008. The measure will allow traders to clear some stocks, but the level is approximately one-third of what could be exported. To date, Ukraine has not adequately justified the measures taken, *i.e.*, it has not convincingly explained how it faces a "critical shortage," as required in order to maintain such a ban under Article XX of the GATT 1994. Several studies point to the contrary. The World Bank's November 2006 report titled "The Quotas on Grain Exports in Ukraine: ineffective, inefficient, and nontransparent" states that the introduction of the quota was not justified, as domestic grain supply was amply adequate to cover all domestic needs. Data from the Food and Agriculture Organization of the United Nations and industry confirm this finding. Further questions are raised by the scope of the measures: the quotas and licenses are also being applied to corn and barley, which are not being used for the production of bread in Ukraine, and to corn, barley, and wheat used as feedstock.

More recently, Ukraine has sometimes argued that export restrictions are needed to combat rising food prices. Ukraine has threatened to extend the export restrictions to sunflower oil in order to combat rising domestic prices of this product.

Industry reports that the initial mismanagement of the issuance of licenses compounded the problem, leaving a large volume of grain in storage in Ukraine's ports, where in some cases it deteriorated past the point where it could be used for human consumption, or even animal feedstock. The World Bank estimated that during the 2006/2007 marketing year the costs to grain traders of demurrage and losses from rotting or otherwise compromised grain that was not able to leave Ukraine's ports exceeded \$300 million. The Ukrainian economy is sustaining some of these losses, including lost export opportunities. These measures have tarnished Ukraine's investment climate and damaged its reputation as a reliable grain exporter and a country that upholds contracts. Ukraine has committed to remove its current quotas prior to becoming a WTO Member, and to apply any future restrictions in conformity with WTO provisions.

Live cattle, sheep, hides, and skins

Export duties have been in place on live cattle, sheep, hides, and skins since 1996. For live calves the duty is 75 percent of the customs value (but no less than 1500 euros/ton of live weight); for live cows it is 55 percent (but no less than 540 euros/ton of live weight); and for live sheep it is 50 percent (but no less than 390 euros/ton of live weight). For raw hides of cattle the duty is 30 percent (but no less than 400 euros/ton of live weight); for sheep hides it is 30 percent (but no less than 1 euro/hide); and for pigskins the duty is 27 percent (but no less than 170 euros/ton of live weight). In November 2006, Parliament enacted amendments to the law that will lower these export duties gradually upon WTO accession. Export duties on live calves, cows, and sheep will fall to 10 percent, 8 years after accession. Export duties on raw hides will fall to 20 percent, 10 years after Ukraine becomes a WTO Member.

Scrap Metal

Since January 2003, Ukraine has imposed an export duty of 30 euros/metric ton on ferrous steel scrap and has 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. Laws passed in the fall of 2006, and amended in May, provide for staged duty reductions to 10 euros/metric ton over a period of 6 years for ferrous metals and reductions to 15 percent *ad valorem* over a period of 5 years for nonferrous metals.

Sunflower Seeds

Sunflower seeds have been subject to an export duty since June 2001, to the benefit of local sunflower oil producers. In July 2005, the export duty on sunflower seeds was lowered to 16 percent of its customs value with further 1 percent annual reductions to be made upon WTO accession, reaching a final duty of 10 percent, 6 years after accession.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Recent years have seen steady improvement in Ukraine's protection of intellectual property rights, but problems remain. On January 23, 2006, the United States reinstated GSP benefits for

Ukraine and lowered Ukraine's designation under Special 301 from Priority Foreign Country to Priority Watch List. Also in January 2006, Ukraine agreed to work with the U.S. Government and with U.S. and domestic industry to monitor the progress of future enforcement efforts through the IPR Enforcement Cooperation Group. This bilateral group has conducted a series of successful dialogues, meeting roughly once every 4 months, throughout 2007. Ukraine has also agreed to meet biannually with European Commission officials as part of an EU-Ukraine IP Dialogue.

Optical Media

Despite the significant reduction of illegal production of optical discs, the retail sale of copyrighted goods in large markets – especially Kyiv's well-known Petrivka market and similar markets in other large cities – is still widespread. The transit of pirated goods also remains a serious problem.

Internet Piracy

Internet piracy is a growing problem in Ukraine. Industry states that many Ukraine-based websites offer pirated material for download with the full knowledge of their Internet Service Providers (ISPs). The United States continues to work with the Ukrainian government to monitor and combat the spread of illegal download websites, and, at one meeting of the IPR Enforcement Cooperation Group, GOU officials agreed to begin monitoring suspected pirate sites jointly with industry.

Royalty Collecting Societies

Rights holders have complained repeatedly that some royalty collecting societies collect fees for public use of copyrighted material without authorization and do not properly return royalty payments to rights holders. An initial draft amendment to the Copyright Law failed to address industry concerns, and the draft is now being reworked.

Additional IPR Efforts

Ukraine has made some important revisions to its IPR laws as part of the WTO accession process. Parliament passed amendments to its Customs Code in November 2006 that provide customs officials the ability to use *ex officio* authority to seize suspected pirated or counterfeit goods. Parliament also passed a law amending the Civil and Criminal Codes of Ukraine in order to provide for the seizure and destruction of IPR-infringing goods and equipment, in line with Article 46 of WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS).

As a result of commitments agreed to as part of its March 2006 WTO bilateral Market Access Agreement with the United States, Ukraine amended its law "On Medicinal Drugs" in November 2006 to provide a 5 year period for the protection of pharmaceutical test data that is submitted to government authorities to obtain marketing approval. The Ministry of Health issued a regulatory act to ensure implementation of this law and to clarify some procedures. Pharmaceutical industry representatives complain that implementation of the law remains a problem, however. Parliament also passed an amendment to the law "On Pesticides and Agrochemicals" in November 2006 that provides a 10 year period of protection for agricultural chemicals. In September, the Cabinet of Ministers issued a regulation to abolish discriminatory fees on the testing and registration of plant varieties.

Parliament also passed an amendment to the law “On Protection of Rights for Indications of Origin of Goods” in November 2006, but Ukraine recognizes that further amendments are necessary in light of TRIPS provisions.

Patent and Trademark

Trademarked and copyrighted goods must be registered for a fee in the Customs Service’s rights holder database in order to be guaranteed protection. Industry has reported instances of production of counterfeit cigarettes within Ukraine as well as growth in the amount of counterfeit pesticides and apparel on the market.

The Ukrainian Ministry of Health does not routinely check the validity of patents when it grants marketing approval in Ukraine.

In 2006, Ukraine adopted the Singapore Treaty on the Law of Trademarks aiming at establishing a uniform mechanism for administrative trademark registration.

Judicial System

Civil IPR lawsuits remain rare because of a general lack of confidence in Ukraine’s legal system, and because there are few judges properly trained in IPR law. However, a recording company won a landmark civil court case against the Ukrainian music download site www.mp3.ua. The court ruling imposed substantive penalties on the owners of [mp3.ua](http://www.mp3.ua) and was subsequently upheld on appeal. February 2006 amendments to the Criminal Code drastically lowered the required threshold (from roughly \$5,200 to \$700) needed to pursue criminal prosecution and increased penalties up to 7 years imprisonment for major offenders. The amendments have helped bolster criminal enforcement in the courts. The U.S. Government has worked closely with the Government of Ukraine to provide specialized IPR training.

SERVICES BARRIERS

Restrictions on services exist in areas such as insurance, banking activities, auditing, legal services, television and radio broadcasting, and information agencies. During bilateral negotiations on services market access with a number of countries in the context of Ukraine’s negotiations to join the WTO, Ukraine agreed to open access for foreign service suppliers in a number of areas, including energy services, banking and insurance branches, professional services, express delivery, and telecommunications. When these commitments are fully implemented, Ukraine will have one of the most liberal services markets in the region.

In 2005, Parliament adopted legislation that will, within 5 years after Ukraine becomes a WTO Member, permit foreign insurance companies to open subsidiaries in Ukraine. In the fall of 2006, it adopted amendments to the law on “Banks and Banking” that would permit foreign banks to open subsidiaries and branches, a law “On Advocacy” that eliminates the nationality requirements for legal services, and amendments to the law “On Publishing” that will cancel limitations on foreign investment in publication services over a 5 year transition period. In May 2007, Parliament amended the law “On Insurance” to allow for unrestricted reinsurance of risks related to waterway transportation, commercial aviation, and space launch (including satellites) from the date of WTO accession.

Foreign professionals are permitted to work in Ukraine, but a lack of transparency hinders foreign access to the Ukrainian services market. A local content requirement exists for radio and

television broadcasting, although it has not been stringently enforced in most cases. All foreign films are required to be dubbed or subtitled in Ukrainian.

In 2006, U.S. industry identified efforts to limit the ability of foreign credit and debit card service providers to provide their services to clients of national electronic payments systems as a significant barrier to trade. When Ukraine becomes a WTO Member, it must take on services commitments in the context of WTO negotiations to maintain an open and competitive banking system, including with respect to credit and debit cards, with full market access to electronic payments services. At present, Ukraine applies no formal restrictions. The United States continues to monitor Ukraine's actions in this important area.

INVESTMENT BARRIERS

The government is working to streamline regulations and eliminate duplicative and confusing laws regarding investment and business. In 2005, Ukraine created several agencies in order to attract investment to Ukraine, including the State Center for Foreign Investment Promotion (known as InvestUkraine) and the State Agency for Investment and Innovation. In 2007, the Cabinet of Ministers of Ukraine created the Council of Investors, a government advisory body, and the Committee for Modernization of the Investment Environment and Development of Capital Markets Infrastructure, to be chaired by the Minister of Finance.

The United States has a bilateral investment treaty (BIT) with Ukraine, which took effect in 1996. The BIT guarantees U.S. investors the better of national and MFN 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 a number of 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 of these cases under subsequent Ukrainian governments despite intensive advocacy by the United States.

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 recently ranked Ukraine 177th out of the 185 countries surveyed in terms of the ease of paying taxes. Ukraine currently 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 36.66 percent and 49.6 percent) that funds pension and social insurance programs. Many analysts single out the payroll tax as being exceptionally high and the main reason why shadow wage payments remain common in Ukraine.

Arrears in the payment of VAT refunds to exporters have also been a serious problem. Ukraine decreased the pace of VAT refunds beginning in August 2006, reimbursing only 76 percent of verified claims, down from 87 percent refunded in 2005. VAT refund problems continued in 2007, leading to calls for an overhaul of the VAT reimbursement mechanism. Industry claims that delays in reimbursements create opportunities for tax officials to demand kickbacks in return for quicker processing of rebates, and several companies reported being approached by "middlemen" who claimed that, for a fee, they could speed up the reimbursement process. Currently, the process for obtaining a refund of VAT payments can take from 3 to 18 months for foreign companies. Increasingly, the delays in reimbursement are becoming an important cost factor for many foreign companies and are seriously affecting the profitability of planned

investments. Foreign companies have the right to use promissory notes for the payment of VAT on inputs to goods destined for export.

Foreign investors complain that the tax regime for nonresidents' representative offices is discriminatory. Funds transferred from a company's foreign home office to its representative office in Ukraine as part of the latter's operational expenses are taxed, while funds transferred from one office to another within Ukraine are not.

Special Economic Zones (SEZs)

Ukraine has in the past maintained two forms of special economic zones (SEZs): Free Economic Zones (FEZs) and Priority Development Territories (PDTs). In April 2005, Ukraine canceled all tax exemptions (*i.e.*, from land tax, corporate income tax, import duty, and VAT on imports) to investors in all SEZs to stop large-scale misuse of these zones for tax evasion and smuggling. While the step reduced corruption and expanded the tax base, the abrupt cancellation of privileges and lack of compensatory provisions caused losses to some legitimate investors. In November 2005, the Parliament adopted legislation to create technology parks, providing for some government financial support, targeted subsidies, and tax privileges for a list of 16 technoparks based on existing scientific and research institutes. At the end of 2006, the Ukrainian government announced its intention to renew tax privileges granted to businesses operating in some SEZs and to introduce a compensation mechanism for investors, but a draft law on the subject never went forward.

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. As of September 2007, revenues from privatization were only 15.4 percent (\$320 million) of the fiscal year's target. 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.

The few privatizations that took place in 2007 were often marked by controversy. In March, the State Property Fund sold a majority share in Luganskteplovoz (a Ukrainian locomotive manufacturer) to Russian-owned CJSC Bryansk Machine Building Plant. Only two related bidders were able to meet the tender requirements as set by the State Property Fund, and the Fund may also have violated rules governing the announcement of the tender, making it impossible for potential investors to learn of the tender in time to submit bids. The President of Ukraine has appealed the decision in court, claiming noncompetitiveness and lack of transparency in the sale.

In August 2007, the state sold a 28 percent stake in Dniproenergo, a regional electricity distributor, to the Donbas Fuel and Energy Company (DTEK), owned by a Member of Parliament in the ruling coalition. The sale was conducted as a controversial debt-for-shares swap, whereby DTEK acquired the shares in exchange for covering a debt owed by Dniproenergo to coal suppliers. Some experts claimed that DTEK acquired the shares in Dniproenergo for only 30 percent to 40 percent of the market value.

In August, Ukraine announced its intention to move forward with the long-awaited privatization of the Odesa Portside Plant, one of Ukraine's largest chemical producers. The State Property Fund canceled the tender in October, however, after the President complained that the tender plan failed to include environmental safety provisions and could allow the formation of a monopoly in the sector.

Ukraine's Parliament amended the Land Code of Ukraine in October 2006, extending a moratorium on the sale of farmland until January 1, 2008. 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. As of October 2007, Ukraine had failed to adopt new legislation necessary to open the land market. As a result, the ban on the sale of agricultural land may be prolonged again.

Corporate Hijacking

Ukraine is currently experiencing an escalation in corporate hijacking activity. Some researchers claim that as many as 2,500 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 deficient legislation, corrupt courts, and a weak regulatory system to gain control of companies 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 limited steps to address it, convening a special state commission in January. In May, Parliament passed in the first reading a draft law "On Joint Stock Companies," considered critical to stopping corporate hijacking, but a protracted political crisis prevented the law from moving forward.

ELECTRONIC COMMERCE

Electronic commerce is underdeveloped in Ukraine, particularly in the areas outside of Kyiv. Experts estimate that active Internet users number about 12.1 percent of the total population. There is a higher level of usage in Kyiv, which accounts for 61.4 percent of all Internet users, and where Internet commerce, while small in total volume, is experiencing strong annual growth. The National Council on Communications is entrusted with monitoring the telecommunications market. The Internet in Ukraine remains mostly unregulated.

OTHER BARRIERS

Inspections

Industry asserts that the frequency of inspections by regulatory agencies is one of the major hindrances to business development in Ukraine. The annual number of inspections conducted throughout the country exceeds 1.5 million. According to a recent study, 57 percent of the private businesses in Ukraine consider inspections to be unclear, complicated, and nontransparent. Ukraine's system of inspections does not fulfill its main purpose of preventing legal abuses, but is primarily punitive in nature. Parliament adopted a new law in June 2007 "On the Fundamentals of State Monitoring (Control) over Economic Activity," which provides for additional inspections and investigations of economic activities, and may worsen the situation. There is also a proposal in the new draft Tax Code to expand the authority of the State Tax Administration so that it could conduct on-site, unplanned inspections of companies and would

no longer need a court order to obtain financial, economic, and accounting reports of audited companies. This proposed change to the Tax Code has not yet been adopted, however.