UKRAINE

TRADE SUMMARY

The U.S. goods trade surplus with Ukraine was $262 million in 2010, a decrease of $130 million from 2009. U.S. goods exports in 2010 were up $1.3 billion, up 51.6 percent from the previous year. Corresponding U.S. imports from Ukraine were $1.1 billion, down 118.8 percent. Ukraine is currently the 68th largest export market for U.S. goods.

The stock of U.S. foreign direct investment (FDI) in Ukraine was $793 million in 2009 (latest data available), down from $912 million in 2008.

United States-Ukraine Trade and Investment Cooperation Agreement

The United States and Ukraine signed a 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, tax policy, and specific business disputes. 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 third time on October 13, 2010. At the third meeting, the two sides agreed to a wide-ranging action plan to improve the protection of intellectual property rights in Ukraine.

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 simple applied tariff rate which fell to an average of 4.6 percent, according to the WTO, down from the 4.95 percent in place after its accession to the World Trade Organization (WTO) in 2008. For agricultural goods, the average applied tariff rate is now 9.7 percent. For industrial goods the average applied rate is now 3.8 percent. Ukraine applies preferential tariff rates to imports from its 12 free trade agreement 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 produced in Ukraine, such as grains, poultry products, sugar, and vegetables such as carrots and potatoes.

Although Ukraine's MFN tariff rates are relatively low, the Ukraine State Customs Service (SCS) continues to assign higher customs values to U.S. imports, including to food and agricultural products and pharmaceuticals, than is declared in the import documentation. There are concerns on how the SCS is determining and/or calculating these values. For some shipments, it is alleged that the result is a customs valuation 100 percent higher than what was declared in the import documentation. Since customs valuation decisions are not published, this lack of transparency is problematic. Importers who have sought to appeal the assigned customs valuation have been instructed by the 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 U.S. Government has raised its concerns about these valuation practices, including at the 2010 Trade and Investment Council meeting.

Excise Duties

Ukraine applies excise duties to a limited set of goods, such as alcoholic beverages, un-filtered cigarettes, motor vehicles, and petroleum products. Excise duties apply equally to imported and domestically manufactured goods. While excise duties are mainly specific (fixed amount per quantity of product), in the case of tobacco products both specific and *ad valorem* rates are applied. High excise duties hinder U.S. exports of wine and grape spirits and automobiles to Ukraine. Import tariffs on automobiles were significantly reduced to implement commitments Ukraine made in the context of its WTO accession; however, the government has introduced a 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 reviewed and amended annually by the Cabinet of Ministers. In 2010, the list included printers' ink, paper with watermarks, optical media production inputs such as polycarbonate, pharmaceuticals, paints and lacquers, dyes, hygiene products, cosmetic products, pedicure and manicure products, shaving aerosols and deodorants, lubricants, waxes, shoe polishes, insecticides, solvents, silicone, fire extinguishers and the chemicals that fill extinguishers, refrigerators and freezers, air-conditioners, humidifiers, and other selected industrial chemical products.

While these import licenses 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 results in 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 June 2010, the Chief State Inspector of the Veterinary Service of Ukraine canceled the authority of regional veterinary offices to issue permits for imports. Since this decision, U.S. and other exporters have faced substantial delays and difficulties in obtaining permits to import meat products. In 2008, the Ministry of Environment significantly tightened procedures for obtaining its approval to import goods that are potentially ozone-depleting. The stricter procedures continue to delay 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 years 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 party to the WTO Agreement on Government Procurement (GPA), but became an observer to the WTO Committee on Government Procurement in February 2009. While Ukraine committed to initiate negotiations for GPA membership within two years of its WTO accession, negotiations have not begun. Ukraine is reportedly preparing its initial offer to begin the process of GPA accession.

In July 2010, Ukraine passed a new government procurement law. The U.S. government, coordinating with the World Bank and other international donors, provided technical assistance during the drafting process and presented a strong message to the Government of Ukraine about the need to enact a law that met international standards. The U.S. government will continue to pay close attention to current attempts to amend the law to ensure that such attempts do not undermine its provisions.

The newly adopted law, which is now in force, requires that all government procurement of goods and services valued at more than UAH 100,000 (approximately $12,500) and public works valued at more than UAH 300,000 (approximately $38,000) must be procured through competitive tenders. Open international tenders are used where procurement is financed by an entity outside of Ukraine. The Anti-Monopoly Committee of Ukraine has the power to review disputes arising from public procurements, but that Committee has not yet been set up. Courts may also hear government procurement-related cases. Cases must be filed on tight timelines, often within 14 days of the alleged violation.

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 total procurements. Among the problems faced by foreign firms are: (1) the lack of public notice of tender rules and requirements; (2) non-transparent 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. The use of mechanisms such as, “bids with limited participation” has been eliminated.

EXPORT BARRIERS

Exports of some categories of products are subject to registration by the Ministry of Economic Development and Trade. Products that must receive a license prior to export from Ukraine include precious metals and stones, cast iron, ferronickel, ferrotitanium, ferroalloys, steel, copper, aluminum alloys, lead, some metallurgy equipment, unrefined oil and gas, scrap metal, printers’ 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.

Export Restrictions on Grains and Sunflower Oil/Seeds

Ukraine ranks among the top grain exporters in the world, but has periodically resorted to grain export restrictions. The supply of products deemed “socially important” (*e.g.*, vegetable oil, bread, and sugar) is controlled by the government.

Ukraine’s major grain exporters, which include a number of U.S. companies, have experienced severe difficulty exporting grain since July 2010. Initially, Ukraine imposed non-transparent and burdensome testing requirements on grain shipments, essentially closing off exports. The Government of Ukraine then announced the introduction of grain export quotas in October 2010. U.S. companies have complained that these grain export quotas were allocated starting on November 12, 2010, in a non-transparent and arbitrary process that resulted in their exclusion, along with a number of other non-Ukrainian companies, from the quota allocation process. Grain export quotas are currently in force through March 31, 2011.

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

Upon WTO accession, Ukraine lowered duties on ferrous scrap exports to 25 Euros/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. According to Ukrainian law, the export duty in 2010 for ferrous metals is 16.4 Euros/ton and 24 percent *ad valorem* 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 2010 Special 301 Report. Key concerns cited in the report included weak enforcement, widespread retail piracy, the transshipment of pirated and counterfeit goods, internet piracy, the continued government use of illegal software, and inefficiencies in the judicial system. The need to improve protection of intellectual property was a major theme of the bilateral 2010 Trade and Investment Council meeting, during which the two sides agreed to an IPR Action Plan. Matters addressed in the plan include, *inter alia*, public awareness, strengthened enforcement, and needed legislative improvements. Additionally, the Plan identifies measures to transition government ministries to legal software. The Government of Ukraine formally adopted the IPR plan in February 2011.

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 SCS Order #900 stated that duties for audiovisual products will be assessed on projected royalties rather than on the underlying carrier medium.

Financial Services

The United States continues to monitor Ukraine's actions 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. Parliament is also considering new legislation that would require all hryvnia-denominated electronic financial transactions to be resolved within Ukraine, at processing centers operated by the National Bank of Ukraine. This proposed change could increase costs and reduce the reliability of transactions, as well as restrict the ability of foreign firms to compete against local service providers.

INVESTMENT BARRIERS

The Ukrainian Center for Foreign Investment Promotion (known as InvestUkraine) is charged with helping attract foreign investment to the country. The Government of Ukraine continues to have an advisory body composed of representatives from foreign and domestic companies to advise the President 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, and several new, U.S. company investment disputes. In most cases, there has been little progress toward resolution despite advocacy by the United States.

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. OPIC is now actively providing 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. Ukraine maintains a corporate profit tax (25 percent, which is scheduled to drop to 16 percent by 2014), a personal income tax (flat rate of 15 percent, scheduled to rise to 17 percent by 2014), 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. Ukraine has adopted a new tax code. While many aspects of the new Code improve on the old taxation system, U.S. companies have raised concerns that the new Code will impact negatively those companies involved in direct selling due to changes in the criteria for those subject to the simplified tax system.

In recent years, delays in the payment of VAT refunds to exporters have also been a problem. While the Government of Ukraine finally refunded a large proportion of VAT refund arrears through a VAT bond scheme in August 2010 (some of these claims had been pending for over two years), the manner in which refunds were distributed was not transparent and the firms complained that they should have received cash rather than bonds. Additionally, some companies received reduced refunds or were refused refunds for arbitrary reasons. While the government stated its intention to introduce a comprehensive electronic system to ensure rapid, automated refunds by the start of 2011, little action has yet been taken in this direction and arrears continue to build. 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 that the terms of a privatization contest are arbitrarily adjusted to fit the characteristics of a pre-selected bidder. Few major new privatizations have been conducted since the privatization rush of 2004. In 2010, the State Property Fund attempted to revoke the privatization of the Krivorizhstal factory (now named Arcelor Mittal Kryvyi Rih), claiming that Mittal Steel had failed to meet its contractual obligations. Ukraine's Commercial Court considered the case and ruled that the government had no basis to reclaim the facility.

No major privatizations took place in 2010, largely due to disagreements over the privatization process. The government announced in May 2010 that it would privatize Ukrtelekom (the State telecommunications company) before the end of the year, with a starting bid of UAH 10 billion. However, the majority of potential bidders dropped out after the bidding floor was set, leaving an Austrian firm as the sole bidder. An auditing firm, contracted to assess the fair market value of Ukrtelekom, announced on February 20, 2011 that the company should be valued at 10.575 billion hryvnias. The sale is scheduled to proceed with this valuation estimate serving as the purchase price. The State Property Fund has also identified the Kryvorizhskyy Ore Mining and Processing Plant, and Turboatom (a producer of turbines for power plants), as priorities for privatization, but neither has moved forward. Other attempts at privatization in recent years were often marked by controversy.

The government has also announced its intention to privatize all of the 112 coal mines still owned by the government in 2011. There are concerns that a few Ukrainian and Russian firms are trying to acquire these mines without going through a fair, transparent privatization process. Industry analysts dismissed the announcement, as similar proclamations have been made in previous years without results. They believe that the majority of the state-owned mines are no longer economically productive, and would need to be bundled with other assets to attract investor interest.

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 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” to help stop corporate hijacking. Companies must fully comply with the law, which is considered to be an improvement in the corporate governance regime, by April 30, 2011.