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**Regulatory Policy in Ukraine: Current State  
and What Should be Done to Improve the Business  
Environment**

*Warsaw, April 2006*

Materials published here have a working paper character. They can be subject to further publication. The views and opinions expressed here reflect the author(s) point of view and not necessarily those of CASE.

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## **Abstract**

The regulatory environment for businesses in Ukraine has been considered unfavorable and market unfriendly. Although various governments have made numerous efforts to improve it, many of these attempts have failed and increasing the quality of the regulatory environment in the country still remains on the agenda of the government. With this report we claim to review a set of measures undertaken in Ukraine after the Orange Revolution in the area of deregulation of business activity. The paper analyzes the effectiveness of actions undertaken in Ukraine in a general framework of successful regulatory policies implemented in other parts of the world. Based on this analysis we developed concrete public policy measures aiming to increase the quality of the regulatory environment in the country, which, in turn, should secure Ukraine's further movement toward a real, functioning market economy.

## Introduction

The regulatory environment for business in Ukraine has for many years been perceived as an unfavorable one. This conclusion has been made in a number of studies undertaken in the late 1990s and in this decade.<sup>1</sup> In comparative cross-country analyzes, Ukraine has also been frequently evaluated as a difficult place to do business. For example, according to the Heritage Foundation Index of Economic Freedom, computed annually since 1995, Ukraine belongs to the group of mostly unfree economies and has been placed close to the end of the list of economies ranked according to decreasing levels of economic freedom<sup>2</sup>. The small size of the SME sector in Ukraine seemed to be yet another piece of strong evidence of the overregulation of the Ukrainian economy. For example, the share of small enterprises in the total production of industry was only 2.9% in 2000.<sup>3</sup> The large size of the gray economy in Ukraine has been an additional indicator of the unfriendly regulatory environment. Moreover, overregulation and poor regulation create incentives and make room for corruption. According to the Transparency International Corruption Perception Index (CPI)<sup>4</sup>, Ukraine has been perceived as a very corrupt country<sup>5</sup>.

The various Ukrainian governments have made numerous efforts to improve the regulatory environment, and these efforts gained momentum in the years 2001-2003 when many programs on deregulation were launched. Despite all these efforts, which were

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<sup>1</sup> See for example IFC (1997); Tegipko (1999); Institute of Competitive Society (2002); Nashchekina and Timoshenkov (2003). Also Quarterly *Enterprise Survey* prepared since August 2002 by the Institute for Economic Research and Policy Consulting in Kiev and available at [http://www.ier.kiev.ua/English/qes\\_eng.cgi](http://www.ier.kiev.ua/English/qes_eng.cgi).

<sup>2</sup> The results and the methodology of the assessment can be found at the Heritage Foundation's website: [www.heritage.org](http://www.heritage.org)

<sup>3</sup> State Statistics Committee (2005). According to the *Law on Enterprises* in Ukraine, manufacturing (and construction) enterprises are classified as small when they employ less than 200 people. In other sectors this limit varies from 15 employees in retail trade to 100 employees in science. In this respect Ukraine differs from the EU where the limit for a small enterprise is 50 workers and a company employing above 50 people and up to 250 is classified as medium-sized. Unfortunately, differences in statistical criteria make a genuine comparison impossible. Knowing, however, the Ukrainian definition of small enterprise, it is fair to say that in Ukraine's manufacturing sector big enterprises dominate, while in the EU member states the SME sector does.

<sup>4</sup> See [www.transparency.org/policy\\_and\\_research/surveys\\_indeces/cpi](http://www.transparency.org/policy_and_research/surveys_indeces/cpi)

<sup>5</sup> The score for Ukraine has been in the range of 2.6 in 1999 and 2.4 in 2002 on the scale 0 – 10, where 0-highly corrupt, 10-highly clean.

discussed in the Blue Ribbon Commission's report for Ukraine published in early 2005<sup>6</sup>, the business climate has remained unfriendly and uncompetitive as compared to what investors find in the majority of market economies. In January 2005 Ukraine was listed only 124th in a ranking of ease of doing business encompassing a total of 155 countries<sup>7</sup>. Domestic and foreign entrepreneurs continued to complain about the administrative burden imposed on them<sup>8</sup>. This is one of the explanations as to why the contribution of small enterprises to manufacturing sector production remained small<sup>9</sup>. The gray economy, conversely, has remained large and by the estimates of the Ukrainian Ministry of Economy accounted for 34% GDP in 2004.<sup>10</sup> Corruption marginally decreased but was still perceived as high<sup>11</sup>.

The objective of this paper is to review regulatory policy and deregulation measures undertaken in Ukraine after the Orange Revolution and aimed at improving the environment for business in the country and thus enhancing entrepreneurship. We start with a brief theoretical discussion about regulation and why governments impose it (Section 1). Then we list problems that regulation creates, though its rationale is to solve specific economic and social problems that emerge in market economies; we also discuss how economic theory explains the origin of these deficiencies. This brings us to Section 2, where we make a brief presentation of the international experience in improving business regulation through undertaking deregulation actions and incorporating basic rules with regard to the creation and execution of business regulation into the everyday practice of governments. The first two sections (1 and 2) provide a good framework and context to discuss the current state of the business regulatory environment in Ukraine as well as to evaluate the regulatory policy of the Ukrainian government in recent years, which are the topics of Sections 3 and 4. The lessons learnt from a number of developed countries that have furthest deregulated their economies, are used to make recommendations for Ukraine on further deregulation as well as on improving the quality of law creation. These recommendations are presented in Section 4 and are divided by problems that are discussed in the subsequent sub-sections.

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<sup>6</sup> Proposal for the President: A New Wave of Reform, Blue Ribbon Commission for Ukraine, Kiev 2005, <http://www.carnegieendowment.org/files/BRCReport121204Eng2.pdf>

<sup>7</sup> World Bank and IFC (2006). *Doing Business in 2006. Creating Jobs.*

<sup>8</sup> See: UCIPR, CIPE, and ICS (2005), *The business climate in Ukraine: the Current Situation and Expectations*. Survey of Business Associations; Ernst & Young (2005). *Doing Business in Ukraine*; IFC (2004), *Business Environment in Ukraine*; Palianytsia (2004). *Business Environment Study Ukraine*.

<sup>9</sup> In fact this further decreased, accounting for 2.4% in 2004, see: State Statistics Committee (2005).

<sup>10</sup> Ministry of Economy (2005). *Tendencies in the shadow sector of the economy*, available at [http://me.kmu.gov.ua/control/uk/publish/article?art\\_id=48658&cat\\_id=38737](http://me.kmu.gov.ua/control/uk/publish/article?art_id=48658&cat_id=38737)

<sup>11</sup> In 2004 CPI was 2.6. See [www.transparency.org/policy\\_and\\_research/surveys\\_indecis/cpi/2005](http://www.transparency.org/policy_and_research/surveys_indecis/cpi/2005). The problem of corruption is investigated in detail in Dubrovskiy (2006).

# 1. What economic theory says about regulation

## 1.1. What regulation is and why it is imposed

The importance of economic freedom for economic growth and the wealth of the nation had been raised and discussed in detail by the father of modern economics, Adam Smith, in his famous work *An Inquiry into the Nature and Causes of the Wealth of the Nations*, published for the first time in 1776. Such a perception of economic freedom has been further elaborated by other classical economists, the Austrian school, and in the 20th century by Friedrich von Hayek and Milton Friedman.

An important element of economic freedom is free entry into the market and free exit from the market. It has been theoretically proven that these two fundamental mechanisms make markets competitive. They will ensure that the more efficient firms, and those producing in line with market demand, survive and prosper, while inefficient units will contract and eventually embark on exit. Free entry and competitors discipline enterprises and force them to decrease costs and introduce technological innovations and new products. Recent developments in the theory of industrial organization have clearly established that the presence of free entry and free exit by itself imposes a discipline on incumbent firms and forces them to behave as if these rivals have already entered the market, ensuring an improvement in the allocation of resources and the overall welfare.<sup>12</sup>

Therefore, the basic question is why governments impose limitations to economic freedom by introducing and executing administrative constraints to individuals and entities starting or running business activities. This is what economic literature calls regulation. The fundamental rationale for government's intervention is the existence of market failure: the free operation of market forces results in a greater (or lesser) than optimum level of output in activities with negative (or positive) externalities. Negative externalities include environmental pollution, unemployment (caused by technological change, etc), asymmetric information, barriers to entry, increasing returns, etc. It is the public interest theory, originating from Arthur Pigou's work *The Economics of Welfare*, that highlighted the need for government to limit economic freedom as to maximize social welfare. The same theory implies that governments can effectively compensate for the impact of market failure caused by externalities. The public interest theory made room and justified the creation and operation of industrial, trade and entrepreneurship policies.

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<sup>12</sup> The theory of *Contestable Markets* by Baumol, Panzar and Willig (1988).



## 1.2. Regulation in practice: why the remedy creates problems

Economists who contributed to the so-called new theory of growth<sup>13</sup> proved, with the use of statistical tests, that high growth rates are positively correlated with a high scope of openness of the country, i.e. with free trade (e.g. Baldwin 1992) and the protection of property rights, and negatively with different forms of administrative regulation (e.g. Barro and Sala-i-Martin 1995).

The empirical research on regulation shows that the way in which government plays its role of imposing and enforcing regulation is of vital importance.

First, there is strong theoretical and empirical evidence that administrative constraints imposed on business impact the scope of economic activities undertaken by entrepreneurs and the macroeconomic performance of the country.

The economic literature has also elaborated on the impact of barriers to entry on technical and allocative efficiency and consumer welfare (Bain, 1968; Stigler, 1968; Von Witzsacker, 1980; Demsetz, 1982).

For the business community, regulation brings about compliance costs: administrative and paperwork costs that are necessary to meet government requirements. In Sweden, which ranks high in the World Bank ranking of ease of doing business for 2005,<sup>14</sup> some six years earlier compliance costs were conservatively estimated at SEK 50 billion (see: NNR, 2002, p. 1).

Debate on the public interest theory has also led to the formulation of alternative explanations for government intervention, including the regulatory capture theory and the theory of rent seeking society. According to the capture theory, economic regulation is introduced at the behest of the regulated sector of the economy, and that it is this sector, and not the public, that benefits from state intervention. In the 1970s economic theory of regulation (also known as interest group theory of regulation) offered an explanation for why a regulatory institution will be captured by producers at the expense of consumers; it is because the latter are worse organized and for them collecting funds for lobbying is much more difficult than for producers (Stigler, 1971; Peltzman, 1976), or by one pressure group against others competing for privileges rationed by the state (Becker, 1983). Much attention was placed on an analysis of the costs of government regulation born by the society and generated by rent-seeking entrepreneurs. They capture a regulatory institution and make it introduce regulation friendly to them and at the expense of consumers, or entrants, or foreign

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<sup>13</sup> Its creation had been initiated by Paul Romer in 1983, whose paper entitled *Increasing returns and long term growth* questioned the assumptions of Solow's theory of growth, which had dominated since the 1960s.

<sup>14</sup> Sweden was 15<sup>th</sup> in the ranking that encompasses 155 countries, see: World Bank and IFC (2006).

investors. The social costs of such rent-seeking emerge and the costs of lobbying for such regulation is a deadweight cost (Tullock 1996).

## **2. Key lessons from international experience on successful state regulatory policy**

The creation and practical implementation of effective regulation has been on the agenda of the group of most developed market economies over the last 30 years. This is due to a number of reasons. First, there has developed a strong and well-grounded consensus that it is business that creates jobs and economic growth and improves the welfare of a society. Second, there has been a growing understanding on the part of governments that the regulatory environment significantly affects the decisions of individual investors and enterprises, and that large administrative burdens imposed on business discourages entry into markets and curtails the growth of active companies. It has been widely recognized that compliance costs are a charge against the scarce resources of the private sector. Furthermore, the globalization of markets, increasing competition and growing international regulatory competitiveness, have contributed to an increased interest on the part of policy makers in improving the quality of business regulation, and, in particular, reducing unnecessary and undesirable administrative burdens to business.

This part of the paper discusses the international experience in improving business regulation and policy lessons gained. These lessons are used in Section 4 of the paper, where specific policy recommendations relevant for Ukraine are proposed.

How do governments actually go about creating better business regulation? National level approaches differ due to a number of factors like national history, administrative culture, etc. Therefore there is the potential for cross-cutting and cross-national learning. Below, experiences of the frontrunners in making regulation better are presented. Lessons learnt are divided into three areas. These areas are: (1) creation of regulation, (2) access of business to information on regulation (3) implementation of regulation.

## 2.1. Quality regulation: creation of good regulation

- Any law should be ex ante assessed to carefully examine how the proposed changes in regulation will affect the economy and welfare of the society. In fact, so called regulatory impact assessment (RIA) should be an integral part of the policy development process, in order to strengthen transparency and accountability in regulatory decision-making. RIA is an effective tool to deal with the most difficult challenges which governments face in regulatory decision-making and, in particular, to continue improving a country's economic competitiveness, ensuring that all government actions are consistent with market economy principles, and to continue to improve transparency in the decision-making process. One of the sub aims of this ex ante audit of regulation is to study and take into consideration the compliance cost of business regulation.

Assessment of the impact of regulation is an obligatory practice in many countries, including Western Europe, USA, Canada, and New Zealand. In New Zealand, with a long tradition of RIA preparation, a much stronger tendency to use ex ante assessments of new regulation has been observed from April 2001. Since then, all policy proposals submitted to the Cabinet of Ministers must be accompanied by a Regulatory Impact Statement (RIS) and Business Compliance Cost Statement (BCCS). RIS and BCCS are published and are included in the Explanatory Notes to bills submitted to the House of Commons.

RIA needs to be adopted by the government and the parliament as a self-constrained device and necessary instrument for high quality regulation. In case this commitment is weak, then RIA becomes a very formal and unimportant exercise. As a result, the idea of ex ante evaluation of intended changes in regulation is spoiled. This statement can be supported by an example from the Polish experience. In 2003, the Polish Cabinet of Ministers approved the methodology of preparing RIA and initiated the assessment of new laws proposed. However, neither the government nor the parliament were seriously concerned with the results of the RIAs, therefore the ex ante assessment of new laws became merely a formal procedure and findings were poor.

- It is important to provide a good institutional intragovernmental environment so as to produce quality regulation and to prepare quality RIA and BCCS.

Well-educated and trained staff is required if quality regulation is to be prepared. Moreover, this staff should be motivated to prepare good quality law and properly assess ex ante its impact, including business compliance costs. Important here is that an internal monitoring system is inevitable as to control the quality of work. In New Zealand, for example, a special unit has been established and placed in the Ministry of Economic Development. The task of this unit is to review the regulatory impact and business compliance costs statements prepared by governmental departments and to make comments whenever standards of analysis are not met. Besides controlling Business Compliance Costs, the unit also teaches how to improve these statements (see MED 2001). In addition, there has been a special education program for government departments to increase the recognition of compliance costs for business and to change approaches in policy planning so as to factor in concerns about the level of these costs.

- The results of regulatory impact assessments and, specifically, business compliance costs assessments need to be published.

RIAs and BCCSs should be published for the following reasons. First, publication of RIAs and BCCSs makes the public in general and business society in particular aware of proposed regulation, and gives them the opportunity to respond and to have a say regarding the cost of regulation. Second, publication of an ex ante regulation evaluation increases the government's accountability. Business society, in particular, and the public, in general, have better grounds for evaluation of government performance and may use this knowledge in the political process (voting). Third, publication of RIAs is also important for the improvement of their quality, as government agencies by nature try to minimize their work load and are inclined to regard regulation from a governmental perspective. A good example is Sweden, where 19 business organizations created in 2001 the Board of the Swedish Industry and Commerce for Better Regulation (NNR) with the task of studying the RIAs, revealing their weaknesses and communicating findings with the government (see NNR 2002). The report, published in May 2002 after reviewing some 150 recent RIAs and assessing them against 11 criteria jointly describing their quality, showed that impact statements were generally much below the standard expectation of being a genuine instrument of ex ante audit of regulation.

- In the process of creating and improving business-related regulation, partnerships with the business community should be used extensively.

Business advice should be sought so as to have first hand knowledge of costs born by enterprises to comply with regulation and so as to identify priorities in alleviating regulatory barriers to entry and growth of companies.

In Sweden, stakeholders are entitled (by law, and this applies to all governmental bodies that propose regulation as well as parliamentary commissions and committees) to express their opinions on proposed regulation, as well as the accompanying RIA (see NNR 2002).

## **2.2. Access to quality information about regulation**

- Business needs good quality and easily accessible information about regulation that is binding for entrepreneurs and companies. Easily accessed and clear information reduces the time, effort and cost necessary to find and comply with regulation and the risk and the costs of “getting it wrong”.

International experience suggests that those countries which provided entrepreneurs and companies with high quality information accessible 24-hours a day through e-technology made tremendous progress in their developments. Much effort and commitment in this direction has been shown by the governments of Australia, USA, Canada, and New Zealand. In these countries, governmental departments have developed and updated websites where they clearly present all information that is needed by businesses. In New Zealand, additionally, a one-stop business portal was created in 2001. Info lines provide assistance in cases where website info does not suffice.

## **2.3. Implementation of regulation**

- Enforcement of regulation should be consistent: to this end the law has to be clear so as to not leave room for different interpretations by implementing institutions
- Administrative capacity has to be in place: well-trained, well-motivated, well-supervised staff, with a customer-focused approach, is necessary
- Procedures need to be transparent and clear so as not to leave room for discretion on the part of the administration
- Forms should be plain and easy to use with electronic templates to be filled in by businesses
- Enforcement of regulation has to be monitored and followed up with revision
- On-line facilities for businesses should be introduced

On-line access to the institutions that implement regulation reduces substantially business costs in terms of both money and time.

On-line facilities are costly investments for the government but they pay back quickly. To enhance their use in some countries, governments introduced special incentives for businesses. In New Zealand, for example, the Companies Office (a companies register) introduced reduced rates for businesses settling their affairs on-line (MED 2001).

- Administrative charges for business need to be reasonably low so as not to create a barrier to the entry and growth of companies

### 3. Regulatory policy in Ukraine in 2005

Starting from the beginning of 2005, the President and the Government have undertaken a number of serious actions aimed at improving the regulatory environment in order to enhance the development of private business. These actions are briefly discussed below. They have focused on increasing the quality of law through improving regulatory impact analysis, the elimination of some redundant or distortive legal acts, securing stakeholders' consultations, and improving laws regulating permissions and inspections. However, some of these steps did not bring the expected results, owing to a number of reasons to be discussed in Section 4 of this paper.

(1) On 12 May, 2005 Presidential Decree (#779/2005) on Liberalization of Entrepreneurial Activity and State Support to Entrepreneurship was issued<sup>15</sup>. It requires that (i) all government agencies review all their regulatory acts and bring them into compliance with article #4 of the law on On the Main Principles of State Regulatory Policy in the Sphere of Economic Activity of September 11, 2003<sup>16</sup>; (ii) all government agencies increase transparency in regulatory policy and improve access to information on regulation of economic activity; (iii) the Cabinet of Ministers prepares and submits to the Parliament (a) a draft law on the unified social tax, (b) a draft law on the permission system for business, (c) amendments to the Law on Licensing of Some Types of Economic Activity, which should decrease the number of activities required to be licensed, (d) amendments to the Law on Profit Tax and Law on Value Added Tax, which should decrease the tax pressure on enterprises by decreasing tax rates; (iv) secures an increase in 2006 budget expenditures for

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<sup>15</sup> The text of the Decree is available at: <http://www.president.gov.ua/documents/2340.html>

<sup>16</sup> Find this at <http://zakon.rada.gov.ua/cgi-bin/laws/main.cgi>. Article 4 concerns principles of the state regulatory policy and defines them as (i) advisability, (ii) adequacy, (iii) effectiveness, (iv) equilibrium, (v) predictability, (vi) transparency and public participation.

the national program on supporting small business development; (v) introduces a “national concept” of developing “administrative services”. The last requirement is rather a vague one.

(2) Presidential Decree #901/2005 concerning state regulatory policy On Some Measures on Securing Implementation of the State Regulatory Policy was issued on 1 June 2005.<sup>17</sup> It requires (i) improvement of qualifications of the state regulatory bodies’ staff through special training programs. Pointing out the importance of the qualifications of the public administration, the Decree has only signaled intention and has left room for government action to this end.

The Decree also asks for (ii) the development of a concept of regulatory impact assessment (RIA). The decree does not specify, however, which spheres it relates to and it is vague. Moreover, RIA has been introduced as a general requirement for all regulatory acts by the 2003 Law On the Main Principles of State Policy in the Sphere of Economic Activity (article 5). Finally, the President requested (iii) a review of all regulatory acts issued by government bodies with the goal of bringing them into compliance with the principles set forth in the Law on the Main Principles of State Regulatory Policy in the Sphere of Economic Activity. In opposition to the previous Decree of May 2005, which had already called for such an action (see point 1 above), this decree was very detailed at this point. Special working groups were to be formed. To increase public awareness of the government’s action and to secure high quality work, the decree envisaged the inclusion of representatives of the stakeholders into working groups and offered them a 50% quota of the seats in such task groups. Based on the recommendations of the working group, the Ministry of Justice was expected to take the decision on reviewed acts before the 45th day after the beginning of the review process. Therefore, it was expected that the “cleaning procedures” would be undertaken in a fast track regime.

(3) On 6 September, 2005 the Ukrainian Parliament passed the Law on Permissions System in Business Activity.<sup>18</sup> The Law had been proposed by the Cabinet of Ministers in response to the President’s request expressed in the decree of 12 May (see point 1 above). The main goal of this law was to introduce clear, more unified and more transparent procedures for granting permits to private businesses and, as a consequence, to substantially decrease room for corruption. The Law specified clearly, as well, which types of activities are to be subject to permits. As a result, two thirds of the existing 1,200 permits were expected to be eliminated from 5 January 2006, when the Law was to enter into force.

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<sup>17</sup> Find this at: <http://www.president.gov.ua/documents/2754.html>

<sup>18</sup> Law No. 2806-IV; find this at: <http://zakon.rada.gov.ua>.

<sup>19</sup> For more details see official address of the Head of the State Committee of Regulatory Policy and Entrepreneurship on February 3, 2006, which is available at: [http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art\\_id=56143&cat\\_id=37571](http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art_id=56143&cat_id=37571)

(4) On November 24, 2005, and with reference to the two Resolutions of the National Security and Defense Council<sup>20</sup>, the President issued Decree #1648/2005<sup>21</sup>. The Decree, which deals with the investment climate, addresses issues related to regulatory policy and regulation. In particular, it requires that (i) within one month government bodies will review and introduce changes in the existing procedures and methodology for developing and evaluating new regulatory acts so as to put them in line with the requirements of the Law On the Main Principles of State Regulatory Policy in the Sphere of Economic Activity<sup>22</sup>; (ii) within one month the government will undertake measures aimed at reducing the length of registration for a new company to one day by introduction of a one-stop-shop system; (iii) concrete measures will be developed to conduct a reform of the tax system; (iv) the government will implement measures aimed at decreasing time limits for processing applications and issuing permits and lower administrative fees, especially those issued by the fire inspections and phitosanitary bodies; (v) the government will submit a proposal on transforming the State Committee for Regulatory Policy and Entrepreneurship into the National Commission of the country's executive body with a special status: supervised by the President and accountable to the Parliament.

(5) On 26 December 2005 a new order of information exchange between one-stop-registration offices and the Unified State Register was introduced. The provisions of a joint resolution issued by the State Committee for Regulatory Policy and Entrepreneurship and the Unified State Register<sup>23</sup> should contribute to reducing the time required to open a new business. The introduction of internet technologies and on-line registration should increase the level of transparency and prevent private entrepreneurs from possible abuses from the side of government officials.

(6) On 18 January 2006 the Cabinet of Ministers passed Resolution N-13-p on Measures on Implementation of the State Regulatory Policy in 2006.<sup>24</sup> This program envisages (i) an increase in the quality of regulation by introducing into the process of creation of regulatory acts a special mechanism: alternative approaches to reach goals targeted in the specific acts are to be assessed ex ante; (ii) introduction of permanent monitoring of the implementation of regulatory acts; (iii) providing regulatory bodies' staff with training programs specifically tailored to their tasks; (iv) increasing transparency and publicity

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<sup>20</sup> Resolution of June 29, 2005 on *Measures to improve Investment Climate in Ukraine* and resolution of October 28, 2005 on *Measures to Increase Efficiency of Private Property Rights Protection*.

<sup>21</sup> Find this at: <http://www.president.gov.ua/documents/3552.html>

<sup>22</sup> For more details see Article 3.10 of the Decree. Available also at <http://www.president.gov.ua/documents/3552.html>

<sup>23</sup> For more details see Press Release of the State Committee on Regulatory Policy and Entrepreneurship of November 11, 2005, which is available at:

[http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art\\_id=54581&cat\\_id=33037](http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art_id=54581&cat_id=33037)

<sup>24</sup> Find this at [http://www.kmu.gov.ua/control/uk/newsnpd?npdList\\_stind=161](http://www.kmu.gov.ua/control/uk/newsnpd?npdList_stind=161)



of the process of developing and passing business regulation; (v) an improvement in cooperation between the central and local administrative bodies on regulatory policy issues.

## **4. Results of the regulatory policy actions and unresolved issues**

Despite the efforts of the President and the government to improve regulatory policy, many issues still remain unresolved and should be part of the government agenda in the near future. The results of actions undertaken so far demonstrate that easing the administrative burden imposed on business is a very difficult, costly, and slow process. In the subsequent sub-sections we present the current state of affairs in a number of areas of regulation in Ukraine and formulate recommendations on how to deal with unfinished reforms.

### **4.1. Creation of regulation**

Ex ante assessment of regulation has been introduced in Ukraine by the Law On the Main Principles of State Regulatory Policy in the Sphere of Economic Activity which was passed on 11 September 2003. Article 5 of this law has determined that all regulatory acts have to be reviewed from the point of view of their possible impact on businesses, while Article 8 requests that a report from this review, which is a regulatory impact assessment (RIA), should include a cost-benefit analysis.

According to statistics compiled by the Council of Entrepreneurship of the Cabinet of Ministers, RIAs have been carried out for 81.7% of laws under preparation in 2004, and for 91.4% in 2005<sup>25</sup>. Taking into consideration these figures only, one has come to a positive picture: in the two years since RIA has been introduced in Ukraine as a mandated part of the lawmaking procedure, a majority of laws have been the subject of ex ante assessment and only less than 9% have not been reviewed.

This positive picture will change, however, when we take into consideration the content of RIAs. Their quality has proven to be far from satisfactory<sup>26</sup>. There are a number of reasons for this: (1) lack of understanding of the task and (2) inadequate skills of the staff performing assessments, which both stem from, (3) high staff turnover (among others

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<sup>25</sup> See the press release of the Council of Entrepreneurship of the Cabinet of Ministers available at <http://www.business-rada.kmu.org.ua/ua/news/337.html>

<sup>26</sup> The same source.

things). Yet another reason was (4) a lack of detailed guidelines concerning procedures and methodology to be applied when working on RIA. Last but not least, (5) inadequate supervision over units in charge of RIA should be mentioned here.

With regard to the last reason, it is important to notice that, according to Article 10 of the law, a government body drafting a regulatory act is also responsible for preparing its RIA and, finally, for monitoring law implementation.

Formally and institutionally, however, room has been created for external supervision over the quality of regulations and RIAs, which is a must in order to guarantee genuine and quality *ex ante* assessment of laws. The State Committee for Regulatory Policy and Entrepreneurship has been equipped with the power to review each regulatory act from the point of view of its compliance with the principles of regulatory policy adopted in Ukraine (Article 21 of the On the Main Principles of State Regulatory Policy in the Sphere of Economic Activity). This encompasses as well the monitoring of the quality of RIA.

All government bodies are obliged by law to submit to the Committee their regulatory act proposals together with RIAs. The Committee has the right to reject proposals if it finds that they do not meet the criteria stipulated by law, as well as to request that they be made compliant. Rejected regulatory act projects must go through the same procedure once again.

Since external supervision over preparing new regulations cannot be fully exercised by the State Committee, then the obvious conclusion is to remove the existing obstacles and give this body full monitoring power. The need for RIA is well recognized in Ukraine and there is also a conviction that the position of the Committee in this respect has to be strengthened. As has already been mentioned in Section 3, Presidential Decree #1648/2005 calls on the Government to develop a proposal on converting the State Committee for Regulatory Policy and Entrepreneurship into an executive body with a stronger position *vis-à-vis* other government agencies.

As has already been discussed in Section 2, the RIA results and, specifically, business compliance costs statements, for the sake of their quality, should be published. Therefore it is important that Article 9 of the Law on the Main Principles of State Regulatory Policy in the Sphere of Economic Activity states that each proposed regulatory act is to be exposed to public discussion. Moreover, public hearing is mandatory and, according to Article 8, should be complemented by the RIA. According to Article 13 of this law, the general public should be informed about prospective regulatory acts and their impact through media and government agencies' internet resources.

The practice of making the public informed about state policies *vis-à-vis* business is, however, still meager. As of January 23, 2006, only four central government bodies made publicly available information on their plans related to drafting regulatory acts for the current

year. These are the Ministry of Economy, the Ministry of Agrarian Policy, the Ministry of Transportation, and the Ministry of Finance. Other central government agencies do not present their plans and thus do not create room for the participation of civil society in the prospective discussions.

## **Recommendations**

1. Increase the quality of RIA so as to make it a genuine instrument for the government in the process of business law creation. To this aim a number of actions are necessary and they are listed below (see recommendations no. 2, 3, and 4).
2. Increase understanding of the objective of RIA and skills of the staff responsible for making assessments by introducing special training programs. The usual requirement to have a good incentive system for staff holds true. Namely, government officers responsible for supervising, as well as preparing, RIA need to know in advance that increases in their salaries and job promotions are related to their performance.
3. Detailed procedures and guidelines on how to prepare regulation impact assessment need to be worked out so as to give clear instructions to government staff and thus to ensure the quality of the RIA content.
4. A genuine external monitoring system over RIA preparation needs to be established. The department of regulatory policy that exists in the State Committee for Regulatory Policy and Entrepreneurship and is responsible for making economic and legal evaluations of regulatory acts needs to be strengthened. A special division should be created with its main task to exercise control over the quality of the work of the ministerial staff responsible for ex ante analysis of compliance costs of regulation to business. Besides the quality control of RIAs, this unit should be mandated with responsibility for preparing training programs for ministerial staff on how to approach and conduct assessments and on how to supervise the quality of training. This unit should also be used as a consultation center.
5. Make state regulatory policy transparent and accountable by ensuring that all government agencies make all information on regulatory acts drafts available to the public. This recommendation embraces also the advice that RIAs should be published.

## 4.2. Review of the regulation stock

The regulation stock in Ukraine is large, difficult to access, and non-transparent and therefore difficult and costly for businesses to comply with. Also some of it is not in use any longer and creates only confusion. Therefore, the action ordered by the Presidential Decree of June 2005 of reviewing regulation was an appropriate one and was welcomed by the business community. The working groups, comprised of administrative staff as well as representatives of the stakeholders; had a mandate to analyze regulatory acts issued by government bodies only, i.e. laws passed by the Parliament were not subject to this action since only the Parliament has the right to repeal them.

In the short period set up for the review, which has been commonly named the regulatory guillotine, 9,340 governmental regulatory acts were screened<sup>27</sup>, and slightly more than half of them<sup>28</sup> were considered to be noncompliant with the state regulatory principles and were requested to be either fully or partly abolished.<sup>29</sup> By 1st September 2005 94.5% of the work was completed<sup>30</sup> Over 1,500 representatives of the business community, academia and the non-governmental sector were involved in this one-time extensive cleaning up action.<sup>31</sup>

In addition to the regulatory guillotine action, the central government bodies (35 ministries and state agencies) have undertaken a separate action and evaluated 236 laws, of which 20 were considered as not fulfilling the requirements of the state regulatory policy. Yet after the evaluation done by the State Committee of Regulatory Policy and Entrepreneurship, seven laws (out of the already examined 216, which in the first round were considered compliant with the principles of the state regulatory policy by the central government bodies) were additionally assessed as requiring changes. Based on this evaluation, central government bodies initiated the process of developing draft laws and amendments to the existing laws, which need to be passed by the Parliament in order to bring them into compliance with the principles of the state regulatory policy. However, as of February 14, 2006 this work was not yet completed. The State Committee of Regulatory Policy and

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<sup>27</sup> According to the Ministry of Justice, the total stock of government regulation consists of 36,052 acts (as of March 20, 2006).

See <http://www.reestrnpa.gov.ua/REESTR/RNAweb.nsf/wpage/RnaAbout?OpenDocument>. It is not clear however, how many of these regard businesses.

<sup>28</sup> 5,184 exactly, which constituted exactly 55.5% of the total number.

<sup>29</sup> See an official address of the Head of the State Committee of Regulatory Policy and Entrepreneurship of February 3, 2006 at:

[http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art\\_id=56143&cat\\_id=37571](http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art_id=56143&cat_id=37571)

<sup>30</sup> See the press release of the State Committee of Regulatory Policy and Entrepreneurship issued on March 7, 2006. Also available at

[http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art\\_id=56940&cat\\_id=33911&search\\_param=%C0%D0%C2&searchPublishing=1](http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art_id=56940&cat_id=33911&search_param=%C0%D0%C2&searchPublishing=1)

<sup>31</sup> The same source as above.

Entrepreneurship has received for its approval only eight draft laws, which introduce amendments to 14 existing laws out of 27 that require amendment.<sup>32</sup>

The effect of this action, however, was relatively small. Although a significant number of regulatory acts was reviewed and many of them eliminated, no central government agency conducted a comprehensive analysis of the quality of the existing regulatory acts. The review has been rather simple, as it focused on checking whether the existing regulatory acts meet the principles of the state regulatory policy and did not examine the effects of the existing legal acts on business and the performance of different industries<sup>33</sup>. The most questioned regulatory acts were those dealing with the competences of different government bodies and, therefore, creating room for conflicts of interest between them, while examining these acts against the principles of the state regulatory policy.<sup>34</sup>

Since the review has not been finished, an interdepartmental commission chaired by the Minister of Economy has been created to complete examination of the remaining regulatory acts. The first results of the commission's work are encouraging, since some important issues have been addressed. In particular, on January 11th 2006 the Cabinet of Ministers passed resolution #17 *On Introduction of Changes to the Procedure of Issuing Fire Inspection Permits to Open Enterprises and Leasing*,<sup>35</sup> which significantly eases the process of obtaining this type of permit. However, some further steps are required. In particular, it is necessary to introduce correspondent amendment to article 3 of the *Law on Fire Safety*.<sup>36</sup>

## Recommendations

1. **Review of the regulation stock initiated in the second half of 2005 should be completed.** The newly elected Parliament should finalize the process of passing amendments to those laws identified as not compliant with the principles of the state regulatory policy.
2. It should be established, through dialog with the business community, whether there is the need to repeat an action aimed at evaluating the remaining business regulation stock.

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<sup>32</sup> See the press release of the State Committee of Regulatory Policy and Entrepreneurship issued on March 7, 2006, referred to above.

<sup>33</sup> See the opinion of the Council of Entrepreneurship of the Cabinet of Ministers of Ukraine at <http://www.business-rada.kmu.org.ua/ua/news/337.html>

<sup>34</sup> Here we mean either the regulatory acts, which were issued by the joint decisions of several government bodies, or those acts which originally created a conflict of interest between government agencies since they targeted questions also under the competence of other agencies.

<sup>35</sup> See <http://www.kmu.gov.ua/control/uk/>

<sup>36</sup> Law on *Fire Safety* № 3745-XII of 17.12.1993 available at <http://zakon.rada.gov.ua/cgi-bin/laws/main.cgi>

### 4.3. Business community involvement

The business community's involvement in the process of the creation of business regulation has been growing since 2003, when Article # 4 of the Law *On the Main Principles of State Policy in the Sphere of Economic Activity* opened room for consultation and obliged governmental bodies to ask for stakeholders' opinions. Although stakeholders' participation in discussions of new regulatory acts has been increasing, it still does not cover all acts issued by the government bodies. The public participation ratio (PPR), reflecting the number of cases publicly discussed to the total number of new regulatory acts, increased from 78% in 2004 to 89% in 2005.<sup>37</sup> At first glance both figures give an optimistic picture, however it should be underlined that in many cases this participation remained in fact insignificant and formal only. There are at least three reasons for this. The first one is that there are technical problems with circulation and publication of regulation proposals by the government agencies, which are caused by a lack of facilities, funding, and trained staff. The second reason is the reluctance of some government bodies to make all information publicly available. The third is intergovernmental departments' conflicts of interest on some regulatory acts, which government bodies do not want to demonstrate publicly.<sup>38</sup>

A special and far-going provision for stakeholders' participation was made in autumn 2005, when a one time action to review regulations was ordered by the President (see Section 3 of the paper). Representatives of stakeholders, i.e. business associations, the private enterprise sector, as well as non-government research institutions and academia were invited into working groups that made recommendations on individual acts and were offered half of the seats there.

Recommendation:

**Ensure genuine and significant involvement of the business community in creating and improving business-related regulation.** The increased participation of the business community is important as it can bring about an *ex ante* feedback on regulation proposals and work to keep the costs of complying with laws and regulations lower. To this end, technical problems with the circulation of information on proposed regulation, opinions of stakeholders and the government's responses to the opinions need to be solved. This requires the development and use of e-government capacities. Also, intergovernmental departments' relations in the process of creation of law need to be clearly defined so as to diminish room for possible

<sup>37</sup> According to data collected by the Council of Entrepreneurs of Ukraine, see <http://www.business-rada.kmu.org.ua/ua/news/337.html>

<sup>38</sup> For more details see I. Akimova, D. Lyapin, et al. (2005). *Monitoring of publicity of regulatory acts by central government agencies in August- October 2005*. UNDP/BRC Analytical Center. A-03/2005.

conflicts of interest between the parties involved; in particular, the tasks, responsibilities and cooperation between departments have to be thoughtfully shaped.

#### 4.4. Registration

Simplification of procedures to open business has been on the agenda of the Ukrainian government over the last couple of years. An important step in this direction was made in May 2003, when the Ukrainian Parliament passed the Law on *State Registration of Legal Entities and Natural Persons – Entrepreneurs*, which formed the legal base for the introduction of one-stop-shop for business registration.<sup>39</sup> As of July 2005, 673 registration offices out of a total number of 677 offered one-stop-shop service.<sup>40</sup> These deal with a number of administrative procedures to be followed before a business may formally start its activity.

Introduction of the one-stop-shop was expected to significantly shorten the registration process for the benefit of entrepreneurs; however in practice the outcome did not meet expectations. One-stop-shop obviously saves the time of would-be entrepreneurs who, prior to the reform of the registration system, had to visit many offices in order to place applications addressed to several administrative bodies. Nevertheless, settling formalities in a one-stop registration office still takes much time. Instead of delivering all necessary applications at one window, the applicant has to queue in a number of lines in order to talk to registration officers in charge of individual procedures. Furthermore, information on registration procedures and documents necessary for reviewing applications is not helpfully exhibited<sup>41</sup>.

It is not only the organization of work but also inadequate technical capacities of registration offices that are to be blamed for the still poor quality of registration services. In particular, registration offices are short of computers and software. They also need to have a joint computer system in order to introduce, store, and transmit business applications to respective registering bodies. Poor coordination of registration offices' work with the work of other administrative bodies responsible for subject registrations is another problem. This issue has been partly addressed by the introduction in December 2005 of a new order of information exchange between one-stop-registration offices and the Unified State Register. The new order is also aimed at facilitating a smooth exchange of information between the

<sup>39</sup> The full text of the law is available at <http://zakon.rada.gov.ua/cgi-bin/laws/main.cgi>

<sup>40</sup> See [http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art\\_id=52383&cat\\_id=33070](http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art_id=52383&cat_id=33070)

<sup>41</sup> The presentation made by the Head of the State Committee of Regulatory Policy and Entrepreneurship and available at [http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art\\_id=52383&cat\\_id=33070](http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art_id=52383&cat_id=33070)

central administrative bodies participating in the registration process by means of internet facilities.

Introduction of one-stop-shop alone cannot ease the administrative burden accompanying registration. As the Ukrainian experience has demonstrated so far, the number of procedures matters, since each of them requires some paperwork and the collection of accompanying documents, which also involve some costs. An investor who decides to register a company in Ukraine has to deal with 15 procedures and this number places Ukraine close to the end of the list of 155 countries for which this data has been collected.<sup>42</sup> Only five countries: Belarus, Brazil, Paraguay, Uganda and Chad require more procedures to get a limited liability company registered than does Ukraine, while four countries: Argentina, Bolivia, Greece and Guatemala have the same number of formalities. Let us also notice that the average number of registration formalities in the CIS countries<sup>43</sup> is 8.3 - close to two times lower than in Ukraine. At the other extreme, there are countries with the most friendly environment for business, where only two (in Australia, Canada, New Zealand), three (in Denmark, Finland, Ireland and Sweden) or four (in Belgium, Norway) formalities need to be passed to start a business.

The registration process in Ukraine is time- and money-consuming, since prior to visiting the one-stop-shop an investor who wants to establish a limited liability company or a joint stock company has to notarize the company's charter and open a temporary bank account, in which 50% of the initial capital has to be deposited in advance. Next, and before going to a registration office, an investor has to fill in all application forms and collect required documents in order to have a business registered at (1) the Unified State Register, (2) the State Statistics Committee, (3) the Pension Fund, (4) the Employment Fund, (5) the Social Insurance Fund, and (6) the Industrial Accidents Fund. The next two formalities, which are registrations at the Tax Police and at the State Tax Administration, are not covered by the one-stop-shop and require visits to the respective offices.

After processing all the applications by respective governmental bodies, a business is registered and then an entrepreneur, or his/her representative, must visit a local police office and apply for permission to produce a seal<sup>44</sup>. Having the permit in hand he/she may have a seal made and next he/she must return to the bank in order to open a permanent bank account for a registered business. District Tax Inspectorate must be notified of the opening of this bank account; however, this formality does not require a visit to the inspectorate, but may be fixed by mail.

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<sup>42</sup> As of January 2005, see World Bank and IFC (2006), pp. 95-97.

<sup>43</sup> Data for Kyrgyz Republic, Georgia, Kazakhstan, Russian Federation, Moldova, Azerbaijan; Ukraine excluded.

<sup>44</sup> Required and regulated by the Decree of the Minister of Internal Affairs № 17 of January 11, 1999.



Such a long and troublesome procedure creates a demand for the services of lawyers to take over the burden of registration; however, their services are obviously not free of charge and thus increase the overall cost of starting business in Ukraine. Furthermore Ukrainian corruption increases the cost of starting a business. If these two costs are not factored in, then the cost of registration of a limited liability company, for example, has been estimated at the level of 10.6% of income per capita as of January 2005<sup>45</sup>. In a comparative perspective this is quite a good result, since for Poland - for example - this is calculated at 22.2%. If these two costs (legal support and bribes) are factored in, then the cost of registration of a limited liability company requires a larger percentage of income per capita.

## Recommendations

1. One-stop-shop system requires an investment in the technical facilities of registration offices and training of its staff in order to be able to perform its tasks properly. Better coordination between registration offices and sectoral registration bodies is also required. Improvement in these areas would help to shorten the registration process. However, an improvement of performance of the one-stop-registration shop system alone will not suffice to bring about a substantial easing for entrants.
2. Registration process should be further eased by the elimination of some of the currently binding formalities. In order to decrease business compliance costs, the obligation to register a business at the four state social funds collecting payroll taxes separately<sup>46</sup> should be replaced by one for all four registration, as has been done, for example, in Poland where the Social Security Office runs the register for all labor-related funds. Such a change will demand, of course, a substantial organizational effort on the part of the government in order to reorganize the internal flow of information, and will involve additional one-off costs. In the long run, however, it will bring substantial gains from reduced public spending (cheaper government). This reform should be synchronized with the introduction of a unified social tax, which has been for some time the subject of public debate in Ukraine.
3. Another detailed recommendation with regard to registration formalities - and this one is easy to introduce - is to abandon the requirement to ask the Ministry of Internal Affairs for a permit to produce a company seal. This formality, whose rationale might

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<sup>45</sup> According to calculations by World Bank and IFC (2006).

<sup>46</sup> These are (1) the Pension Fund, (2) the Employment Fund, (3) the Social Insurance Fund, and (4) the Industrial Accidents Fund.

have been to increase the security of contracts, takes time and is not free of charge, while it does not, in fact, protect business partners and customers from fraud.

#### 4.5. Permits

Market entry has been under tough administrative control in Ukraine during the entire transition period. At the end of 2005, there were as many as 61 broadly named business activities that were subject to permission. Within these activities there were 1,200 specific ones for which receiving permission was a must if a business activity was to be started and run legally. Access to business activities subject to an administrative decision have been regulated by more than 60 laws and close to 100 decrees issued by the Cabinet of Ministers. Therefore, abandonment of bureaucratic control over entry into two thirds of activities which stems from *the Law on Permission System in Business Activity*<sup>47</sup> that is in force from early January 2006 needs to be appraised as a very important move towards the improvement of the business environment in Ukraine.

The procedures for processing and issuing permits have been numerous, non-transparent and cumbersome, while requirements vis-à-vis businessmen and companies applying for permits have not been clearly defined and have been difficult to access. In addition to general regulations on permissions, however, there have also been many local regulations introduced by regional governments. In general, the burden imposed on entrepreneurs and companies has been high, and this has been especially damaging for small entities which, as compared with big companies, face strong financial constraints<sup>48</sup>. In individual areas, however, the actual burden connected with obtaining a permit differed significantly<sup>49</sup>. The most difficult permits to obtain have been those issued by the fire and phytosanitary inspections, which are supervised by the Ministry for Emergencies and Affairs of Population Protection from the Consequences of the Chernobyl Catastrophe and the Ministry of Public Health respectively. It is worth noticing that without having these two permits no single business is allowed to start and operate an activity in Ukraine. Construction and re-construction of buildings, for which permits are granted by local government bodies, has been another difficult area.

Private businesses have also been required to obtain permissions, which had only an indirect relation to the type of activity that they run. As a result, Ukrainian entrepreneurs and

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<sup>47</sup> Find this at <http://zakon.rada.gov.ua/cgi-bin/laws/main.cgi>

<sup>48</sup> See for example findings of IFC/SME Support Project in Ukraine round table 2005, available at <http://www.vlasnasprava.info/ru/dozvil>

<sup>49</sup> See studies done by World Bank (2004), IFC (2005), and UNDP (2005).

companies have been forced to spend significant amounts of time and money (official fees as well as bribes) in order to obtain the obligatory permits.

Finally, it should be added that many permits were constructed in such a way that they were granted for a limited period of time and therefore need to be frequently renewed. Companies navigating the troublesome procedures, have had to do so again after some time.

In these circumstances, passing the *Law on Permission System in Business Activity*, which proclaims more unified and transparent procedures for the issuance of permissions, is a very good step towards shortening the time and decreasing the costs needed to obtain permits. It should also help to limit corruption. It is important that the Law imposes principles of common procedure for granting permits by both central and local government. However, the detailed provisions of the Law may not ensure the same practice in different economic activities. Articles 4.2 and 4.3 stipulate that the procedure for granting permit by a central government body will be set by the Cabinet of Ministers, while the procedures to be followed by local government bodies are to be set by the respective administrator, however, this should be in line with the common procedure. As a result, there is still room for making the procedures of locally granted permits more troublesome and lengthy.

President's request (Decree #1648 of 24 November, 2005) to take measures aimed at substantial reduction in the time required to process applications and a decrease in administrative fees for granting permissions, has also provided a good response to the existing problems. The Decree, which was very general, at one point was more concrete, asking the government to start deregulation with the permits issued by the fire and phytosanitary bodies.

Despite the fact that the Decree has set a one-month deadline for government to come up with specific measures, so far (until mid-March 2006) there has been no formal action made by the Cabinet of Ministers. Moreover, it is clear that the response may come in June at the earliest, after the parliamentary election on 26 March and formation of the new government.

*The Law on Permission System in Business Activity* has introduced an important innovation, which should save the time of entrepreneurs and companies starting business activity or renewing permits. One-stop-permit centers were proclaimed to be established to accept applications for receiving permission and accompanying documents and – after the applications were successfully processed - to hand over permits. Article 7.8 set a short time limit of five days for the issuance of a permit. As of the end of 2005, there were over 700 centers open. However, a further increase in the number of centers was halted by opposition on the part of local governments, which complained about a lack of budgetary funds needed to establish and run such centers. Since this innovation seriously hurts the interests of local

bureaucrats, this might be yet another serious, though not explicit, explanation for resistance to the further development of the centers' network.

As far as the performance of the one-stop-permit centers is concerned, entrepreneurs complain about the work organization and pace of dealing with applications. The head of the permits department in the State Committee for Regulatory Policy and Entrepreneurship has declared that centers will be able to reduce the time for processing applications and issuing permits by three to four times.<sup>50</sup>

A broader record of how the new Law works may be available later this year after the Cabinet of Ministers makes a review of the implementation of new regulation, which should be done after six months from the date of its publication (i.e. after 6 March).

## Recommendations

1. **Enforcement of the Law on Permission System in Business Activity should be regularly monitored** to give the government and the business community information as to whether and to what extent the unified procedures are followed by individual government bodies granting permits. Based on this information, the Government should react to cases of misconduct and bring the granting procedures in line with legal standards
2. **The principle of granting many permits for a limited period of time should be thoroughly reconsidered.** The longer the time limit of the permit, the better for business development, whereas customer protection can be well secured by inspection, whose task is to check if permit terms are being fulfilled by an enterprise
3. In order to improve and speed up the processing of applications and the issuance of permits, the **legislative base should be further developed**
4. **Introducing special training programs for the staff** working in one-stop-permit centers should secure more effective and friendlier functioning of the centers
5. Finally, it is important to **secure business community awareness of the specifics of the one-stop-permit centers' activity**

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<sup>50</sup> See the statement dated 9 December 2005 and published at [http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art\\_id=54976&cat\\_id=33070](http://www.dkrp.gov.ua/kompred/control/uk/publish/article?art_id=54976&cat_id=33070)

## 4.6. Licenses

The system of licensing is regulated by *the Law On Licensing of Some Types of Economic Activities*<sup>51</sup> and is very extensive. Article 9 of the Law identifies as many as 74 types of economic activities for which obtaining a license is a must. The prerogative to define government bodies responsible for issuing licenses has been given to the Cabinet of Ministers.<sup>52</sup> The Decree of the Cabinet of Ministers # 1698 of November 14, 2000<sup>53</sup> listed 36 government bodies that have the right to issue licenses.

As has already been mentioned in Section 3 above, the Presidential Decree On Liberalization of Entrepreneurial Activity and State Support to Entrepreneurship #779/2005 requested the Cabinet of Ministries to prepare and submit to the Parliament amendments to the Law On Licensing of Some Types of Economic Activities no later than in October 1, 2005 (Article 2.3). The amendments were expected to reduce the number of activities subject to licensing.

The Cabinet of Ministers did not prepare the requested amendments. It was a Member of Parliament who submitted (on October 27, 2005) the draft law on amendments to the Law On Licensing. This draft proposes to introduce some changes to the licensing procedures so as to make these easier for businesses and more transparent; it does not tackle, however, the severe issue of excessive administrative control over market entry. The draft proposes to reduce the number of business activities subject to licensing to 72, i.e. by two only. The proposal has not been subject even to a first reading.

### Recommendations

1. The scope of licensing is large and needs to be substantially reduced so as to widen the freedom to entry and decrease the costs of operating business activities in Ukraine. Therefore, passing the new, more liberal law on licensing should be a high priority.
2. When working on a reduction in the scope of licensing, it is essential to ensure that this is not being done in isolation from other forms of administrative control, which are currently in use. In particular, licenses and permits jointly create one system of administrative control over businesses and therefore they should be considered together whenever any changes are planned to be introduced. Such an approach guarantees that only one administrative instrument to control market entry will be

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<sup>51</sup> *The Law On Licensing of Some Types of Economic Activities* #1775-III of 1 June 2001. Available at <http://zakon1.rada.gov.ua/cgi-bin/laws/main.cgi>

<sup>52</sup> See article 1 and 6 of the Law.

<sup>53</sup> Available at <http://zakon1.rada.gov.ua/cgi-bin/laws/main.cgi>

used in relation to a concrete business activity. In the case of the pending amendments to *the Law On Licensing of Some Types of Economic Activities* it may be assumed that some of the licenses should be removed for the simple reason that they duplicate the functions of existing permits.

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