

Eighteen Months Under Yanukovych

UKRAINE'S REFORM RECORD AND IMPLICATIONS

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Under President Victor Yanukovych, Ukraine's government has launched a variety of initiatives in different policy areas aimed at improving governance and modernizing the country's regulatory system. One motivation for these reforms has been to improve the international perception of Ukraine, which is still seen as having a corrupt and inefficient state apparatus. In the year and a half since Yanukovych came to power, have any reforms met their objectives? Or is the concentration of power in the hands of the president the only obvious outcome of Ukraine's "new deal," a narrative strongly promoted at home and abroad?

Because Ukraine's "honeymoon" with Russia is over and there are no more Western illusions about Ukraine, Kyiv is unlikely to find sufficient financial and political resources abroad needed to help solve Ukraine's fundamental and immediate issues. At the same time, the current international climate allows the Ukrainian government to continue along a path of multi-vectorism so long as the erosion of democracy in Ukraine does not become too pronounced. This balancing act, however, may soon need to end, if Ukraine gets the opportunity to sign the EU-Ukraine Association Agreement that could bring Kyiv a step closer to European integration and a step away from the Customs Union, which is strongly promoted by Russia.

Yanukovych's reforms are diverse, with the most significant ones being in the spheres of the constitution, administration, judiciary, anti-corruption, energy, public procurement, and taxation.

Constitutional Reform

Ukraine's constitution was changed in September 2010, half a year into the president's new term, by a Constitutional Court ruling that reverted Ukraine's system of governance back to a presidential model similar to the one that existed from 1996-2004. By reviving the older model, the president generally became independent from

parliament, while regaining powers that allow him to control the Cabinet of Ministers, Security Service, and Prosecutor's Office. His rapid consolidation of power had an impact on Ukraine's entire political environment, including electoral processes, which were free and fair from 2005 to 2009. As seen by the local elections of October 2010, the new reforms have not contributed to Ukraine's democratic development.¹ Afterwards, Freedom House lowered the country's level of democracy from "free" to "partially free."

Administrative

Yanukovych launched his administrative reforms in December 2010, when he ordered cuts in the number of cabinet ministries aiming to reduce red tape and expenses. Yanukovych reduced the number of ministries from 20 to 16 and the number of cabinet members from 26 to 17. All his key ministers, including Prime Minister Mykola Azarov, kept their posts. Yanukovych stressed that administrative reforms would reduce budget expenditures and help Ukraine cut the public budget deficit, a core condition for future cooperation with the International Monetary Fund. The reforms lack any provision to strengthen institutional capacity and accountability. However, some progress was seen when some bureaucratic procedures were improved, such as the reduction of red tape for 22 types of licensed business activities and the implementation of an electronic national business registration system.

Judiciary

A June 2010 law on the judiciary was supposed to overcome the obvious deficiencies of Ukrainian courts. In practice, however, it threatened judicial independence. First, the new law established short deadlines for the examination of cases, risking the dismissal of who fail to meet the deadlines. The law did not establish any competition-based principles for judicial nominations and does not define any criteria for the appointment of judges to higher courts. The court system thus remains unable to meet basic European criteria. Researchers claim that a large number of Ukrainian enterprises have suffered so-called corporate hijacking attempts over the last years, and foreign investors have been among those targeted. According to EUbusiness.com: "Ukrainian courts have a long record of striking down or ignoring contractual provisions that assign legal responsibility for dispute resolution to a foreign court or arbitrator."² These features have not changed under the new government. It is mostly due to the untrustworthy judicial system in Ukraine that the overall investment and business climate in the country remains poor. This is in direct contradiction to the president's leading economic policy goal, which is to improve the investment climate.

Also, the arrest of former Interior Minister Yuri Lutsenko and opening of a criminal case against (and eventual arrest of) former Prime Minister Yulia Tymoshenko are examples of a "selective" judiciary system, as are corruption investigations of former top officials who are now in the opposition.

¹ "[NDI Sees Deterioration in Ukraine's Election Environment and Urges Improvements](#)," November 3, 2010

² Ina Dimireva, "[Ukraine Investment Climate](#)," 2009

Anti-Corruption

Corruption remains pervasive in Ukrainian society despite long-term efforts to curb it. In 2010, Transparency International's Corruption Perception Index ranked Ukraine 134 out of 178.³

The new leadership launched a vocal campaign against corruption. Immediately after his inauguration, Yanukovich set up a National Anticorruption Committee, which fervently got down to business in the second half of 2010. However, most of the top-level people rounded up were former officials, now in opposition or the ex-president's camp.

Numerous conflicts of interests at the top echelons of power, along with the anti-corruption rhetoric of authorities, have undermined all real attempts to defeat corruption and have led to mistrust in society of government actions. In June 2009, parliament passed a package of laws expanding anti-corruption activities: establishing anticorruption measures in the civil service, introducing checks on employment procedures for the civil service, banning the acceptance of gifts while carrying out official duties, requiring officials and their close relatives to publicly declare their assets, and introducing anticorruption experts. However, implementation of these important laws was postponed from January to April 2010, and then a second time until January 2011. International organizations, the Council of Europe in particular, were very critical about these delays. Finally, the entire 2009 anti-corruption package was abandoned by parliament in January 2011, due to the submission of a softer new anti-corruption law. This law was only ratified on May 2011, making it too early to judge its effectiveness.

Energy

Ukraine's biggest achievement in the energy reform sphere was the adoption of a June 2010 law on Ukraine's natural gas market. Based upon relevant EU directives, it sets up a commitment by Ukraine to ensure non-discriminatory access of companies and consumers to different segments of the gas market, creating conditions for a competitive gas sector.

In September 2010, Ukraine signed a protocol on joining the Energy Community Treaty (ECT), ending a lengthy process of negotiations, informal consultations, and the implementation of additional EU conditions and prerequisites. Ukraine's official accession to the ECT was supposed to give a boost to Ukraine's energy integration with the EU. But if Ukraine's overall reform pace remains low, as it is now, Ukraine will not garner any benefits from the deal. Currently, a year after the gas market law went into force, its main provision regarding equal access to markets has not been fully realized.

It should also be noted that the year 2010 witnessed the remarkable return of energy intermediary Rosukrenergo to the Ukrainian gas market. This group was previously banned, primarily by the efforts of Yulia Tymoshenko. The dominance of this business group raises questions about the prospects of better governance and transparency in Ukraine's energy sector.

³ Transparency International: [2010 Corruption Perceptions Index](#)

Public Procurement

The adoption of Ukraine's public procurement law in 2010 was a positive step toward improving standards. However, six months after the adoption of the law, the Ukrainian government enacted a number of amendments that had a negative impact on the law's efficiency and limited the scope of goods and services that it applied to. This provoked sharp criticism from the EU and even led to the suspension of an EU budget support program in January 2011. More recent changes introduced in May 2011 improved some elements but even these were criticised for reducing transparency.

Taxation

Tax reforms went into effect on January 2011. They were aimed at codifying the country's fiscal legislation into one comprehensive legal act. The adoption of the new tax code was a step in the right direction. At the same time, the process of its adoption provoked a conflict between the government and representatives of small- and medium-sized business, who considered the new rules to be discriminatory. It seems that most of the progressive tax reforms were designed to support large, oligarchic, businesses. For instance, only large businesses can enjoy the automatic return of VAT fees – and the list of such large businesses must be approved by the government. Delays and problems with VAT returns traditionally hamper all-sized businesses that engage in international operations. Why favor a few?

Conclusion

The Ukrainian economy remains overregulated and suffers from chaotic governmental interference, despite "reform" efforts. The World Bank puts Ukraine in the 145th position among 183 economies when it comes to "Ease of Doing Business." The Heritage Foundation and *The Wall Street Journal* in their 2011 annual rating of economic freedoms give Ukraine a score of 45.8, making its economy only the 164th freest among 179 ranked. The regulatory framework has not improved and the sense is that Ukraine remains mostly non-business friendly.

Public opinion polls may be an indicator of progress. Recent polls do not show any positive change in public perception of government services. According to a Razumkov Center poll conducted in September-October 2010, the Security Service of Ukraine was trusted by 13.2% and not trusted by 36.3%; the police were trusted by 8.7% and not trusted by 51.2%; public prosecutors were trusted by 7.4% and not trusted by 47%. Only 5% of people polled expressed confidence in Ukrainian courts while 51.5% indicated no confidence.⁴

Though declaring support for giving greater power to local authorities, the central government did its utmost to boost its own influence at the expense of local and regional self-governance. The emphasis on a centralization of power undermines the already weak connection between authorities and rural residents, not to mention their

⁴ Razumkov Centre: [Public Opinion Poll: September 30-October 5, 2010](#)

ability to participate in shaping public policy. The government's further centralization of power has not contributed to a better understanding between the eastern and western parts of Ukraine. In fact, 2010 local elections demonstrated an increase in split attitudes as the radical-right, nationalist, Svoboda party took a majority in several councils in Ukraine's western regions.

After years of political turbulence due to constitutional deficiencies and inter-personal conflicts between top leaders, Ukraine began a period of centralized power consolidation that has evinced elements of order, consistency, and manageability. This has allowed the country to escape from its long-lasting institutional stalemate. At the same time, the newly established stability is not based on rule of law, democratic legitimacy, or a viable system of checks and balances. A year and a half into the new administration's term, we see instead a monopolization of power achieved through the manipulation of legal procedures and democratic norms, deviating Ukraine ever further from EU standards.