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Time to change tax

New administration making encouraging noises but business reform very much a work in progress

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No great period of time has yet elapsed since the recent presidential elections and while the emotions the campaign generated are calming down, various pre-election promises remain in the forefront of people's minds. To recall, among other things there were statements throughout the campaign of support for small and medium businesses (including talk of decreasing their tax burden and introducing five-year tax holidays). Candidates also discussed reducing the VAT rate in 2011, gradually reducing the corporate profit tax rate and adopting the Tax Code, among other things.

New Tax Code on its way

With the new Yanukovich administration having been in office for less than the traditional 100 days it remains far too early to pass judgment on their business policy. In terms of tax collection, we can expect no drastic liberal changes within a short timeframe: it is simply unrealistic to expect them right now. In fact the opposite is probably true and it is almost taken for granted that in the short term there will be attempts to squeeze more taxes out of business. Hopes are focused, however, on the medium and long term perspectives, when momentum could build towards improving the quality of tax legislation. Notably, adopting a Tax Code in the coming months would be a meaningful step towards establishing a solid platform for further rectification of the problems associated with Ukraine's weak, outdated and controversial stack of tax laws. The government is currently promoting this idea and sounds eager to have the Tax Code voted for by mid-year so that it takes effect on 1 January 2011. It seems that the draft Tax Code developed in 2007 will be used as a basis and further updated, taking into account the anti-crisis measures adopted in 2008-2009 as well as the current situation and current needs and priorities. However, there is no unanimity on the side of officials about whether it is more efficient to use the available draft or to start from scratch.

One may with good reason doubt whether the rush is appropriate, considering that the document is pretty raw and that little time for detailed consultation can, obviously, be allowed. Indeed, perfection would be desirable. It would be a pity, however, if the perfect were to become the enemy of the good, resulting in more devastating inaction. It is far more important to find a reasonable compromise and finally put together a viable codifying tax statute. Any ambitions towards perfection can be served later when tuning up what would be an already valid document.

Although discussions concerning the Tax Code have been intensive, the VAT refund problem may soon replace them on the front pages. What is primarily at issue is the recently announced "VAT bonds" plan, which has a good chance of being introduced first among all the current tax initiatives under consideration. This measure is quite controversial and has seemingly been undertaken in despair. It's hard to predict what the reaction of the business community will be; however, much will depend on the exact legal framework and factual circumstances surrounding implementation of this instrument. Particular points of concern include whether the use of VAT bonds will be voluntary, and whether, at the end of the day, business will have a realistic opportunity to get full cash compensation of its costs, or whether everything will end up in a situation in which the bulk of unpopular state securities are traded with heavy discounts and in which taxpayers are offered unfavourable tax treatment. For some weird reason VAT bonds are currently being advertised as a stand-alone solution, though they can hardly be perceived as a panacea. The VAT refund issue can only be solved through complex and system-level measures, including not only introduction of other

Current issue

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With a Kremlin-friendly regime now firmly in place in Kyiv and agreement reached to keep Russia's Black Sea fleet in Sevastopol until 2042, this year's bumper 65th anniversary Victory Day celebrations in Moscow are likely to be particularly satisfying for Vladimir Putin and the Kremlin hierarchy

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point-counter tools but also review of the VAT system in general.

Tax reform as part of broader pro-business environment

Routine work on ad hoc issues is also reportedly underway. Thus, the first fortnight in April was marked by drafts of three laws. The first one relates to the indicative salary and is designed to be used for calculating personal income tax and contributions to state pension and social funds. The second draft suggests introducing a new tax on luxury items (to be levied upon purchases of aircraft, helicopters, yachts, luxury cars and real estate) with the aim of generating state budget revenues. The third document, the draft law "On Family Business," targets private entrepreneurs and is to replace the simplified taxation system with new rules.

One could also note the cancellation of the previous government's notorious regulations on VAT and other tax matters. These regulations violated the effective tax laws. Importantly, however, these efforts to codify and improve the tax laws are in essence palliative and insufficient in the absence of substantial work to liberalize business regulations. Among the most relevant areas are, for example, simplifying the business set-up and exit rules, creating a level playing field for foreign investors and removing regulatory barriers, improving the permission and licensing system, optimizing the currency control regulations and land reform. Reportedly, draft laws that could improve the investment climate are coming, but it is too early to say anything concrete. Miscellaneous discussions and vague expectations characterize the moment. Hopefully, these good intentions will materialize into something tangible, giving businesses in Ukraine a breath of fresh air.

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