Customs in Ukraine: Business Wants Reforms, Government Seeks to Maximize Revenue

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Economic recession in Ukraine made Ukrainian government look for additional sources of income to fill up the drained state budget. Among such sources were import duties, which in 2015 contributed a sizeable share to the country's finances in spite of the falling amounts of imported goods. However, businesses in Ukraine – the importers that deal with the customs on a regular basis and pay the fees – want the customs procedures to become less income-focused and instead, to be aimed at facilitating trade. As the 2015 survey of Ukrainian businesses by the Institute for Economic Research and Policy Consulting showed, changes in trade regulations and customs rules are needed to boost international trade.

The continuing economic crisis, falling rate of national currency, and lesser spending capacity of the residents of Ukraine made imports into the country drop last year. Ministry of Finance of Ukraine reports 31.1 percent decline in the volume of imports in 2015 as compared to 2014. **Still, the revenues collected from import duties were 3.2 times bigger in 2015 than in 2014 – largely due to the additional import fees** that the Ukrainian government introduced in 2014 to counter low budget proceeds.

Out of the UAH 39.9 billion (around 1.5 billion euros) of the 2015 import revenues, UAH 25.2 million were collected through the additional import fees[1]. The remaining import income has been obtained through regular payments of duties, which grew in terms of Ukrainian national currency as the currency itself fell in value (the National Bank of Ukraine assessed the devaluation of the Ukrainian hryvnya to the US dollar in 2015 as much as 83.8 percent).

This makes revenues from imports a considerable source of financing for the struggling economy of Ukraine. **Expected incomes from customs payments are included in the annual state budgets, and regional customs offices in the country keep receiving a monthly "plan" – the target amount of collected fees and duties**. Yet, this practice raises the cost of doing business for the importers in Ukraine. The businesses surveyed by the Institute for Economic Research and Policy Consulting (IER) say that the revenue-oriented approach makes the customs less transparent and fair and leads to higher prices of imported goods for the end consumers in Ukraine.

The IER conducted the survey of Ukrainian importers and exporters in 2015 as a part of the Trade Facilitation Dialogue, a program which is supported by the European Union and aims to facilitate policy dialogue between business and public authorities and to reduce costs of trade in Ukraine. The total sample of 381 firms representing different sectors and regions of Ukraine answered the questions about the problems and hurdles they face when moving goods across the border and dealing with the customs system in Ukraine.

The problem most businesses reported in the survey is Ukrainian customs trying to collect higher import duties than the ones based on the actual price of the imported goods. This is done by using the system of "indicative prices" instead of the contract price. **Arriving at customs, the importer expects to pay the fees according to their value as indicated in the invoice from the supplier**. In practice, however, Ukrainian custom officials often refuse to accept the contract as a proof of the declared price and demand payments according to the pre-determined price as recorded in their database, which is usually higher.

This has come to be known as the "reserve" method of establishing the value of imported good, which Ukrainian laws obliged the customs to use when the "primary" method of following the contract price was not available. Yet in September 2015, this method became effectively mandatory for the import operations after the Cabinet of Ministers of Ukraine issued the resolution No. 724 that recommends customs to follow the fixed prices. And while the government advocates the indicative system as the one that will level the field for businesses and help identify risks, this method creates significant obstacles for Ukrainian importers.

Firstly, as the IER survey suggests, it raises the end price of the imported goods for the consumers in Ukraine because the importing firm has to pay more at the border. Secondly, it makes the customs duties unpredictable – businesses cannot plan their expenses as they are not sure that the customs will accept the price of the goods as put down in the contract. Moreover, **the importers surveyed by the IER said they have no access to the database of indicative prices, which makes it hard to guess a possible price at which their import will be valued**. And thirdly, the method of assigning prices for the imported merchandise creates opportunities for corruption and discretion. Facing higher import duties, businesses may prefer to bribe the customs into setting the prices lower in what they may see as a lesser transaction cost than the official payment. And the decision about the price ultimately lies with a customs official who may choose to use either the contract price or the indicative one.

In some cases the customs demand from the importers to present additional documents that would prove the price in order to recognize the contract value of the imports. For the surveyed businesses, obtaining extra documents beyond the contract means losing valuable time in the import cycle. In general, the uniform setting of prices makes competition among the importers futile and discourages them from bargaining for better prices from their foreign supplier.

Ukrainian government tries to soften the fiscal burden on the customs operations by offering a few pilot regions to invest the surplus from the customs revenues into the local infrastructure**. If a regional customs office collects more in fees and duties than was expected in the plan, half of the extra funds will be allocated to build roads, for which there is a major need in virtually every part of the country**. But the business in Ukraine expects the reforms in the customs system that would make it more transparent and business-friendly. As the importers and exporters said in the IER survey, the customs needs to drop the fiscal function and to focus on facilitating and accelerating international trade operations. An open and efficient customs will better meet the needs of Ukrainian business.

1 Source: the Ministry of Finance of Ukraine **http://ukurier.gov.ua/uk/articles/informaciya-ministerstva-finansiv-ukrayini-08/**