

ICPS newsletter

Budget reform will open the way to steady growth

A balanced and transparent budget, together with financial stability and a coherent taxation policy, constitute the basis for economic growth. This year, the government has achieved significant progress in reforming the budget policy in this direction. Participants of a public discussion on "Budget reform in Ukraine", conducted as part of ICPS's project "Ukraine's Future: Public Feedback on Reform Policy", spoke on further actions necessary to improve budget policy

Progress of budget reform

A balanced budget, prohibition of mutual debt offsets, cancellation of tax privileges, and increasing the efficiency of budget expenditures—these priorities of budget policy have been determined by the Ministry of Finance of Ukraine.

Mr. Ihor Mitiukov, the finance minister, noted that the public is already concerned with the positive impact of a balanced budget on the national economy. Due to the reduction in financing the state budget deficit using the resources of the National Bank of Ukraine, overall lending has increased. The financial crisis confirmed that there was a need to decrease government consumption, thus during the last 4–5 months it was reduced by 25 percent.

This year, the government should completely resolve the debt offset problem, since budget revenues are directly proportional to the share of cash payments to the budget. The minister admitted that last year the mistake lay in limiting offsets regarding payments to the national budget only (while such restrictions were not imposed on local budgets). This drawback has been eliminated, and in 2–3 months we can expect positive results.

Another crucial point of the budget policy,

During May–June 2000, the International Centre for Policy Studies, jointly with the Secretariat of the Cabinet of Ministers and the Ministry of the Economy of Ukraine, with the financial support of Freedom House, is carrying out a project titled "Ukraine's Future: Public Feedback on Reform Policy".

The project is aimed at achieving the following objectives: promoting the democratic practice of public participation in decision-making by conducting public discussions of policy options; increasing awareness of the steps taken by the President and the government as part of the reform strategy; and improving communication between government agencies and public organisations. Participants of these meetings will discuss the implementation of the Government Action Plan as concerns the given activities.

This project entails conducting a series of seminars to build a general public understanding of the goals of public policy and a unified vision of social priorities and certain measures.

Public discussions are planned on the following topics:

- public discussion of the government Action Plan (April 15);
- agricultural reform (May 12);
- regional policy (May 17);
- budget policy (May 25);
- changes in the business environment (June 1);
- reform policy in the power sector (June 9);
- administrative reform (June 15).

Representatives of the Administration of the President of Ukraine, the Verkhovna Rada, the Cabinet of Ministers, non-government organisations, the mass media, and international experts are invited to participate in the public discussions.

Please note that dates of seminars have been changed from those announced previously.

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in the minister's opinion, is the government's decisions to cancel tax privileges and holidays granted previously, as well as reject granting new privileges of this type. The tax system should be reformed on the principles of neutrality and equality in tax payment liabilities for all economic entities. The existence of different tax regimes in a particular sector aggravates corruption.

According to the minister, the government had developed its budget expenditure policy in one direction only: unilateral reduction of expenditures, based on existing resources. But such actions are ineffective, since they are not matched with the policy in the particular sector. Equal reduction in expenditures prevents development, since none of the strategic

priorities can be fulfilled. Till the present, the formation of budget expenditures has been made on the basis of quantitative indicators (staff, beds etc.); instead, now there is a need for considering qualitative indicators. Mr. Mitiukov informed seminar participants that the development of methods for analysis of expenditure effectiveness has already been started.

Ms. Maryna Shapovalova, head of the Department for Macroeconomic Indicators and Monetary & Lending Policy at the Ministry of Finance of Ukraine, emphasised that the goals and objectives to be achieved by the government through the budget should be clearly identified. Such goals and priorities should be determined for the average- and long-term future, not only at the central but also at local levels.

Shift to program-oriented budget will encourage economic growth

According to Mr. Anatoli Maksyuta, head of the Budget Department of the Ministry of Finance of Ukraine, huge tax and budget arrears are evidence of the imbalance of the Ukrainian budget, caused by budget planning on the basis of unlimited demand. The Ministry of Finance has calculated that 150 billion hryvnias per year would be required to implement the law on budgetary financing for enterprises and citizens. Not counting reinstated personal savings [lost to Russia with the breakup of the USSR], this sum would be 70 billion hryvnias, i.e., 55% of GDP in 1999. At the same time, demand greatly exceeds budget revenues. If budget reform is further hampered, the budget imbalance will threaten economic growth in Ukraine.

The shift to a programmatic approach of budget expenditure planning will allow to liquidate the budget imbalance, improve the quality of spending, and promote economic development. Forming budget expenditures according to public policy goals and real budget revenues, the government will be able to implement its functions at the lowest cost to society. However, Mr. Maksyuta noted that the shift to a program-oriented budget is time-intensive and demands much effort. (For example, in the USA the switch to a programmatic approach lasted 10 years.) In 2000, the Ministry of Finance has begun preparations for this process: examined necessary changes in budget classification and now has been developing program evaluation criteria. Mr. Yuri Lupenko, deputy head of the Department on Economic Policy at the Administration of the President of Ukraine, affirmed that the shift to a program-oriented budget is supported by the presidential administration.

Independent financial control is a component of budget reform

Mr. Vitali Melnychuk, deputy head of the Accounting Chamber of Ukraine, believes that providing independent financial control of budget resource allocation is a mandatory element of budget reform. In Ukraine, the Accounting Chamber was established three and a half years ago. Today, this agency ensures control over the legitimacy, expediency, and effectiveness of public expenditures. The Accounting Chamber also carries out analytical functions: it monitors budget and tax legislation, prepares information reports on

Summarised public proposals on budget reform developed during group work

Impediments to implementing state policy on reform of the state budget:

- high level of corruption;
- insufficient information on the current state of budgets;
- large public sector;
- distrust of the powers that be;
- fear of public reaction to budget restrictions;
- lack of consensus in society.

- ### Instruments for budget reform:
- adoption of the Tax Code;
 - composition of tax legislation in favour of tax payers;
 - granting the Accounting Chamber the authority to control budget revenues;
 - create an independent revenue base for local budgets;
 - switch to a programmatic approach of budget formation;
 - determine efficient and exclude inefficient budget expenditures;
 - harmonise legislation on the issues of the administrative system and budget procedures.

Proposals on improving the quality of government decisions on budget reform:

- conducting public discussions of draft government decisions;
- strict separating of state bodies' authorities;
- informational support of decision-making;
- ensuring independent expertise of government decisions.

Proposals on improving the effectiveness of international technical aid:

- acquiring international experience (e.g., introduction of the programmatic approach in the USA);
- involving international experts in the development of the Budget Code;
- introducing international standards of accounting of state financial resource flows;
- ensuring targeted assistance to regions.

review of draft state budget and on budget execution during reporting periods for the Verkhovna Rada, and develops recommendations on budget legislation improvement.

Mr. Melnychuk pointed out that in order to increase the effectiveness of the Accounting Chamber, the following measures are needed as part of budget reforms:

- authorise the Accounting Chamber to control the allocation of budget revenues;
- establish regional offices of the Chamber;
- design a methodology for examining the allocation of state budget expenditures;
- develop a mechanism of co-operation between the Accounting Chamber and similar institutions of Western countries, particularly for controlling money laundering.

It is time to establish a new system of inter-budget relations

Inter-budget relations are the main problem of the 2001 budget. The current centralised system of inter-budget relations does not correspond to the Law "On local authorities". Today, budgets of local communities depend on 27 oblast budgets. Instead, the law foresees the creation of about 700 independent budgets of local communities. According to Mr. Ihor

Mitukov, minister of finance, the shift to new system of inter-budget relations should be a gradual process. Lack of procedures and tools for levelling financial abilities of the low income local communities will hamper the successful implementation of government liabilities. However, decentralisation and providing of financial independence for these communities should follow treasury execution of local budgets.

2001 Budget will be planned on new principles

Mr. Yuri Yekhanurov, first deputy prime minister of Ukraine, noted that during planning of the state budget for 2001 the following major issues should be settled: tax base, privatisation proceeds, budget balance, separating functions of the central and local budgets, and degree of ministry independence regarding fund allocation. According to Mr. Yekhanurov, the state budget for 2001 will be drafted on new principles if the Tax Code and laws on personal income tax, local taxes and levies, property tax, and local excises will be adopted. ■

The public discussion on "Budget Reform" co-organised by the Secretariat of the Cabinet of Ministers and the Ministry of the Economy of Ukraine, and the International Centre for Policy Studies was held at ICPS on May 25, 2000.

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