

ICPS newsletter

Draft Tax Code: Harmonisation of interests goes on

The main goal of the tax reform, currently discussed by the parliament, is to set optimal levels of payment. Tax charges have exceeded taxpayers' capacity in Ukraine, because the needs of the government had not been adjusted when the new tax system was created. In the absence of integral tax policy, this provoked both legal (through lobbying privileges) and illegal evasion of tax regulations. Last week, the Verkhovna Rada of Ukraine adopted the draft Tax Code in the first reading. Ms. Tetiana Sytnyk, ICPS chief economist, comments on this event

Metaphorically speaking, the payment of taxes reflects a compromise between the citizens of a country and its government. Realising the benefits of public services (education, health care, and infrastructure) and equitable distribution of incomes to society, producers and consumers agree to contribute a part of their incomes to the budget. In this context, taxes should fit the following criteria:

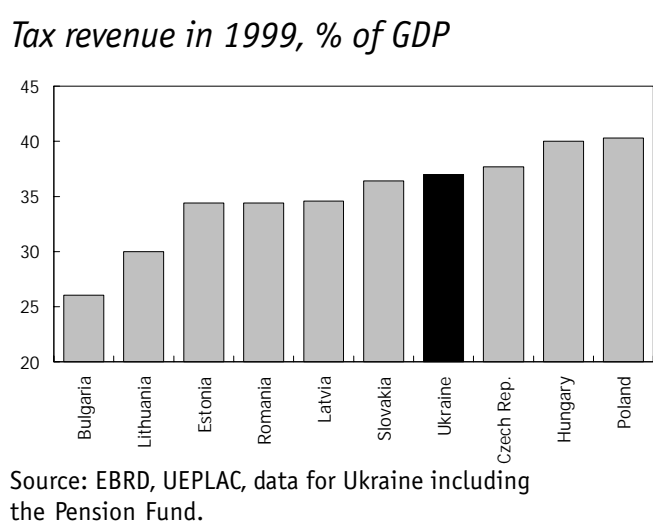
- Adjustments or changes required of households and businesses after the introduction of taxes should be minimal. For this reason, modern tax systems rely primarily on indirect taxes instead of direct ones—the effect of taxes on consumption (in particular, VAT) on consumer choice is almost undiscernible.¹

- The tax burden should be evenly distributed. To ensure the equitable redistribution of incomes, the tax burden must be spread out proportionately, according to the “paying power” of taxpayers. For example, graduated tax rates have been used for personal incomes.

- The system of tax payment should be unambiguous. Easy collection and accounting are the most valuable characteristics of good taxes.

The Tax Code is an instrument of integrated tax policy that can help to form stable expectations in the business sector, and stimulate economic growth. In our opinion, the draft Tax Code being considered by the Verkhovna Rada of Ukraine aims to accomplish the following tasks:

- reduce the tax burden;
- ensure equitable distribution of the tax burden and preserve only those exemptions that stimulate socially useful activities; for example, this draft Tax Code envisions VAT exemptions for



Last Week

The People's Voice Project is expanding into Ivano-Frankivsk.

As a part of ICPS's People's Voice Project, a conference on "Improving Government Services to Municipalities" was held on 7–8 July in the southwestern Ukrainian city of Ivano-Frankivsk, co-organised by the Ivano-Frankivsk city council, the mayor's executive office, the Agency for Urban Development, and the Association for Economic Development, in cooperation with the Canadian International Development Agency, the World Bank, the World Bank Institute, and the International Centre for Policy Studies.

The overall goal of the People's Voice Project is to implement mechanisms and procedures that promote public participation in building effective, responsible and open government at the municipal level, as well as to ensure public participation in policymaking in particular.

The primary objective of the project is to assist municipal governments in selected Ukrainian cities to reform and improve their services to households and businesses, and to enhance their level of integrity in the process.

At the conference, attendees learned that in a democratic society, people do not rely on the moral qualities of state authorities and officials; rather, as emphasised Ms. Vira Nanivska, director of ICPS, they establish procedures, norms, and rules that

provide public control and can influence policy decisions.

Mr. Tom Monastyrski, People's Voice Project director, noted that in order to strengthen integrity, particularly at the local level, the following measures should be carried out:

- creating transparent procedures for government procurement;
- establishing an independent committee for supervising privatisation and government procurement;
- conducting budget hearings where citizens and state authorities could discuss budget issues together;
- publicising decisions of the city council;
- conducting public discussions of major problems and plans; and
- researching corruption in certain areas, in order to determine problems and possible solution alternatives, with further publication of research findings.

One of the conference results was the creation of the Coalition of Ivano-Frankivsk Non-government Organisations. According to the first meeting of Coalition members, its priority activities are educational reform, budget hearings, joint training of local government officials and NGO representatives in order to strengthen their relations, and support for cultural and art initiatives.

Preliminary results of the survey on public service delivery in Ivano-Frankivsk, which was conducted through interviews with households, businesses, and civil servants, were presented during the conference. The final survey results will be published in the nearest future.

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the services of preschools and homes for the aged;

- simplify procedures for charging and accounting taxes; the Ukrainian government proposes that legal entities would submit P&L statements once a year (along with monthly advance payments) and that small businesses could use simplified taxation procedures;
- meet international taxation standards; this will help attract foreign investments; and
- determine the rights of taxpayers and powers of tax authorities; this part of the code is the most important, because the relations between Ukrainian taxpayers and tax authorities have not yet been legally defined.

Reaching a compromise by achieving these goals requires some time to harmonise the interests of all parties. Moreover, the Tax Code should be sufficiently comprehensive as not to require supplementation in the future. Therefore, we believe that the Tax Code should be put in effect gradually, and

the following steps should be carried out first:

- Reduce tax rates and the number of taxes to stimulate investments and consumption.²
- Carefully discuss and refine the draft Tax Code, particularly the part which stipulates the rights of taxpayers and powers of the tax authorities.
- Bring the draft Tax Code and the draft Civil Code into line (the Civil Code is being prepared for consideration in the third reading) and coordinate efforts in the implementation of tax and budget reform.

We anticipate that the Tax Code will become effective in 2002. Approval of the code will be preceded by a reduction of tax rates and the number of taxes in 2001. ■

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¹ In modern tax systems, the value-added tax is levied on all consumer goods. Therefore, VAT does not affect consumer choice. Excise duties are usually imposed on goods which are in steady demand, so they do not change consumption patterns on these goods, either.

² The draft Tax Code submitted by the Ukrainian government to the Verkhovna Rada envisions a gradual reduction of the VAT rate: from 20% to 19% in a year after the code becomes effective, and to 17% later on. The corporate profit tax rate will be reduced from 30% to 25% (in a year after the code becomes effective), and to 20% later on. The maximum rate of personal income tax will be cut from 40% to 20%. The number of state taxes is to be reduced from 18 to 13, and the number of local taxes from 16 to 10.

This Week

NGO coalitions are mastering the mechanisms for effecting the policymaking process. An international conference titled "Creating mechanisms that strengthen the involvement of NGO coalitions in local government decision-making processes throughout Central and Eastern Europe", co-organized by the ICPS's People's Voice Project and the International Renaissance Foundation, will be held in the southwestern Ukrainian town of Yaremche, Ivano-Frankivsk oblast, on July 20–22, 2000.

The goal of the conference is to develop skills and facilitate a dialogue on ideas that will allow NGO coalitions to become further involved in decision making at the local government level. Among the participants will be representatives of NGO coalitions from Ukraine, Bulgaria, the Czech Republic, Hungary, Poland, Romania, and Slovakia. Conference participants will have the opportunity to exchange their experiences in effective co-operation between NGO coalitions and local governments, and to establish relations for future collaboration.

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