

The Week

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Even good reforms can bring pain, says analyst

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Dr. Irina Paliashvili is the president and senior counsel of the Washington-based Russian-Ukrainian Legal Group, P.A., which she founded in 1995. Early in 2005, Paliashvili prepared a study on measures needed to improve Ukraine's business and investment environment. Her analysis appeared in the Action Ukraine Report this past March.

The Post talked to her about some of the problems outlined by the study at her Kyiv office on April 1.

KP: *What are the things that concern you most regarding the business climate in Ukraine under the new government?*

IP: I can speak of the very specific problems that I can see in the area where I work: international business and investments. The main problem...is the absence of any steps to fix the terrible problems created by the former regime, which seems to be in contradiction to the continuous appeals made by President Viktor Yushchenko and his government to foreign investors to come to Ukraine immediately.

The thing is that the new government has a very narrow window of trust. Between now and the time when new investors actually come to Ukraine and start taking their first steps ... the legal climate [needs to be improved]. If that does not happen and the obstacles to foreign investment that were created...are not removed, all this trust will be gone, the window will close.

KP: *Could you name some of the most crucial problems that foreign investors face in Ukraine?*

IP: The commercial and civil codes are in conflict with each other. The commercial code is a document based on Soviet legal concepts, which would have sense and seemed progressive, maybe, 25 years ago. Today, however, it acts as a brake that hampers business development.

Writing up even a basic contract that would be fully compliant with the law of Ukraine is impossible in principle - one or another law would be broken. On one hand, we have a commercial code that limits the freedom of contracts and is Soviet in essence. On the other hand we have a civil code which is more market-

oriented, but still has many contradictions. In addition, there are other laws to consider, and all three are not in coordination.

Naturally, this leads to corruption. For example, during a court dispute, one side might cite one code, while its adversaries - another. The judge thus gets an opportunity to decide which code to use in making a decision.

This is a complete disgrace, as the codes, effective since Jan. 1, 2004, have caused legal chaos. It might have been somehow understandable, given the turmoil of 2004, but now this is simply unacceptable. The commercial code is a relic that simply needs to be cancelled immediately - Ukraine doesn't need this socialist-style document.

Another problem that I find not as fundamental as the previous one, even though it causes a lot of harm...is the National Bank resolution from [last year] [which] has caused huge obstacles to foreign investment to Ukraine. Before, investing in Ukraine was relatively straightforward; the problems usually would begin later on. The resolution made investing itself extremely difficult.

[NBU resolution 482, introduced on Nov. 11 2004, requires all investments to be made in hryvnya through a commercial bank within Ukraine's borders. -ed.]

To describe [the resolution], I would use the term "domestication." All foreign investment in Ukraine has to be converted into Ukrainian currency and then invested.

This contradicts our basic legislation on foreign investment and international agreements that Ukraine [has signed]. It's basically confiscating hard currency from investors who are then forced to convert 100 percent of their investment into hryvnya.

Some of our clients simply refused to come to Ukraine, once we explained to them what they would have to [do to] invest.

In October of 2004, when the hard currency reserves of the NBU were falling due to the presidential elections, [the rule] was, most likely, meant to be an extra source of hard currency for the government.

In February of 2005, the Justice Ministry suspended this resolution in response to a number of court cases that investors filed because the resolution violated Ukrainian laws and international agreements. Ukrainian banks, however, did not abide [by the change], and they waited for NBU instructions, which [never came].



As the result, for two or three weeks the banks would simply not open any accounts for investments to Ukraine...At the very moment when Yushchenko spoke in Davos, Switzerland [at the World Economic Forum in late January] urging foreign investors to come to Ukraine, all investments to Ukraine were paralyzed.

[...] These are only some of the problems that immediately need to be removed and apologized for, as they ruin the image of Ukraine as investment-friendly country, which it nowadays is being promoted as.

KP: *In your opinion, how much time does the new government have to deal with such problems?*

IP: Not much time. Information about things like this spreads very quickly. Personally, I trust the new government and think that they are moving in the right direction. I also understand that some time has to pass before the government machine starts functioning efficiently at all levels, but at the same time the trust in Ukraine is expiring.

Ukraine has received huge positive PR worldwide, but we are very close to the point when its government actually has to show the results of its performance.

KP: *Some experts believe that the government's campaign against contraband has increased prices. How should the government act when its reform attempts seem to cause harm, like increases in prices?*

IP: The reforms are not possible without negative side effects. They are bound to take place. But you just cannot make it an excuse for not implementing reforms. Then why not just have a corrupt state flooded with contraband, and then we would not have to move anywhere at all?

If you, for example, cancel the commercial code, or the NBU regulation which we have discussed, their lobbyists also would call it the end of the world... you can make up all kinds of causes and effects, but they need to be proven.

I am very glad that the new government of Ukraine has chosen to liberalize the economy to root out the corruption, instead of trying to jail all corrupted officials, which is simply impossible.

KP: *Is the new government's honeymoon over?*

IP: For me, not yet. Everybody has his own time limits. I understand that there is a huge resistance and inertia, mental, physical and financial, so two months is just not enough.