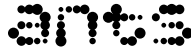




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# INTRODUCTION

The full-scale aggression of the Russian Federation requires an unprecedented mobilization of all the country's resources to ensure defense capability and fund the Armed Forces of Ukraine. Historically, a significant portion of these needs, as well as the coverage of the state budget deficit, has been financed through extensive international support.

As of 2025, the main donors to the Ukrainian budget, ensuring its macro-financial stability, remain the European Union, the International Monetary Fund (IMF), as well as a number of partner countries, including Canada, Japan, the United Kingdom, and others.

However, the situation with international assistance is undergoing significant changes. In particular, in 2025, there is an almost complete absence of direct budgetary support for Ukraine from the United States of America. This is associated with a number of factors, among which domestic political processes in the U.S. play a key role, notably the election of President Donald Trump. His new policy is characterized by a review of foreign expenditures, an emphasis on «America First,» and a general desire to reduce financial assistance to other countries, which directly affects the volume of support for Ukraine.

At the same time, support from the European Union, in particular within the framework of the key Ukraine Facility program totaling 50 billion euros, is vital, but its provision is strictly tied to Ukraine's fulfillment of the agreed reform plan. Already in 2025, significant risks and challenges are evident. Specifically, due to non-compliance with the requirements of this plan, Ukraine is already receiving 1.5 billion euros less. This situation underscores the critical importance of meeting reform obligations.

The absence of proper reforms, their delays, as well as the rollback of reforms in certain areas, particularly anti-corruption, law enforcement, and the judiciary, significantly reduce the trust of our international partners and may lead to further reductions or even a complete cessation of funding, which would have catastrophic consequences for the stability of the state budget and the ability to fund the Armed Forces of Ukraine.

Given these realities, ensuring stable and sufficient funding for the Armed Forces of Ukraine, as well as strengthening our financial independence and resilience, is critically important. This draft proposes a comprehensive approach to potentially increasing internal financial revenues for the budget by 500 billion hryvnias, which will allow us to enhance our defense capability and accelerate the achievement of victory amid a reduction in external budgetary support.



# **ANALYSIS OF INTERNATIONAL FINANCIAL SUPPORT FOR 2022-2025 AND UKRAINE'S NEEDS FOR 2026**

The full-scale invasion by the Russian Federation in February 2022 radically changed Ukraine's financial situation, causing a significant drop in GDP, a sharp increase in the budget deficit and enormous needs for financing defence, social commitments and reconstruction. International financial support has become a key pillar of macro-financial stability, enabling the Government of Ukraine to avoid financial collapse and sustain the country's vital functions.

## **Volumes and structure of international financial assistance (2022-2025)**

During 2022–2025, Ukraine received unprecedented volumes of international assistance totaling 138.9 billion USD. The main donors were institutions of the European Union, the USA, the International Monetary Fund (IMF), the World Bank, as well as individual G7 countries and other partners. This assistance came in the form of grants (which do not require repayment), concessional loans (with low interest rates and long repayment terms), and in the form of a conditional debt obligation, the Extraordinary Revenue Acceleration for Ukraine (ERA), implemented by the Ministry of Finance in cooperation with G7 countries and the EU. The ERA mechanism, totaling up to 50 billion USD, involves directing loan funds to Ukraine, which will be repaid and serviced using future revenues obtained from frozen Russian assets.

- 2022: Ukraine received approximately 32.1 billion USD in international financial assistance. The lion's share consisted of grants and loans from the USA, the EU, the IMF, and Canada.
- 2023: The volume of funding increased significantly, reaching approximately 42.6 billion USD. The European Union became the largest donor, providing substantial macro-financial assistance, while support from the USA remained significant. The IMF continued the implementation of its extended financing programs.
- 2024: International assistance remained high, estimated at 41.6 billion USD. The main driver was the EU's Ukraine Facility program (totaling 50 billion euros for 2024–2027), which provided regular tranches contingent on meeting conditions. Support from the USA, although subject to some delays due to domestic political disputes, continued to arrive but showed a trend toward a reduction in the grant component.
- 2025: As of July 15, the total volume of external financing amounts to 30.5 billion USD. The total need for external financing by the end of 2025 is 39.3 billion USD.

**In 2025, there were significant changes in the financing of needs, driven by several key factors:**

- Significant reduction in US support: This is perhaps the most significant factor. Against the backdrop of domestic political changes in the US, in particular the election of President Donald Trump, there has been a radical review of foreign spending policy. The 'America First' policy has led to the prioritisation of domestic issues and the minimisation of financial investments in external conflicts. This has resulted in an almost complete absence of direct budgetary support for Ukraine from the US in 2025, in contrast to previous years, when American grants and loans were among the largest sources of funding.
- Conditionality of EU support under the Ukraine Facility program: Although the Ukraine Facility program is long-term and large-scale, its implementation directly depends on Ukraine's fulfillment of the agreed Reform Plan. These conditions cover a wide range of areas, from the rule of law and anti-corruption efforts to macroeconomic stabilization and structural reforms. Unfortunately, by 2025, problems with meeting the schedule and completeness of these requirements have already emerged. According to preliminary data, Ukraine is already receiving approximately 1.5 billion euros less in tranches planned for 2025 due to non-fulfillment of reform indicators. In particular, issues with appointing an independent head of the Economic Security Bureau (ESB) and attempts to introduce legislative changes that could undermine the independence of key anti-corruption bodies, such as

the National Anti-Corruption Bureau of Ukraine (NABU) and the Specialized Anti-Corruption Prosecutor's Office (SAPO), have already caused concern and mistrust among European partners. Further rollback or sabotage of reforms could lead to a significant reduction or even a complete cessation of EU funding, which would have catastrophic consequences for the Ukrainian budget.

- o Decline in activity of other donors: Some other countries and international organisations may also review their aid volumes, citing growing domestic economic problems, changing geopolitical priorities, or expectations of more significant progress in reforms in Ukraine.

### **Ukraine's needs for 2026**

Forecasting Ukraine's financial needs for 2026 is a difficult task, as it depends on many variables, including the dynamics of hostilities, the level of domestic economic activity, reconstruction needs, and demographic changes. It is further complicated by the International Monetary Fund's requirement to reduce the budget deficit from 19.4% in 2025 to 9.9% in 2026. As stated by Finance Minister Serhiy Marchenko ["We are talking about hundreds of billions of hryvnias in lower expenditures compared to the budget we currently have"](#).

Ukraine's budget deficit for 2026 according to the [draft budget](#) amounts to 2 trillion 544.5 billion hryvnias (55.68 billion USD), of which domestic financing is 419.6 billion UAH (9.18 billion USD) and external financing is 2 trillion 124.9 billion UAH (46.5 billion USD). This underscores the critical need to strengthen internal resource mobilization, as the projected international support - especially considering the trends of 2025 - may be insufficient to fully cover these needs. The reduction in external financing highlights the urgent need to develop and implement effective domestic revenue-generating mechanisms, which is the main objective of this study.



# ASSESSMENT OF KEY TAX EVASION SCHEMES AND MEASURES TO MINIMIZE THEM

The shadow economy remains one of the biggest challenges for Ukraine’s financial stability, especially under martial law. According to various estimates, its size ranges from 20% to 40% of GDP, representing colossal losses for the state budget. In particular, the EY Economic Analysis Team, in its [report](#) from March 2025, estimated Ukraine’s shadow economy at 19.3%. The Ministry of Economy, in its 2021 [report](#) estimated the shadow economy at 32%. Higher estimates [have](#) been presented by government officials: notably, Minister Yulia Svyrydenko in June 2024 assessed the level of the shadow economy at approximately 40%, and the head of the Verkhovna Rada’s Tax Committee, Danylo Hetmantsev, stated in an interview that about half of the economy operates “in the shadows,” with certain sectors, such as trade, reaching 60–70%. Combating shadow schemes is not only a matter of fiscal discipline but also crucial for restoring trust in state institutions and ensuring a level playing field for business.

According to [research](#) by the Institute for Social and Economic Transformation and the CASE Ukraine analytical centre, the main shadow schemes that have the most harmful effect on the economy are:

Nº	Violation scheme	2020 p.	2022 p.	2023 p.
1	“Black” salaries (paid in envelopes)	110–150	70–110	115–230
2	Violation of customs rules, smuggling, and corruption at the border	70–120	80–150	120–167

3	Counterfeit goods, illegal trade in excise goods	38–43	46–51	35–40
	– including:			
	– tobacco products		19–21	17–20
	– petroleum products		16–18	10–12
	– alcohol		11–12	8
4	Transit-conversion centers, tax gaps	17–25	20–30	30–40
5	Scheme-based VAT credit (VAT “twists”)	24–30	16–20	15–18
6	Abuse of the simplified taxation system (entrepreneurs instead of hiring, underreporting turnover)	7–16,3	5–12,3	11,5–22
7	Offshore schemes, transfer pricing, and BEPS	15–35	13–28	9–11
8	Shadow market for leasing agricultural land and real estate	10–21	5–6	1–2

As can be seen from the table, the main shadow schemes are as follows:

- “Black salaries” (paid in envelopes) and violations of customs regulations (smuggling, border corruption) are the largest schemes in terms of the volume of losses.
  - Losses from “black” salaries increased from 70–110 billion UAH in 2022 to 115–230 billion UAH in 2023, indicating a growing shadowization of the labor market, likely due to the war and increased fiscal pressure.
  - Customs violations consistently generate huge losses: 70–120 billion UAH in 2020, rising to 120–167 billion UAH in 2023. This underscores a critical problem with border control and indicates the persistence, and possibly even strengthening, of corruption schemes during wartime.

- Counterfeit goods and illegal trade in excise goods remain a significant problem, although total losses in 2023 (35–40 billion UAH) slightly decreased compared to 2022. However, tobacco products consistently generate substantial losses (17–20 billion UAH in 2023).
- Transit-conversion centers and “tax gaps” show a clear trend of increasing losses: from 17–25 billion UAH in 2020 to 30–40 billion UAH in 2023. This indicates an intensification of schemes for money laundering and tax evasion through fictitious transactions.
- Scheme-based VAT credit (“VAT twists”) shows a positive trend, with losses decreasing from 24–30 billion UAH in 2020 to 15–18 billion UAH in 2023. This may be the result of certain efforts by tax authorities to combat these schemes.
- Abuse of the simplified taxation system (entrepreneurs instead of hiring employees) increased in 2023 (11.5–22 billion UAH) compared to 2022, indicating businesses’ adaptation to wartime conditions by minimizing their tax burden.
- Offshore schemes, transfer pricing, and BEPS show a noticeable decrease in losses, from 15–35 billion UAH in 2020 to 9–11 billion UAH in 2023. This may be related to the implementation of international standards to combat base erosion and profit shifting (BEPS) and the overall reduction in business activity with large international companies due to the war.
- The shadow market for leasing agricultural land and real estate experienced a significant drop in losses: from 10–21 billion UAH in 2020 to only 1–2 billion UAH in 2023. This is likely due to territorial occupation, hostilities, and decreased activity in the real estate and agricultural land markets.

Overall, the table confirms that, despite the war, the key sources of budget losses remain the shadow labour market and customs space. This indicates priority areas for the state in combating the shadow economy and mobilising domestic financial resources for the needs of defence and reconstruction in Ukraine.

## 2.1. Grey imports and smuggling

**Gray import** (import of goods without proper customs clearance or with understated customs value) and smuggling (illegal movement of goods across the state border) are among the most widespread and large-scale schemes of tax and customs evasion. These practices cause multi-billion losses to the budget annually, distort the competitive environment, and contribute to the growth of corruption.

## Scales and channels:

- **Understatement of customs value:** One of the most common schemes, where importers declare a significantly lower value of goods than their actual price in order to reduce the tax base for VAT, customs duties and excise taxes. This scheme is particularly common for consumer goods, electronics, clothing and footwear.
- **Substitution of goods or HS codes:** Declaring different goods or using HS codes that imply lower duty rates or no excise.
- **“Postal” schemes:** Abuse of duty-free import rules for international postal shipments, where commercial batches are split into smaller parcels to avoid taxation.
- **False declaration and “twists”:** Importing goods without proper declaration, using forged documents, or creating chains of fictitious companies to sell goods on the domestic market without paying taxes.
- **Direct smuggling:** Moving goods outside customs control, often through “green corridors” or hidden channels. This is especially common for tobacco products, alcohol, fuel, and raw materials such as amber or round timber.
- **Geographical hubs:** Major flows of “gray” imports and smuggling traditionally pass through western borders (from the EU) and seaports (prior to the full-scale war).

## Assessment of loss volumes:

Accurately estimating budget losses from “gray” imports and smuggling is difficult due to the hidden nature of these schemes. However, various [analytical studies](#) and assessments by [deputies](#) indicate multi-billion annual losses, which in some years exceed **50–70 billion UAH**.

Current data confirm the growing scale of the problem. According to the results of an [annual survey](#), conducted by the Institute for Economic Research and Policy Consulting, in 2024 the share of “gray imports” / commodity smuggling in Ukrainian markets was on average estimated at 11.6%. This is a record high for the entire period of the study, although a significant share of “Don’t know” responses (40.6%) may affect the reliability of the data. Among the available results, the highest share of “gray imports” was recorded in the Volyn region (36.8%).

## Specific examples clearly demonstrate the scale of the losses:

- **Apple product market:** In the first three months of 2025, only 47,869 iPhones were [officially imported](#) into Ukraine, while operators registered 250,166 new iPhones. This means that 202,297 units of devices (over 80%) were brought in illegally. A

similar situation is observed in other categories of Apple products:

- **Mac:** 7 823 officially, 11 735 illegally (60% shadow market).
- **iPad:** 9 295 officially, 21 689 illegally (70% shadow market).
- **Apple Watch (AW):** 11 418 officially, 17 127 illegally (60% shadow market).
- **AirPods (AP):** 16 856 officially, 71 859 illegally (81% shadow market).

Overall, Apple's market volume for these three months amounted to UAH 11.2 billion, of which about 80% is in the shadow economy. Direct budget losses from non-payment of VAT and customs duties at the border during this period amounted to about UAH 1.8 billion.

- **Tobacco market:** According to a [KPMG research](#), Ukraine saw a significant reduction in the illegal cigarette market in 2024: its volume decreased by 2.4 billion cigarettes (29%), and its share in total consumption fell to 16.1%. This decline, mainly due to a reduction in the volume of contraband marked 'For Duty Free Sale' and counterfeit goods, is the largest among all countries surveyed. Despite this positive trend, Ukraine remains the second largest illicit market in Europe and continues to be a significant source of cigarette smuggling into EU countries, with flows of illicit products from the country even increasing slightly in 2024.

### Measures for minimization and reform challenges:

Combating “gray” imports and smuggling requires comprehensive reforms of the State Customs Service, which can be divided into institutional and anti-corruption measures, largely reflected in **the National Revenue Strategy and the State Customs Service Reform Plan for 2024–2030**.

1. Anti-corruption measures and “customs reboot”:

- **Internal measures:** 489 measures were implemented to prevent the appointment of dishonest individuals. **A pilot project was launched to use individual portable video cameras (IPVs) at the Rava-Ruska border crossing point**, with plans to scale up by 2027 for continuous monitoring of customs formalities.
- **Law on the “Customs Reboot”** (Law of Ukraine № 3977-IX): This law establishes new procedures for service in customs authorities, including the certification of officials, systematic integrity checks (including polygraph testing), rotation, the formation of a personnel reserve, as well as a new system of motivation and social guarantees.

- **Competitive selection of management:** Law № 3977-IX provides for competitive selection for the position of Head of the State Customs Service, following the example of best practices of NABU, SAPO, and NACP, with the involvement of international experts. The competition commission shall consist of three representatives proposed by the Ministry of Finance and three representatives from international organisations.
- **Key problems and challenges:** Despite legislative progress, the implementation of the “customs reboot” faces serious obstacles. As of the end of May 2025, the selection commission for appointing the Head of the Customs Service is still absent, although the Cabinet of Ministers was supposed to form it back in November–December 2024. This delay, which is an obligation to the IMF (the disbursement of a \$425.1 million tranche depends on it), is explained, among other reasons, by the suspension of project funding from USAID. An additional “nuance” is Cabinet Resolution № 1365, which introduces the position of the Government Commissioner for Customs Reform. His broad powers could completely override the “political independence” of the future Head of the Customs Service provided for in Law № 3977-IX, calling into question the success of the reform. Overall, the Reform Index rated the customs reform at 2+ out of 5 points, which is a low score.

## 2. International cooperation:

- In **2024, the exchange of preliminary customs information with Romania and Moldova** was established. It is planned to expand this process to other countries by 2029.
- Work continues on establishing joint control at border crossing points with neighbouring countries, which will enhance the effectiveness of border control.

## 3. Institutional changes and harmonisation of legislation:

- Internal changes **include increasing customs officers’ salaries** and improving the overall personnel management system based on European practices.
- On 19 April this year, a number of **European integration changes to the current Customs Code of Ukraine regarding authorisations came into force.**
- Active work is underway to develop **a new Customs Code of Ukraine**, which is a key recommendation of the European Commission’s Report on

EU enlargement. The new code is expected to be approved by the Verkhovna Rada in January 2026.

### **Proposals for minimising grey imports and smuggling:**

To effectively address the issue of 'grey' imports and smuggling, it is necessary to focus on the following key areas:

- **Immediate and unconditional fulfillment of obligations regarding the «customs reboot.»** This includes the urgent formation and commencement of work of the selection commission to choose a new, independent, and competent Head of the State Customs Service. Overcoming bureaucratic and political obstacles, such as Cabinet Resolution №1365, is critically important to ensure the efficiency of leadership and the independence of the institution.
- **Scaling up transparency and automation of the State Customs Service's activities.** Cultivating the practice of using individual portable video cameras by customs officers should become a nationwide standard. At the same time, it is extremely important to fully implement modern IT solutions – **the electronic or E-Customs system** – as well as to adopt draft law № 10380 on introducing automated customs clearance in «Diiia,» which will reduce the human factor and corruption risks.
- **Formation of effective KPIs for the State Customs Service.** These indicators should be focused not on meeting a «plan,» but primarily on **minimizing «schemes,» reducing the level of shadow imports, ensuring transparency of procedures, and increasing budget revenues.** Continuous monitoring of their implementation is necessary for a more well-grounded evaluation of the service's performance.
- **Introduction of the institution** of customs representation to enhance transparency and protect the interests of businesses.
- **Strengthening international cooperation.** It is necessary to continue efforts to ensure the exchange of customs information with all major trading partner countries and to create an effective mechanism for automated comparison of relevant documents and customs values of goods. This will make it possible to effectively identify cases of undervaluation and other manipulations.
- **Eradication of the practice of 'presumption of guilt'** in tax and customs administration. Creating a comfortable environment for legal business without unjustified inspections and corrupt pressure will contribute to its development and legalisation.

- **Strengthening responsibility for smuggling:** It is necessary to review the legislation on the criminalisation of large-scale commodity smuggling, as the current administrative penalties are often not an effective deterrent.

The implementation of these comprehensive proposals will not only significantly reduce the volume of 'grey' imports and smuggling, providing tens of billions of hryvnia in additional revenue to the state budget, but will also improve the investment climate and create more equitable and transparent conditions for doing legal business in Ukraine.

## 2.2. Salary «in envelopes»

**«Salary «in envelopes»**– It is the payment of employees' wages fully or partially “off the books,” without being recorded in the company's accounting records and without paying the corresponding taxes and fees (personal income tax – PIT, military levy – ML, and unified social contribution – USC). This phenomenon is one of the largest sources of losses for the state budget and the Pension Fund of Ukraine, undermines employees' social guarantees, and distorts competition in the labor market.

### Scales and channels:

- **Reasons for prevalence:** The high tax burden on the wage fund in Ukraine has historically encouraged employers to minimize costs through shadow payments. Although the unified social contribution (USC) rates have been reduced, the overall burden remains significant. Low tax culture and insufficient effectiveness of state control also play an important role.
- **Sectors of prevalence:** “Envelope salaries” are most common in areas with a high share of cash transactions and/or a large number of low-skilled workers – retail trade, food service, construction, agriculture, services, and transportation. A significant part of the IT sector also uses optimization schemes by registering employees as private entrepreneurs (FOPs), which, although legal, often imitates employment relationships in order to minimize taxes.
- **Typical schemes:**
  - **Full shadowing:** The employee is not officially registered at all.
  - **Partial shadowing:** The employee is registered for the minimum wage, while the rest is paid “in an envelope.”
  - **Imitation of private entrepreneurship (FOP):** Instead of formal employment, the worker registers as a private entrepreneur (FOP) and receives payment

for “services” at significantly lower tax rates (for example, a 5% unified tax), which represents a quasi-shadowing of employment relations.

### **Assessment of losses:**

The budget losses from ‘envelope salaries’ are enormous. According to the table provided, in **2023**, estimates of losses from “**black salaries**” ranged from **115 to 230 billion UAH**. This figure is the highest among all shadow schemes presented in the table and shows significant growth compared to 2022 (UAH 70-110 billion) and 2020 (UAH 110-150 billion). Such growth during a full-scale war may be associated with:

- The desire of businesses to minimise costs during an economic crisis.
- Increased mobilisation risks, which cause some employees to avoid formal employment.
- Reduced effectiveness of state control during wartime.

These losses consist of unpaid amounts of personal income tax (PIT), military levy, and, critically, the unified social contribution (USC), which is the main source of funding for the Pension Fund and social insurance funds.

### **Measures to minimise:**

Effective combating of shadow employment requires a comprehensive approach combining incentives for legalisation, tighter controls and preventive measures:

#### **1. Reducing the tax burden on the payroll fund (FOP-Private Entrepreneurs):**

- **Reforming USC and PIT:** Consider the possibility of further optimizing USC and PIT rates to make legalization more attractive for employers and employees. This could be implemented through the consolidation of payroll taxes into a single tax or through a progressive taxation scale with a high non-taxable minimum (to be discussed in more detail in section 3.2.2).
- **Incentives for de-shadowing:** Development of temporary programs that would encourage employers to bring salaries “out of the shadows,” for example, through preferential tax regimes for a certain transitional period for companies that commit to legalizing all employees.

#### **2. Strengthening state control and accountability:**

- **Effective monitoring:** Strengthening the work of the State Labor Service of Ukraine and tax authorities to detect cases of undeclared labor and “envelope” salaries through risk analysis and information exchange between

agencies (Tax Service, Pension Fund, State Labor Service).

- **Administrative and criminal liability:** Enhancing responsibility for the use of unofficial labor and payment of “gray” salaries, with an emphasis on the inevitability of punishment. Applying significant fines and, in cases of systematic violations, criminal liability for officials.
- **Improving detection mechanisms:** Using modern IT tools to analyze bank transactions, cash operations, and to reconcile production/sales data with the number of officially registered employees and their wage levels.

### 3. Raising awareness and legal protection for workers:

- **Information campaigns:** Conducting broad information campaigns for the population on the benefits of formal employment (social guarantees, pensions, sick leave, holidays, protection from unscrupulous employers) and the risks of ‘shadow’ employment.
- **Simplification of procedures for protecting rights:** Creation of accessible and effective mechanisms for employees to report cases of ‘envelope wages’ or undeclared work without fear of reprisals from their employer. Ensuring confidentiality and legal protection for such persons.

### 4. Improving the regulation of FOPs (Private Entrepreneurs):

- **Distinguishing between employment and civil-law relations:** Improving legislation for a clearer distinction between where independent entrepreneurial activity of an FOP ends and employment relationships begin, which require appropriate taxation. This is especially relevant for the IT sector.
- **Strengthening control over activity types:** Verifying whether the actual activities of an FOP correspond to the declared NACE codes (KVEDs) and whether they are not a hidden form of employment.

### 5. Development of cashless payments:

- Encouraging the use of non-cash payments for all types of transactions, which reduces the scope for cash shadow payments.

The implementation of these measures will not only reduce budget losses, estimated at UAH 115-230 billion in 2023, but also ensure social justice, increase pension provision for citizens and create a level playing field for honest businesses.

## 2.3. Illegal trade in excise goods

Illegal trade in excise goods such as tobacco products, alcohol and petroleum products is one of the oldest and most persistent schemes of the shadow economy in Ukraine. Its existence leads to significant losses to the state budget, creates unfair competition for legal businesses, and poses a threat to consumer health due to the lack of quality control.

### Scales and channels:

**The illegal market for excise goods is formed mainly from three main sources:**

**1. Smuggling:** Importing goods from abroad without paying customs duties and excise tax. This is particularly relevant for tobacco products and alcohol from neighbouring countries with lower excise rates.

**2. Illegal production (counterfeit):** Production of goods without licences, in 'shadow' factories or workshops, using counterfeit excise stamps or without them. Such goods are often of low quality and dangerous. This is typical for all types of excise goods, including counterfeit alcohol and 'bootleg' fuel.

**3. Unrealised Duty Free/Export:** Goods that were produced for duty-free trade (Duty Free) or export but are illegally sold on the domestic market of Ukraine without paying excise duty and VAT.

### Assessment of losses:

According to the table provided, illegal trade in excisable goods consistently generates significant losses for the budget:

- **2020:** 38–43 billion UAH
- **2022:** 46–51 billion UAH
- **2023:** 35–40 billion UAH

Despite a slight decrease in 2023 compared to 2022, the total amount of losses remains critically high. A breakdown by product type shows:

- **Tobacco products:** Consistently high losses – 19–21 billion hryvnia in 2022 and 17–20 billion hryvnia in 2023. According to [current](#) data Kantar Ukraine, in February 2025, the illegal tobacco market again showed growth to 14.1%, resulting in annual budget losses of 24.2 billion UAH. The volume of the shadow cigarette market in Ukraine is estimated at over 5 billion cigarettes.
- **Petroleum products:** 16–18 billion UAH in 2022 and 10–12 billion UAH in 2023.

- **Alcohol:** 11–12 billion UAH in 2022 and 8 billion UAH in 2023.

It is important to note that a significant portion of counterfeit products (for example, 33% of tobacco products) bear signs of forged excise stamps, and more than half of illegal products marked as Duty Free or intended for export but sold in Ukraine are produced by domestic factories (such as the Vynnykivska tobacco factory). This indicates deeply rooted internal schemes.

### **Measures to minimise:**

Effective combating of illegal trade in excisable goods requires comprehensive and decisive action:

#### **1. Strengthening control over production and circulation:**

- **Effective goods traceability system:** Implementation and full operation of an electronic system for monitoring the circulation of excise goods (e.g. **Track & Trace** for tobacco products in accordance with the EU Directive). This will allow tracking the movement of each unit of product from the manufacturer/importer to the end consumer, identifying 'leaks' at any stage.
- **Mandatory licensing:** Strict control over compliance with licensing conditions by manufacturers and distributors.
- **Market monitoring:** Regular inspections of retail and wholesale outlets, warehouses and petrol stations for illegal products.

#### **2. Combating smuggling (supplements section 2.1):**

- **Technical equipment and automation of customs:** Use of scanning systems, electronic customs, risk management systems to detect illegal shipments at the border.
- **International cooperation:** Active exchange of information with border and customs services of neighbouring countries to stop cross-border channels.

#### **3. Strengthening accountability and inevitability of punishment:**

- **Criminalisation of illegal production and distribution:** Strengthening criminal liability for the manufacture, storage and distribution of excisable goods without excise tax stamps of the established sample or with counterfeit stamps.
- **Confiscation of equipment and products:** Mandatory confiscation of equipment used for illegal production and all detected counterfeit or

contraband products.

- **Fighting corruption:** Strict measures against officials who ‘protect’ the illegal circulation of excisable goods.

#### 4. Tax policy:

- **Balanced excise policy:** Gradual increase of excise duties to European levels (to be discussed in more detail in section 3.1), but taking into account the purchasing power of the population and the risks of increasing the shadow economy. A sharp jump in excise duties could stimulate the growth of the illegal market.
- **Optimisation of excise duty rates:** Consideration of the possibility of revising the structure of excise duties for certain goods in order to reduce incentives for shadowing (e.g. introduction of a minimum excise duty liability for tobacco products).

#### 5. Information and educational work:

- Conducting campaigns for the population on the dangers of illegal excisable goods to health and their negative impact on the economy.

The implementation of these measures will significantly reduce the volume of illegal trade in excise goods, providing significant additional revenue to the state budget, as well as contributing to the protection of citizens’ health and the creation of fairer conditions for legal business.

## 2.4. Trade without fiscalisation

Trade without fiscalization means conducting payment transactions for goods (services) without using cash registers (RRO) or online cash registers (PRRO), that is, without issuing a fiscal receipt to the buyer and without recording the transaction in the tax system. This allows business entities to hide the actual volume of their income and, accordingly, evade paying taxes (mainly the unified tax for FOPs, as well as VAT for large taxpayers).

#### Scales and channels:

- **Reasons for prevalence:** The main reasons are businesses’ desire to minimize tax obligations, avoid accounting and control, as well as insufficient oversight by tax authorities.

- **Sectors of prevalence:** This scheme is particularly common among private entrepreneurs (FOPs) operating under the simplified taxation system, as well as in small and medium retail outlets, markets, service sectors (hair salons, car service stations, beauty salons), food service establishments, passenger transportation, taxi services, courier deliveries, and online sales.

### Typical schemes:

- **Complete absence of RRO/PRRO:** The business entity simply does not use fiscal registers.
- **Issuing “goods receipts” or “tickets” instead of fiscal receipts:** Documents without fiscal significance are issued to simulate the legality of the transaction.
- **Not processing part of transactions through RRO/PRRO:** The seller processes only part of the payment transactions through the fiscal register, while the rest are conducted “off the books.”
- **Online trade:** A particular problem is trade via social networks, messengers, and classified ad platforms, where payments are often made to individuals’ personal bank cards, making tracking and taxation impossible.

### Assessment of losses:

Although in the provided table “Trade without fiscalization” is not highlighted as a separate category, its impact is integrated into other schemes, such as “Abuse of the simplified system” (section 6). According to this table, losses from **“Abuse of the simplified system (FOP instead of employment, underreporting turnover)” in 2023 are estimated in the range of 11.5–22 billion UAH.** A significant portion of these losses comes specifically from underreporting turnover through non-fiscalized transactions.

### Budget losses from untaxed trade include:

- **Underpayment of the single tax:** Sole proprietors under the simplified taxation system declare lower incomes than they actually receive.
- **Underpayment of VAT:** For VAT payers, transactions that are not fiscalized fall out of the taxation base.
- **Violations in the field of employment:** Part of the non-fiscalized turnover may be used to pay «salaries in envelopes,» which, as we have already seen, is the largest source of losses.

## Measures to minimise:

### 1. Expansion of the use of software-based fiscal cash registers (PRRO).

- **Simplicity and accessibility:** Ensuring maximum simplicity and free use of software-based fiscal cash registers (PRRO) for all categories of businesses. State-provided PRROs must be convenient and functional.
- **Information support:** Conducting awareness campaigns among entrepreneurs about the advantages of using PRROs and the liability for failing to use them.
- **Mandatory use for all categories:** Reviewing and, where possible, unifying the requirements regarding the mandatory use of fiscal cash registers (RRO/PRRO) for most types of activities, eliminating exemptions that are used for minimization purposes.

### 2. Strengthening control and accountability:

- **Data analysis:** Active use of analytical tools by tax authorities to identify high-risk taxpayers (for example, discrepancies between purchase volumes and declared sales volumes, or significant cash inflows to accounts not supported by fiscalization).
- **“Buy and Verify” campaigns:** Encouraging consumers to check fiscal receipts through the State Tax Service’s dedicated online platforms. Implementing “cashback” mechanisms for customers who identify non-fiscalized transactions, in order to promote public oversight.
- **Tougher penalties:** Increasing fines for failure to issue fiscal receipts and for non-use of RRO/PRRO, with an emphasis on the inevitability of enforcement.
- **Conducting control purchases:** Strengthening the activities of tax authorities in performing control (test) purchases to detect violations.

### 3. Regulation of online commerce:

- **Monitoring online platforms:** Developing mechanisms for monitoring commercial transactions carried out via social networks, messengers and marketplaces, with a focus on those that use personal card accounts for commercial purposes.
- **Introduction of mandatory fiscalisation for all online transactions:** Regardless of the payment method, if a transaction is commercial in nature,

it must be fiscalised.

- **Restrictions on the use of personal cards for business purposes:** Awareness-raising and tax incentives for businesses to switch to corporate accounts.

#### **4. Encouraging cashless payments:**

- Further expansion of cashless payments in all areas, as they are more transparent and easier for tax authorities to track.

The implementation of these measures will significantly reduce the volume of untaxed trade, contributing to the de-shadowing of the economy and providing additional billions of hryvnia in revenue to the state budget, as well as increasing the transparency of the business environment.

## **2.5. Gambling business**

The legalization of the gambling business in Ukraine in 2020 aimed to bring the sector out of the shadows and generate budget revenues, which was partially successful: in 2023, the industry paid over UAH 10 billion in taxes. However, alongside the legal market, a large-scale shadow sector continues to operate, undermining the positive effects of the reform.

The fundamental cause of abuses was a strategic mistake – the launch of the market without simultaneously implementing a key control instrument, the State Online Monitoring System (SOMS). The absence of this system, which would provide the government with real-time access to data on all transactions, created conditions for tax evasion schemes to flourish.

The problem also has a national security dimension: up to 90% of illegal online casinos operating in Ukraine have Russian origins. This represents not only a channel for tax evasion but also a tool for capital outflow and the collection of sensitive financial information about Ukrainian citizens.

### **Scale and channels**

The shadow sector dominates the gambling market. According to various estimates, its share ranges from 39% to over 53% of total turnover, which means that approximately half of the industry's financial flows bypass the state treasury.

The aggressive expansion of illegal operators is leading to a massive outflow of players

from legal platforms: every quarter, between 20,000 and 25,000 Ukrainians switch to shadow sites. The reasons for this are the advantages offered by illegal operators: no verification, the possibility of avoiding taxation on winnings, and no limits.

### **The following key channels and schemes are used to operate the shadow market:**

- **Miscoding:** The most common scheme in which acquiring banks, in collusion with operators, assign a fraudulent merchant code of another service to gambling payments (for example, «purchase of flowers» instead of «gambling»). This makes the transaction invisible to financial monitoring. At least nine banking institutions were involved in the schemes.
- **P2P transfers («drops»):** The use of an extensive network of individuals' personal bank accounts to process payments. This masks commercial transactions as ordinary transfers between citizens.
- **«Mirrors»:** The rapid creation of dozens of copies of blocked illegal sites on new domain names, allowing activity to continue almost uninterrupted.

### **Volume of abuses**

The financial losses to the state from abuses in the gambling business are enormous. Overall expert estimates of annual budget losses range between 10–15 billion UAH.

- According to [data from the Verkhovna Rada's Temporary Investigation Commission](#), In 2024 alone, the budget lost UAH **23.4 billion** in taxes due to the activities of the shadow market.
- According to the audit by the Accounting Chamber, in 2022–2023 the budget lost **1.9 billion UAH** due to abuses of the simplified taxation system (2%).
- The activities of the illegal sector directly undermine the legal market. It is forecasted that by the end of 2025, the legal industry will lose at least **15 billion UAH** in revenue compared to expected figures.

In addition to direct financial losses, the uncontrolled market causes significant social harm, leading to the uncontrolled spread of gambling addiction (ludomania), especially among military personnel, which places an additional burden on the healthcare system.

### **Measures to minimise and challenges of reform**

An effective fight against the shadow market requires a comprehensive approach that combines technological, financial and law enforcement measures.

#### **1. Technological control:** Immediate and full-scale launch of the **State Online Monitoring**

**System (SOMS).** This system will provide the government with the ability to track every bet and transaction in real time, making schemes such as miscoding impossible in the legal segment. The new regulator, PlayCity, has already begun its implementation process.

**2. Financial accountability:** Introduction of strict and inevitable sanctions against banks and payment systems found to be facilitating miscoding. Sanctions should include multi-million fines exceeding the potential profits from illegal activities, up to the revocation of banking licenses.

**3. Strengthening law enforcement:** Transition of the Bureau of Economic Security (BEB) and the Security Service of Ukraine (SBU) from merely blocking websites to proactive investigations aimed at exposing and dismantling the organizational cores of the shadow business, its owners (especially those with Russian connections), and its financial networks.

**4. Regulatory and tax reform:** Completion of the tax reform (adoption of draft law No. 2713-d) to create stable and competitive conditions for legal businesses. Strict enforcement of the new, more stringent rules regarding gambling advertising is also necessary to protect vulnerable groups of the population.





# OPTIMISATION OF TAX POLICY

Optimising tax policy is one of the most direct and effective ways to increase state budget revenues. However, this process requires a balanced approach that takes into account not only the fiscal effect, but also the impact on business activity, the investment climate, social justice and the fight against the shadow economy. The goal of tax changes should not be simply to increase rates, but to create a system that encourages legalisation, stimulates economic development and ensures stable revenues.

## 3.1. Potential for increasing excise taxes

Excise taxes are one of the most important sources of budget revenue, as they are levied on the final consumption of certain goods (alcohol, tobacco, fuel, electricity, etc.) and, in addition to their fiscal function, also perform a regulatory function aimed at reducing the consumption of harmful goods. **Increasing excise taxes is one of the most obvious opportunities for quickly filling the budget, especially in wartime. Excise tax is the fourth most important source of tax revenue for the state budget (after VAT, personal income tax and corporate income tax), and the main types of excisable products that generate budget revenue are tobacco products, fuel and alcoholic beverages.**

**The problem of illegal production and circulation of excisable goods and the role of control:**

Despite the potential for increasing excise revenues, the problem of **illegal production and circulation of excisable goods** remains one of the main obstacles to fully exploiting

this potential. It leads to **direct underfunding of the state budget**, including funds for Ukraine's defence, as the bulk of excise tax goes to the state budget. Local budgets also suffer losses, as they receive 13.44% of the excise tax on produced/imported fuel and the excise tax on retail sales of excisable goods.

**According to experts of the Temporary Investigative Commission (TIC) of the Verkhovna Rada of Ukraine, the annual budget losses from the illegal production and circulation of excise goods (tobacco, alcohol, fuel) amount to approximately 35 billion UAH. Breakdown of losses: fuel – 9–10 billion UAH, tobacco products – 18–20 billion UAH, alcoholic beverages – 7–8 billion UAH.** Although in 2024 the volume of losses slightly decreased, these schemes remain among the most common methods of tax evasion.

**To investigate the factors contributing to this activity, the Temporary Investigative Commission conducted significant work, highlighting the importance of strengthening the corresponding oversight by tax authorities, as well as the Bureau of Economic Security (BES) and other law enforcement agencies:**

- **Providing information to law enforcement agencies:** The TI (Temporary Investigative Commission) provided the Bureau of Economic Security of Ukraine, the State Tax Service of Ukraine, and the National Police of Ukraine with a compiled list of physical outlets, websites, and Telegram channels involved in the illegal sale of excise goods. This is critically important for prompt response and holding violators accountable.
- **Establishing cooperation:** The Commission established collaboration with associations of excise goods producers, public organizations, and conscientious citizens to systematically receive information about points of illegal sales. This approach strengthens public oversight and the effectiveness of detection.
- **Information and analytical work:** In collaboration with economic experts from leading analytical centers, thorough work has been conducted, including:
  - Analysis of monthly excise tax revenues to budgets by type of excisable goods.
  - Development of a methodology for quarterly assessment of the shadow market and tax burden.
  - Monthly monitoring of the volume of goods sold based on data from the cash register data accounting system (CRDA).
  - Monthly monitoring of websites and Telegram channels selling illegal tobacco

products and alcoholic beverages.

These activities by the TIC demonstrate that effective control, based on analytics, information sharing and joint efforts, is the key to successfully combating the shadow market for excise goods.

## **Specification of goods and potential income:**

### **1. Tobacco products:**

- **Potential:** Ukraine has commitments to the EU regarding the gradual increase of excise tax rates to the minimum level established by EU Directive No. 2011/64/EU. This implies reaching a level of €1.8 per 1,000 cigarettes (or approximately €70 per 1,000 cigarettes in total excise tax) by 2025, and further adjustments by 2027. Current rates in Ukraine are significantly lower.
- **Fiscal effect:** Each step of excise tax increase (for example, by 20% annually) can generate an additional **10–15 billion UAH** in annual budget revenues.
- **Current state of the shadow market:** According to research by Kantar Ukraine LLC, in the first quarter of 2024, the level of illegal tobacco trade slightly decreased to 19.1% (compared to 14.1% in February 2025, based on preliminary data, indicating fluctuations). The share of counterfeit products decreased to 8.7%, and «Duty Free» products to 9.2%. However, **the projected size of the illegal tobacco market in Ukraine in 2024 was estimated at 16.1%**, with the volume of the shadow cigarette market at 6.3 bn units, and annual budget losses of approximately **21.9 billion UAH**. The highest levels of illegal tobacco distribution were recorded in Dnipropetrovsk (18%), Odesa (13%), Kyiv city and Kyiv region (11%), Kharkiv (10%), Khmelnytskyi (8%), and Lviv (6%) regions.

### **2. Fuel (petrol, diesel fuel, liquefied gas):**

- **Potential:** Excise taxes on fuel are a significant source of revenue. Increasing excise rates to European standards, which began to be implemented in 2024–2025 in line with EU integration commitments (draft law № 11256), will continue to generate additional funds.
- **Fiscal effect:** Each stage of excise tax increases can generate an **additional 20–30 billion UAH per year**.
- **Current state of the shadow market:** According to experts from the Economic Expert Platform and the NGO «Institute of Socio-Economic Transformation,» as a result of the operations of illegal gas stations, the

total losses to the state and local budgets amount to **9–10 billion UAH** per year, corresponding to a 15% shadow share of the industry. The turnover of counterfeit petroleum products through the network of illegal gas stations reaches 500,000 tons per year, leading to losses in VAT and excise taxes (which, since 2024, are directed to the general fund of the state budget, causing underfunding of defense). The Oil and Gas Association of Ukraine estimates that annually over **1.5 million tons** of fuel are sold without fiscalization (RRO). Personnel at illegal gas stations often work without official employment, resulting in underpayment of personal income tax, military levy, and social security contributions. Illegal gas stations also create environmental hazards and deprive local communities of land tax revenue.

### 3. Alcoholic beverages:

- **Potential:** Excise duties on alcohol are also lower than in Europe. A consistent increase in rates could significantly increase revenues.
- **Fiscal effect:** An increase in excise duties on beer, wine and spirits could bring in an additional **5-10 billion UAH per year**.

### Measures to minimise and exploit potential:

Effective use of excise revenue potential requires comprehensive measures that enhance the effectiveness of both fiscal policy and control mechanisms:

**1. Harmonisation of excise duty rates with the EU and gradual increase:** Consistent approximation to European excise duty rates is an integral part of European integration commitments and will ensure stable revenue growth. It is important to find a balance between the fiscal effect and the risk of stimulating the shadow market.

### 2. Strengthening control and administration:

- **Implementation of effective product traceability systems:** Full implementation of **Track & Trace** systems for tobacco products in compliance with EU requirements.
- **Digitalization and analytics:** Active use of IT solutions for risk analysis and monitoring of the circulation of excise goods (based on data from fiscal devices, reports, and public information). **Joint analytical work of tax authorities, the Bureau of Economic Security, and the National Police is critically important.**
- **Combating illegal production:** Regular raids and elimination of illegal alcohol and tobacco production facilities.

- **Control over gas stations:** Strengthening inspections of the legality of gas station operations, documentation, and the use of fiscal and software-based cash registers (RRO/PRRO).

**3. International cooperation:** Active exchange of information with the customs services of neighboring countries to combat smuggling.

**4. Strengthening accountability:** Criminalization of the illegal production and distribution of excise goods, stricter fines, and mandatory confiscation of property and equipment.

**5. Coordination of authorities:** Ensuring close and effective coordination among the State Tax Service (STS), the Bureau of Economic Security (BEB), the National Police, the Security Service of Ukraine (SBU), and the Prosecutor’s Office to systematically counter the shadow circulation of excise goods.

### **Total potential:**

With a balanced excise policy and **effective strengthening of control by tax authorities and the Bureau of Economic Security**, the potential increase in budget revenues from excise taxes in 2026 and the following years could amount to an additional **40–60 billion UAH** annually, taking into account existing EU integration commitments. This requires not only raising tax rates but also effectively closing the “loopholes” in the system that allow the shadow market to thrive.

## **3.2. Improving taxation of personal income**

Improving the personal income tax system is a key element of tax reform, which aims not only to increase budget revenues, but also to ensure social justice, reduce wage shadowing and stimulate economic development. This is a comprehensive approach that includes both improving administrative efficiency and a possible review of rates and approaches to taxation of various types of income.

### **3.2.1. Increase in “luxury tax”**

A ‘luxury tax’ (or wealth tax) is a tool aimed at increasing fiscal revenues by taxing expensive assets and luxury items. Its purpose is to ensure a more equitable distribution of the tax burden and to replenish the budget at the expense of high-net-worth individuals.

#### **Potential and mechanisms:**

- **Taxable items:** Certain elements of a “luxury tax” already exist in Ukraine, but they

could be expanded and strengthened. These include:

- **Real estate:** Increasing property tax rates for real estate (apartments over 60 sq. m and houses over 120 sq. m) for large and/or high-value properties, especially in major cities and prestigious districts. A progressive taxation scale based on the property's value could be introduced.
- **Vehicles:** Reviewing and increasing transport tax rates for luxury-class cars, possibly expanding the list of such vehicles or reducing their age threshold. Introducing a tax on expensive motorcycles, yachts, and private aircraft (where applicable).
- **Luxury consumer goods:** Considering the introduction of an additional excise tax or an increased VAT rate on certain categories of luxury items (for example, high-end jewelry, watches exceeding a certain price threshold, fur products, and exclusive works of art).
- **Fiscal effect:** Precise calculations of potential revenues require a detailed analysis of property registers and their market values. However, according to expert estimates, increasing the “luxury tax” could generate an additional 3–7 billion UAH annually, depending on the depth and scope of the implemented measures. This figure could be higher in the case of effective administration and detection of hidden assets.
- **Social aspect:** The introduction or strengthening of the “luxury tax” has strong public support, especially in wartime conditions, when society demands greater fairness in the distribution of the fiscal burden.

### **Challenges and risks:**

- **Administration:** Effective administration of the “luxury tax” requires the establishment and operation of high-quality property registers with up-to-date assessed values, which can be a complex task.
- **Evasion:** High-income individuals may use tax avoidance schemes (registering assets under other persons' names, using offshore structures, or undervaluing property).
- **Market impact:** Excessively high rates may trigger “capital flight” or reduce investment in certain market segments.

### **3.2.2. Progressive taxation scale and introduction of a tax-free minimum**

The current flat PIT rate (18%) in Ukraine is often criticized for its regressive nature, as it

creates the same tax burden for both low-paid and high-paid workers. The introduction of a progressive taxation scale and a non-taxable minimum is a common international practice aimed at increasing social fairness and the efficiency of the tax system.

### Concept:

- **Progressive scale:** Income is taxed at different rates depending on its amount. The higher the income, the higher the tax rate. This allows the tax burden to be redistributed in favour of less affluent segments of the population.
  - For example, rates of 10% for low incomes, 18% for medium incomes and 20-25% for high incomes could be introduced.
- **Non-taxable minimum (or significant tax social benefit):** A portion of income that is not taxed at all or is taxed at a zero rate. This helps ensure that individuals with low income, which barely covers basic living needs, do not bear an excessive tax burden. It can also serve as a tool for de-shadowing the economy, as the legalization of “minimum” wages becomes fiscally more advantageous.

### Fiscal effect and social aspect:

- **Increase in revenues:** The introduction of a progressive scale can significantly increase PIT revenues to the budget, especially if the upper rates are applied to truly high incomes. The potential fiscal effect may amount to an additional 15–30 billion UAH annually, depending on the number of brackets, their rates, and the size of the non-taxable minimum.
- **Reduction of the tax burden for the poor:** The non-taxable minimum will reduce the tax load on low-income individuals, increasing their purchasing power and stimulating consumption.
- **Social justice:** This will strengthen the principle of tax fairness (“the one who can pay more, pays more”).
- **Incentive for de-shadowing:** For part of the “shadow” incomes (especially low ones), official declaration may become more advantageous if they fall under lower tax rates or the non-taxable minimum.

### Challenges and risks:

- **Administration:** The complexity of administration, especially for tax agents. However, with the development of digital technologies, this is becoming less problematic.
- **“Shadowing” of high incomes:** There is a risk that highly paid professionals

or business owners will seek ways to avoid higher rates (for example, through dividend payments, sole proprietor schemes, or offshore structures). This requires comprehensive measures, including combating “envelope salaries” (p. 2.2) and abuses of sole proprietorship schemes (p. 2.4).

- **Application thresholds:** It is important to properly set income thresholds for each rate to avoid the “poverty trap” and maintain incentives for income growth.

### 3.2.3. Taxation of asset increases (indirect methods of income control)

Taxation of asset increases is an indirect method of controlling citizens’ income, which involves verifying the compliance of declared income and tax deductions with the value of acquired assets (real estate, cars, investments, etc.). If a significant difference is found between the value of the assets acquired and the officially declared income, the person may be required to explain the source of the funds, and in the absence of such an explanation, to pay tax on the amount of such “unconfirmed” asset growth.

#### Concept:

- **Zero declaration (capital amnesty):** Usually, before introducing such a tax, a “zero declaration” or tax amnesty is conducted, allowing citizens to legalize their previously undeclared assets by paying a small fee. This creates a “clean” starting point for further monitoring.
- **Monitoring of large purchases:** Tax authorities receive information about significant property acquisitions (from notaries, banks, and registries).
- **Tax control:** In case of discrepancies between income and expenses, the tax service may request explanations.
- **Additional taxation:** If the origin of funds is not confirmed, a tax rate is applied to the amount of asset increase (often high, for example, 18% PIT + 1.5% MS).

#### Fiscal effect and social aspect:

- **Potential:** Depends on the amount of “shadow” assets and the state’s readiness for strict control. It can potentially bring tens of billions of hryvnias in the long term, as its main goal is not so much a one-time budget replenishment as systematic de-shadowing and reducing incentives to hide income. After the 2021–2022 tax amnesty, which did not bring significant results, regular monitoring of assets should become a more effective tool.
- **De-shadowing:** Encourages citizens to declare real incomes and pay taxes, since hidden funds will not be possible to use legally for large purchases.

- **Social justice:** Fights corruption and illegal enrichment, as officials and other persons living beyond their means can be held accountable.

### Challenges and risks:

- **Legal aspects:** Requires a clear legal framework that complies with the constitutional rights of citizens.
- **Corruption risks:** Increased opportunities for abuse and pressure on businesses by regulatory authorities if strict mechanisms for controlling their activities are not introduced.
- **Trust:** Success depends on the level of trust in the state and its ability to ensure fair and transparent administration.
- **Personal data protection:** Need to ensure adequate protection of confidential information about citizens' financial status.

The implementation of these changes in personal income taxation requires in-depth analysis and broad public discussion, as they have both significant fiscal potential and important social and economic implications.

### 3.3. Taxation of goods from foreign online stores

The issue of taxation of goods purchased from foreign online stores is becoming increasingly relevant with the development of e-commerce. Significant volumes of such purchases, which arrive in Ukraine via postal and express delivery, are often made outside the scope of proper tax control, leading to budget losses and creating unequal competitive conditions for Ukrainian retailers.

#### The essence of the problem and its scale:

The main problem lies in the existence of limits on duty-free imports of goods for individuals. In Ukraine, there is a limit of **€150 per parcel** for duty-free imports. This means that shipments worth up to €150 are not subject to import duties and VAT. Although this limit is lower than in some countries (e.g. the United States), it still creates opportunities for evasion schemes:

- **Splitting of commercial consignments:** Commercial batches of goods exceeding the 150 EUR limit are artificially divided into several smaller parcels, each of which

does not exceed the established threshold. This allows avoidance of customs duties and VAT payments, resulting in significant budget losses.

- **Undervaluation:** Declaring a lower value of goods in accompanying documents to fit within the duty-free limit or to minimize tax liabilities.
- **Unequal competition:** Ukrainian online stores and retail chains that pay all taxes (VAT, customs duties, corporate income tax, payroll taxes) find themselves at a disadvantage compared to foreign sellers and “grey” importers. This stimulates shadow imports and reduces budget revenues.
- **Administrative complexity:** The large volume of small postal shipments complicates effective control by customs and tax authorities.

### **Assessment of losses:**

Previously, there were no accurate and public estimates of budget losses directly from ‘grey’ imports through foreign online stores in terms of postal imports. However, **the introduction of an electronic customs clearance system for postal and express shipments has made it possible to significantly increase the coverage of international postal traffic and better assess its scale.**

According to the National Bank of Ukraine, as a result of these changes, the volume of imported goods delivered as postal shipments reached **1.6 billion USD in Q1 2025 and 3.5 billion USD** for the entire 2024 year. This represents a significant increase compared to previous estimates, which were **53 million USD for Q1 2025 and 228 million USD for 2024.**

This radical clarification of the NBU data indicates that the real volumes of postal **imports are significantly larger than previously believed**, which in turn underscores the huge potential for budget losses from the abusive use of duty-free limits and splitting schemes. Even with a duty-free limit of 150 EUR, with such turnover volumes - part of which is non-fiscalized - the budget misses out on significant amounts of VAT and customs duties. The analysis of “grey” imports and smuggling (as in point 2.1), in particular the case of Apple products, where up to 80% of imports are illegal, clearly demonstrates that a large share of these goods may be entering precisely through online store channels and subsequent illegal importation.

### **Measures to minimize and increase the efficiency of taxation:**

To effectively tax goods from foreign online stores and combat evasion schemes, comprehensive measures are needed:

#### **1. Reduction or cancellation of duty-free limit:**

- **Alignment with European standards:** Consider lowering the current limit of €150, or abolishing it altogether, for all goods coming from outside the EU, with few exceptions (gifts, personal effects of negligible value). Many EU countries apply a zero limit for goods purchased from online stores from third countries, or mechanisms where VAT is paid directly upon purchase.
- **Fiscal impact:** This move could significantly increase budget revenues from VAT and customs payments from online purchases.
- **Challenges:** May cause consumer dissatisfaction and will require significant modernization of customs procedures to process a large number of small payments.

## 2. Introduction of the VAT payment mechanism at the point of purchase (OSS system):

- **EU model (Import One Stop Shop – IOSS):** Implementation of a system under which foreign online stores or platforms (marketplaces) register in Ukraine (or through a special tax representative) and independently collect VAT from buyers at the point of sale, then remit it to the Ukrainian budget. This allows avoiding tax payments at the border and speeds up delivery.
- **Advantages:** Simplifies procedures for buyers, ensures tax revenues, and increases transparency.

## 3. Strengthening control and information exchange:

- **Automated data exchange:** Establishing automated data exchange on postal items between postal and express carriers and customs authorities, using risk management systems to identify suspicious items. **The already implemented electronic customs clearance system is a positive step that needs to be developed and used to its full potential.**
- **International cooperation:** Strengthening cooperation with customs and tax authorities of other countries to combat cross-border evasion schemes.

## 4. Information work:

- Conducting an educational campaign for the population about the rules of duty-free import and responsibility for their violation.

## 5. Stimulating legal imports:

- Creating favorable conditions for the activities of legal importers and

Ukrainian retailers to reduce the attractiveness of «gray» schemes.

Increasing the efficiency of taxing goods from foreign online stores is an important step toward creating a level playing field for business and ensuring additional budget revenues, which is critical for the financial stability of the state. Especially considering the revised NBU figures for postal imports, this area requires immediate and decisive tax reform and strengthened control.

### 3.4. Increase in duties on non-critical imports

Increasing the duty on non-critical imports is a fiscal measure aimed at generating additional revenue for the state budget, as well as reducing the demand for foreign currency for the purchase of goods that are not vital for the population or critical for the functioning of the country's economy in wartime.

#### Rationale and objectives:

In conditions of martial law, when the state budget is experiencing a colossal burden and gold and foreign exchange reserves are strategically important, restrictions on non-critical imports perform several functions:

- **Fiscal:** Direct increase in state budget revenues through higher customs duty rates.
- **Currency:** Reduction of foreign currency outflow, which could be used for the purchase of critically important imports (e.g., for defense needs, energy resources, critical equipment) or for stabilizing the hryvnia exchange rate.
- **Stimulation of domestic production:** Theoretically, higher prices for non-critical imported goods may encourage the development of domestic production of similar products, contributing to job creation and strengthening the economy.

#### Trade balance dynamics and the need for measures:

The need for such measures becomes even more evident when analyzing the dynamics of Ukraine's trade balance. According to the National Bank of Ukraine, imports of goods significantly exceed exports, resulting in a substantial negative trade balance.

- In **2024**, imports of goods amounted to **\$66.2 billion**, while exports of goods totaled only \$35.8 billion. Thus, **the negative trade balance of goods for 2024 was \$30.4 billion.**
- In the first quarter of **2025**, imports of goods reached **\$17.6 billion**, while exports

totalled \$10.2 billion. Accordingly, **the negative trade balance for first quarter 2025 was \$7.4 billion.**

Such a significant trade deficit puts pressure on the foreign exchange market and the country's gold and foreign exchange reserves. In these circumstances, measures to restrict non-critical imports, such as increasing tariffs, are justified to stabilize the macroeconomic situation.

#### **Justification according to WTO rules:**

It is important to note that the introduction of an additional import duty (or levy) is possible even within the framework of Ukraine's membership in the World Trade Organization (WTO). According to **Article XII of the General Agreement on Tariffs and Trade 1994 (GATT-1994) and the Understanding on the Balance-of-Payments Provisions of GATT-1994**, WTO members, in the event of a deterioration in the balance of payments, have the right to take restrictive measures. Preference is given to price-based measures, which include additional import duties. This provision allows Ukraine to use such instruments to protect its financial stability, citing the critical balance-of-payments situation.

#### **Categories of «non-critical» imports:**

##### **«Non-critical» imports usually include goods that are not:**

- Raw materials and components for domestic production.
- Critical equipment and technologies.
- Vital goods for the population (for example, certain groups of medicines, basic food products, which are not sufficiently produced domestically).
- Defense goods.

##### **Instead, the list of goods on which duties may be increased often includes:**

- Expensive consumer goods: Some types of luxury cars, expensive jewelry, branded clothing and footwear, luxury items.
- **Some types of household appliances and electronics** that have domestic analogues or are not a primary necessity.
- **Certain categories of food products** that are imported, if there is sufficient domestic production or their significant value.
- **Some services** that can be provided on the territory of Ukraine.

## Potential fiscal impact:

Estimating potential revenues from increasing tariffs on non-critical imports is complex and depends on many factors:

- **Clarity in defining “non-critical” imports:** The challenge lies in determining the specific list of goods so as not to harm related industries or consumers.
- **Customs duty rates:** The extent of the increase in customs duty rates.
- **Demand elasticity:** How sensitive demand for these goods is to price changes. A sharp increase may lead to a significant reduction in imports and, consequently, a smaller fiscal effect.
- **Scale of shadow imports:** Higher customs duties may stimulate the growth of smuggling and “grey” imports if customs control is not strengthened (as discussed in p. 2.1).

Taking into account these factors, the potential additional revenue from increasing duties on non-critical imports could range from **5 to 15 billion UAH annually**. This is a rather conservative estimate, as the exact list of goods and rates would require a separate in-depth analysis.

## Challenges and risks:

- **Classification:** The greatest challenge is the objective classification of goods as “critical” or “non-critical” without creating “grey areas” and opportunities for corruption. A clear and transparent list is essential.
- **Impact on inflation:** Higher customs duties may lead to an increase in prices for imported goods and affect the overall inflation level.
- **Smuggling introduction:** As noted above, high customs tariffs always stimulate shadow schemes, which requires strengthened control.
- **Trade relations:** Although WTO rules allow such measures in exceptional cases, their implementation may still require explanatory work with partner countries.
- **Administrative burden:** Increased administrative load on businesses and customs authorities.

## Recommendations:

**1. Creation of a clear list of non-critical imports:** Development of a transparent list of product categories with Ukrainian Classification of Goods for Foreign Economic Activity

codes to which higher customs duty rates will apply, with regular review and adaptation to the needs of the economy.

**2. Gradual implementation and monitoring:** The introduction of changes should be gradual, with constant monitoring of their impact on the market, inflation, and import volumes.

**3. Strengthening customs control:** Alongside increasing customs duties, it is necessary to intensify efforts against smuggling and grey imports to ensure that additional revenues are not “absorbed” by the shadow sector.

**4. Communication with business:** Conducting consultations with business representatives and industry associations to minimize negative consequences.

Increasing duties on non-critical imports is a tool that can bring additional revenue to the budget in wartime, but its implementation requires a balanced approach and careful analysis of potential consequences.

### **3.5. Permission for the export of military products with the introduction of export duties**

In the context of mobilizing domestic financial resources and developing the national defense-industrial complex (DIC), the issue of permitting the export of military products while simultaneously introducing an export duty is a subject of discussion. This measure could potentially become a new source of revenue for the state budget; however, it requires an extremely cautious and strategically balanced approach, especially under the conditions of the ongoing full-scale war.

#### **Rationale and objectives:**

The main idea of this measure is to use surplus or specific production capacities of the domestic defense industry to generate foreign exchange revenues that can be used to finance defense needs or general budget expenditures. The mechanism provides for:

- **Export permit:** The removal or liberalization of existing restrictions on the export of certain types of military products.
- **Introduction of export duty:** The establishment of a certain percentage of the value of exported military products to be paid to the state budget.

#### **Consideration of options by the Cabinet of Ministers of Ukraine:**

## **The Cabinet of Ministers of Ukraine is considering three main options for regulating Ukrainian arms exports, each of which has its own characteristics and potential consequences:**

**1. Targeted approval of export contracts:** This is the current practice, which means that the export of military technologies is not legally prohibited, but each export contract requires individual approval by the government. This option ensures maximum state control but is slow and may limit the ability of the defense-industrial complex (DIC) to respond quickly to market demands.

**2. Mechanism of 50% of the volume of Ukrainian contracts:** This option provides that manufacturers may export up to half of the volume of their state contracts. At the same time, they will be required to allocate part of their export revenue for the purchase of weapons for the Armed Forces of Ukraine. This is intended to stimulate production but may be complex to administer and may not fully account for the market's potential.

**3. 20% export duty on foreign sales:** Under this scenario, 20% of the value of arms exports would be directed to a special fund used to finance weapons procurement for the Ukrainian military.

Both options, 50% of the contract value and 20% of the customs duty, are intended to provide financial resources for additional purchases of weapons for the Armed Forces of Ukraine. However, the issue of providing the Ukrainian army with the necessary weapons before allowing exports remains relevant.

### **Advantages of the third option and the proposal regarding export duty:**

The third option, which provides for permission to export military products for all licensed business entities subject to payment of export duty, is the most attractive for a quick and significant replenishment of the budget, especially if it is combined with the liberalization of licensing procedures. Advantages of this option:

- **Maximizing export potential:** Allowing all licensed entities to export, not just manufacturers, enables a wider network of agents who can effectively find buyers and organize logistics. This can significantly increase overall export volumes.
- **Stimulating competition and efficiency:** Healthy competition among exporters will help increase sales efficiency, find new markets, and streamline processes, which will ultimately have a positive impact on budget revenues.
- **Decentralization and transparency:** With strict licensing, proper customs clearance, and effective control, the export duty system can bring significant amounts of arms trade out of the shadows, providing official budget revenues.

- **Flexibility:** Allows for faster response to changes in demand on the global arms market and adapts export strategy.
- **Targeted defense financing:** Revenues from customs duties to a special fund provide direct and transparent financing of procurement for the Armed Forces of Ukraine.

As for the export duty rate, it is **proposed to set it at 10%**, although the Cabinet of Ministers is considering the option of 20%. The 10% rate is more reasonable at the initial stage for the following reasons:

- **Export stimulation:** A lower duty rate will be more attractive for potential exporters without creating excessive financial burdens that could make Ukrainian products uncompetitive in the global market. This will allow export volumes to grow more quickly.
- **Reduction of shadowing risks:** A higher duty rate may increase incentives to use shadow schemes and evade taxes, especially in the sensitive arms trade. A 10% rate is a more balanced option, providing significant revenue while minimizing such risks.
- **Flexibility for future adjustment:** An initial 10% rate will allow for assessing the actual export volume and its market impact. Subsequently, with stable growth in volumes and refined control mechanisms, the rate can be gradually revised upwards.

### **Key challenges and risks (requiring careful analysis):**

**1. Priority of national defense: The most important aspect is the unconditional fulfillment of the needs of the Armed Forces of Ukraine.** The export of military products should **only be permitted if domestic demand for weapons and ammunition is fully and preferentially met.** Any export activity that could slow down or jeopardize rearmament and the supply of the Ukrainian army is unacceptable.

**2. Production capacity:** Does the domestic defense-industrial complex (DIC) have sufficient surplus production capacity to meet both domestic and export demand, especially considering the need for continuous expansion of production for the Armed Forces of Ukraine?

**3. Competition in the global arms market:** The global arms market is highly competitive. It is necessary to assess the competitiveness of Ukrainian products, their compliance with international standards, and the presence of sustainable demand.

**4. Risks of corruption and shadow schemes:** Trade in military products is a high-profit and sensitive area, increasing the risks of corruption and illegal circulation. The introduction of an export duty and regulation will require extreme transparency and

strict control.

**5. International restrictions and sanctions:** International sanctions and restrictions on arms trade, as well as reputational risks, must be taken into account.

**6. Participation in European programs:** It is important to leverage available opportunities, such as the **European Union's launch of the Rearm Europe program with a budget of €800 billion**. Ukraine, as a country actively developing its defense-industrial complex (DIC) and possessing unique experience in the use of modern weapons, **can and should claim a portion of these funds**. This would not only strengthen domestic production but also facilitate integration into the European defense industry.

### **Potential fiscal impact:**

According to the **Technological Forces of Ukraine, the current export potential of weapons is estimated at 2 billion USD**. This indicates significant opportunities for generating additional budget revenues.

Estimating potential revenue from export duties on military products is extremely complex and contains a high degree of uncertainty. It depends on:

- Volumes and nomenclature of products allowed for export.
- Domestic production capabilities over the needs of the Armed Forces of Ukraine.
- Global demand and prices for relevant types of weapons.
- The amount of the established export duty.

Based on the estimated potential of 2 billion USD and the proposed 10% duty rate, the potential additional revenue for the budget could amount to around **200 million USD annually (or approximately 8 billion UAH at the current exchange rate)**. However, at the current stage of the war, when all efforts are focused on meeting the needs of the Armed Forces of Ukraine, this potential is more of a **medium- to long-term prospect, to be realized after stabilization of the situation and significant development of the domestic defense-industrial complex (DIC)**.

### **Recommendations:**

**1. Unconditional priority of domestic needs:** Any export permit must be conditioned on the full and primary satisfaction of the needs of the Armed Forces of Ukraine.

**2. Creation of a clear regulatory framework:** Development of transparent legislation defining the list of military products that can be exported, licensing procedures, control mechanisms and export duty rates.

**3. Strict control and transparency:** Introduction of extremely strict control mechanisms over export operations to minimize corruption risks and ensure full receipt of duties to the budget. Active involvement of the Bureau of Economic Security and other law enforcement agencies.

**4. Market analysis and strategic planning:** Detailed analysis of the international arms market to identify the most promising niches and types of products, as well as strategic planning for the development of the defense industry, which will allow increasing volumes based on the needs of the Armed Forces of Ukraine and export potential.

**5. Use of revenues:** A clear definition of where export duty revenues will be directed (for example, to a special fund for the development of the defense industry, for rearmament of the army, or for social expenditures for veterans).

Permission to export military products with the introduction of duties is a powerful but complex tool that can significantly strengthen the financial capacity of the state and its own defense industry, but its implementation must be carried out with maximum responsibility and taking into account the primary interests of national security.



# INCREASE IN REVENUE FROM STATE PROPERTY MANAGEMENT

Effective management of state-owned assets is one of the most important tools for increasing state budget revenues. Ukraine possesses a significant number of state-owned enterprises (SOEs), real estate properties, and other assets that, if properly managed, can generate substantial dividends and contributions. Unfortunately, historically, this potential has been used inefficiently, leading to losses, corruption, and lack of transparency. Increasing revenues from the management of state assets requires a comprehensive set of measures aimed at maximizing the financial return from these assets.

## 4.1. Audit of financial statements of state-owned enterprises and increase in dividends from them

Many state-owned enterprises (SOEs) in Ukraine have traditionally shown low efficiency, unprofitability, or insufficient contributions to the budget. One of the main reasons is the lack of transparency, effective oversight, and proper auditing of their financial activities. Implementing mandatory, independent, and regular audits of SOE financial statements, as well as reviewing and increasing the standards for allocating a portion of net profits as dividends, are key steps toward addressing this situation.

### **Problem and its scale:**

- **Lack of transparency:** Many state-owned enterprises (SOEs) operate in a closed manner; their financial statements are often not public or not verified by independent auditors. This creates a breeding ground for corruption schemes, inefficient use of

resources, and fund diversion.

- **Low efficiency and unprofitability:** A significant portion of SOEs are unprofitable or operate on the edge of profitability, requiring budget subsidies instead of contributing to it.
- **Insufficient dividend allocations:** Even profitable SOEs often pay minimal or zero dividends to the budget, citing the need for reinvestment, although the real reasons may be linked to inefficient management or profit concealment.
- **Lack of accountability:** SOE management often does not bear proper responsibility for financial performance and management efficiency.

At the same time, recent government initiatives indicate positive changes in the approach to dividend policy. For example, **for 2023, the government planned to increase the allocation of a portion of SOEs' net profits to the budget, reflecting an understanding of the need to strengthen financial discipline and improve the efficiency of state asset management.**

## Mechanisms and measures:

### 1. Introduction of mandatory independent audit:

- **Regular audit:** All state-owned enterprises (SOEs), especially large and strategic ones, should undergo an annual independent audit of their financial statements in accordance with International Standards on Auditing (ISA).
- **Publication of results:** Audit outcomes (auditor reports and opinions) must be made publicly available and easily accessible to the public.
- **Role of DASU and the Accounting Chamber:** Strengthen the oversight functions of the State Audit Service of Ukraine (DASU) and the Accounting Chamber, which should monitor not only the use of budget funds but also the efficiency of SOE operations, using data from independent audits.

### 2. Review and increase of the dividend allocation standard:

- **Increase of the rate:** The current rate of allocating a portion of SOEs' net profits as dividends can be reviewed and raised. For example, the **government is already considering a draft law to increase dividend allocations to 80% for SOEs based on 2023 results.** This represents a significant step compared to previous practice.
- **Differentiated approach with clear justification:** It is important to apply

differentiated allocation standards depending on the industry, strategic importance, and investment needs. For instance, **for 2023, exceptions were proposed for “Ukrhydroenergo” (50% allocation) and “Energoatom” (30% allocation)**. These lower percentages are justified by the companies’ critical investment needs, particularly as **Energoatom accumulated around 60 billion UAH in profits, part of which (42 billion UAH) is planned to be directed toward completing the construction of Khmelnytskyi NPP Units 3 and 4.**

- **Control over the justification of reinvestments:** If an SOE requests to retain part of its profits for reinvestment, this must be supported by a clear business plan, feasibility assessment, and monitoring of implementation to prevent abuses. For example, in the case of Energoatom, an initial expectation of UAH 36 billion in dividends was reduced to UAH 18 billion due to a change in the allocation standard.

### 3. Strengthening corporate governance:

- **Independent supervisory boards:** Establish professional and independent supervisory boards for all major SOEs, responsible for overseeing financial activities, approving strategy, and appointing effective management.
- **KPI for management:** Set clear Key Performance Indicators (KPIs) for SOE management, including financial results and dividend allocations, with corresponding incentives linked to their achievement.

### Potential fiscal impact:

#### The impact of these measures is multifaceted:

- **Direct revenues:** Increased dividend allocations from profitable SOEs. Planned dividend payments to the budget based on **2023 results amount to approximately 45.4 billion UAH, of which 18 billion UAH** comes from state-owned enterprises (excluding banks, which have a separate allocation procedure – around 27.4 billion UAH). This already indicates significant progress. Further strengthening of control and improving efficiency will allow this amount to grow.
- **Reduction of losses and subsidies:** Enhanced oversight and increased efficiency will reduce SOE losses and, consequently, the need for state subsidies, freeing up budgetary funds.
- **Improvement of the investment climate:** Transparency and effective management of state assets will increase investor confidence and create more favorable conditions

for potential privatization of some SOEs in the future.

### **Challenges and risks:**

- **Resistance to the system:** Significant opposition from interest groups that benefit from the lack of transparency and inefficiency of SOEs.
- **Balance between investments and dividends:** The need to find a balance between generating dividends for the budget and maintaining the ability of SOEs to reinvest in their development and fulfill strategic functions, as in the case of Energoatom. It is crucial that the justification for reinvestments is fully transparent.
- **Audit quality:** Ensuring truly independent and high-quality audits, avoiding “in-house” or biased auditing firms.
- **Staff shortage:** Lack of qualified and ethical specialists for supervisory boards and executive positions.

### **Recommendations:**

- 1. Legislative enshrinement:** Clear legal establishment of the mandatory nature and standards of independent audits for all SOEs, as well as transparent rules for publishing reports.
- 2. Revision of dividend policy:** Review and approval of new, more ambitious dividend allocation standards by the Cabinet of Ministers of Ukraine, with clear criteria for exceptions, which must be exceptional and properly justified.
- 3. Engagement of international partners:** Possible involvement of international auditing firms for auditing the largest SOEs and international experts on supervisory boards to strengthen trust.
- 4. Strengthening accountability:** Introduction of personal responsibility for SOE management and supervisory board members for failure to meet financial plans and low dividend allocations.

The implementation of these measures is a fundamental step towards improving the efficiency of state property management, which will allow transforming state-owned enterprises from an expense object into a stable source of revenue for the state budget.

## **4.2. Increasing revenue from the use of seized assets (ARMA)**

The State Agency of Ukraine for the Identification, Tracing and Management of Assets

Obtained from Corruption and Other Crimes (ARMA) plays a key role in the management of seized property. The effectiveness of its work directly affects the state budget, as the task of ARMA is not only to preserve, but also to increase the value of these assets and receive income from them until their confiscation or return to their owners. Unfortunately, to date, the potential of this mechanism has not been fully utilized, although recent legislative changes are designed to correct this situation.

### **The essence of the problem:**

- **Low management efficiency:** Despite the significant volumes of seized assets (from real estate and corporate rights to funds and securities), their management is often inefficient. This leads to asset downtime, depreciation, low management income, or even losses.
- **Bureaucratic obstacles and complexity of procedures:** The procedures for transferring property to ARMA management, finding managers, conducting an assessment, and monitoring their activities are overly bureaucratic and lengthy, which delays the receipt of income.
- **Lack of transparency and corruption risks:** The processes for selecting managers and monitoring their activities often raise questions about transparency and may be prone to corruption risks.
- **Limited financial revenues:** The actual revenues that ARMA transfers to the budget are significantly lower than the potential volumes. Even with billions of dollars in seized assets, real revenues are measured in tens or hundreds of millions of hryvnias, not billions.

### **Mechanisms and measures to increase profitability:**

#### 1. Acceleration and simplification of transfer procedures:

- **Automation:** Introducing digital tools to more quickly transfer seized assets from law enforcement to ARMA and speed up the process of finding a manager.
- **Clear timings:** Establishing strict time frames for all stages of asset management – from the moment of seizure to transfer to management and sale/receipt of income.

#### 2. Increasing the efficiency of selection and control of managers:

- **Expanding the pool of managers:** Involving a broader circle of ethical and professional managers through transparent competitions with clear criteria.

**An important step has already been taken in this direction: the recently signed Draft Law № 13268, approved by the President, legally enshrines innovative approaches that ARMA has already implemented, including open competitions for selecting managers.** This increases transparency and reduces corruption risks.

- **Strengthening control:** Implementation of an effective system for monitoring and oversight of managers' activities, including regular audits of their financial reports on the management of seized assets.
- **KPI for managers:** Establishment of specific Key Performance Indicators (KPIs) for managers, linking their remuneration to the achieved financial results from asset management.

### **3. Expanding asset management and sales tools:**

- **Income models:** Focus on managing assets that can generate income (e.g., real estate rentals, corporate rights management of profitable enterprises, investing in government bonds).
- **Efficient sales:** Ensuring the quick and transparent sale of assets that depreciate quickly or are impractical to manage (e.g., perishable goods, vehicles that require significant maintenance costs).
- **Use of electronic platforms:** Maximizing the use of the “ProZorro.Sales” system for asset disposal. **Draft Law № 13268, in particular, legally enshrines the use of electronic auctions,** which are the most transparent and competitive mechanism.
- **Management of virtual assets:** An important innovation of Draft Law No. 13268 is granting ARMA the authority to manage cryptocurrencies, including the ability to sell virtual assets. This opens a new potential source of budget revenues, as a significant portion of criminal assets may be held in cryptocurrency.

### **4. Strengthening the institutional capacity of ARMA:**

- **Human resources:** Strengthening ARMA with qualified personnel, with proper motivation and protection from political pressure and corruption.
- **Technological equipment:** Providing ARMA with modern IT systems for accounting, monitoring and asset management.

### **Potential fiscal impact:**

A significant part of the seized assets is a source of shadow income or is idle, not bringing any benefit to the budget. Provided that effective mechanisms are introduced and the provisions of the new legislation are implemented, increasing the profitability of the management of seized property can bring from **1 to 5 billion UAH** of additional revenue to the state budget annually. This indicator is very dynamic and depends on the quantity and quality of the seized property, as well as on the real effectiveness of the reformed management system. It is important that these funds flow to the budget regularly, and not only from time to time after high-profile confiscations. Permission to manage cryptocurrencies can potentially significantly increase this amount.

### **Challenges and risks:**

- **Legislative gaps:** Despite the adopted law, there may be a need for further refinement of subordinate regulations to ensure effective implementation of the new provisions.
- **Resistance from corrupt circles:** Significant opposition from individuals whose assets have been seized and from interest groups that benefit from the inefficiency of the system.
- **Judicial processes:** Lengthy court proceedings that can delay the final confiscation of assets and their transfer to state ownership.
- **Valuation challenges:** Difficulty in objectively and impartially assessing the value of seized assets, especially virtual assets.

### **Recommendations:**

**1. Full implementation of Draft Law №13268:** Rapid development and adoption of all necessary subordinate regulations to fully launch the new mechanisms provided by Draft Law №13268.

**2. Digitization of processes:** Maximum digitalization of all stages of ARMA's operations to enhance transparency and reduce human factors.

**3. Independent expertise:** Involvement of international experts to audit ARMA's activities and develop best global practices.

**4. Strengthening cooperation:** Enhancing interaction between ARMA, law enforcement agencies, the judiciary, and other state bodies for a comprehensive and effective approach to asset management.

The effective work of ARMA is not only a source of budget revenues, but also a powerful anti-corruption tool that demonstrates the inevitability of punishment and the economic disadvantage of crimes. New legislative initiatives are an important step towards

increasing its effectiveness.

### 4.3. Acceleration of privatization, including seized sanctioned assets

Privatization of state property is one of the most effective mechanisms for filling the state budget, attracting investments, increasing the efficiency of asset management and reducing corruption. In conditions of a full-scale war, when the budget is experiencing a colossal burden, accelerating privatization processes, as well as the possibility of selling seized sanctioned property, acquire special importance.

#### The essence of the problem and potential:

- **Inefficiency of state assets:** Many state-owned enterprises remain unprofitable or operate well below their potential, absorbing budget funds instead of generating them.
- **Bureaucratic obstacles and lengthy processes:** Privatization procedures in Ukraine have historically been complex, lengthy, and often opaque, which deters potential investors.
- **Unrealized potential of seized assets:** In addition to traditional state assets, a significant amount is seized assets seized from corrupt officials, as well as sanctioned assets confiscated from individuals associated with the aggressor. This property often sits idle, depreciates, and does not benefit the state.
- **Need for funds:** Ukraine's state budget is in dire need of additional sources of funding, especially for defense needs and social programs.

#### Mechanisms and measures to accelerate privatization:

##### 1. Simplification of privatization procedures:

- **Minimization of bureaucracy:** Maximum simplification of the legislative and regulatory framework for privatization, reducing the number of permits and approval stages.
- **Shortening of timelines:** Establishment of strict and realistic deadlines for all stages of privatization, from preparation to sale.
- **“Privatization deregulation”:** Elimination of excessive regulatory barriers that slow down the process and make it less attractive for investors.

##### 2. Expansion of privatization objects:

- **Small and medium privatization:** Activation of small-scale privatization

through the “ProZorro.Sales” system, which allows for quick and transparent sale of smaller assets (real estate, small enterprises).

- **Large-scale privatization:** Unblocking and accelerating the privatization of strategically important enterprises, for which independent supervisory boards have already been established or are being created. It is important to involve international investors.
- **Privatization of seized sanctioned assets:** Legal regulation of a mechanism for accelerated privatization of seized assets already transferred to state ownership, especially those belonging to individuals sanctioned for aggression against Ukraine. This can include industrial facilities, other valuable real estate, or corporate rights.

### 3. Increasing transparency and investment attractiveness:

- **Open data:** Ensuring full access to information about privatization objects (financial statements, legal status, audits).
- **Guarantees for investors:** Ensuring protection of property rights of new investors and avoidance of re-privatization.
- **International marketing:** Active marketing of privatization opportunities on international investment platforms.
- **Potential fiscal impact:**
- **Direct revenues:** Privatization can generate significant, albeit one-time, revenues for the state budget. Depending on the volume and sale prices, the potential income from accelerated privatization could range from 5 to 20 billion UAH annually (or more if truly large and attractive assets are sold).
- **Reduction of budget expenditures:** Selling unprofitable SOEs will reduce the need for their subsidies from the budget, freeing up funds.
- **Increase in long-term tax revenues:** Private owners typically manage assets more efficiently, leading to higher profits, creation of new jobs, and, consequently, increased tax contributions (corporate income tax, VAT, personal income tax).
- **Attracting investments:** Privatization is a powerful tool for attracting both foreign and domestic direct investment, which will support production modernization and economic growth.

### Challenges and risks:

- **War conditions:** The ongoing war significantly reduces the investment attractiveness of assets and may lead to their sale at undervalued prices. It is necessary to balance the urgent need for funds with preserving asset value.
- **Anti-corruption measures:** Risks of unfair competition and corruption during privatization auctions, especially concerning large and attractive assets.
- **Social consequences:** Potential social impacts (such as job losses) in case of ineffective restructuring of enterprises by new owners.
- **Legal challenges:** Complexity and length of court proceedings related to the confiscation of sanctioned assets, which can delay their privatization.

### **Recommendations:**

**1. Development of a clear privatization «roadmap»:** Creation of a transparent privatization plan for each facility, with realistic deadlines and targets.

**2. Maximizing the use of electronic auctions:** Privatization through «ProZorro.Sales» for all types of facilities, where possible, in order to ensure maximum transparency and competition.

**3. Regulation of issues of sanctioned property:** Adoption of all necessary laws and by-laws for the prompt and effective confiscation and further privatization of seized sanctioned property, taking into account international experience.

**4. Creation of a favorable investment climate:** Ensuring stability of legislation, protection of investor rights and minimizing administrative pressure.

**5. Communication:** Active and transparent communication with the public and potential investors on the advantages and conditions of privatization.

Accelerating privatization, including the sale of confiscated sanctioned property, is a significant reserve for filling the state budget and increasing the overall efficiency of the economy, but requires a comprehensive, transparent, and balanced approach.



# OPTIMISATION AND REDUCTION OF NON-CRITICAL GOVERNMENT EXPENDITURE

In a state of martial law, when every resource is worth its weight in gold and the needs of defence and social protection are growing significantly, it is critically important not only to find new sources of income, but also to use existing funds as efficiently as possible. Optimising and reducing non-critical government spending is a fundamental step towards strengthening the country's financial stability and ensuring that priority needs are met. This process involves a thorough analysis of all budget items in order to identify and eliminate inefficient, excessive or non-priority expenditures.

## **The essence of the problem:**

- **Consequences of “peacetime”:** Many government programmes, administrative procedures and institutions were created or operated in peacetime, when the efficient use of funds was not always a top priority.
- **Bureaucratic inertia:** The government machine is prone to inertia, and changes in familiar spending patterns meet with resistance.
- **Inefficient use of resources:** Even in wartime, spending on projects that are not critically important or are implemented inefficiently may continue, leading to waste of funds.
- **Growing budget deficit:** Defence needs require significant and constant injections of funds, which places a huge burden on the budget and deepens its deficit.

## **Key areas for optimisation and reduction:**

## 1. Review and audit of all government programmes:

- **Effectiveness assessment:** Each government programme must undergo a thorough audit to assess its effectiveness, relevance and alignment with current wartime priorities. Programmes that demonstrate low performance or are not critical should be reviewed, reduced or cancelled.
- **Freezing non-priority projects:** Temporary suspension of funding for capital investment projects, construction, and repair of facilities (except for critical infrastructure and defence facilities) that do not have a direct impact on defence capabilities or the livelihood of the population.
- **Abandoning “image-building” expenditures:** Reducing expenditures on non-priority activities that are primarily image-building or entertainment-oriented (festivals, certain cultural events, participation in international exhibitions, unless related to the defence industry or critical imports).

## 2. Reduction of administrative costs of public authorities:

- **Staff optimisation:** Review and reduction of excess staff in government agencies, especially those whose functions are duplicated or have become obsolete.
- **Reduction of maintenance costs:** Reduction of costs for maintaining government institutions (rent, utilities, vehicle fleets, business trips, entertainment expenses).
- **Digitisation of services:** Maximise the digitisation of administrative services and internal processes in the state apparatus, which will reduce costs for paper document flow, postal services and reduce the need for excessive staffing.

### Potential fiscal effect:

Optimization and reduction of non-critical government expenditures have enormous potential. Depending on the depth and decisiveness of reforms, annual savings could range from 20 to 50 billion UAH, and even higher in the long term. These funds could be redirected to finance defense needs, social programs, the restoration of critical infrastructure, or reducing the budget deficit. Savings would be achieved not only through direct cuts but also by increasing efficiency and eliminating corruption schemes.

### Challenges and risks:

- **Political resistance:** Expenditure optimization often encounters significant

opposition from various ministries, agencies, and lobbying groups.

- **Social consequences:** Staff reductions may lead to a temporary increase in unemployment, necessitating the development of social support programs.
- **Risks to service quality:** Unbalanced cuts in spending can negatively affect the quality of public services.
- **Need for clear prioritization:** It is important to clearly distinguish between “critical” and “non-critical” expenditures to avoid harming the state’s vital functions.

## **Recommendations:**

**1. Establishment of an interdepartmental commission:** Establishment of a high-level interdepartmental commission headed by the Prime Minister or Deputy Prime Minister for Economic Affairs to conduct a full audit and review of government spending.

## **2. Introduction of a clear algorithm for reducing budget expenditures:**

- **Stage 1:** Detailed analysis and identification. Conduct a thorough audit of all budget items based on a “zero-based budgeting” approach, where each ministry/agency must justify every hryvnia of its expenditures. Identify overlapping functions, excessive programs, inefficient or non-priority spending, as well as expenditures that are not directly related to meeting defense needs and the country’s vital functions during wartime.
- **Stage 2:** Prioritisation of expenditure. Clear identification of critical expenditure (defence, social payments, critical infrastructure, health, education) and non-critical expenditure that can be reduced or frozen. Use of an importance and effectiveness matrix for each item of expenditure.
- **Stage 3:** Developing reduction plans. Creating specific reduction plans for each ministry and agency with clear deadlines and responsible persons. This may include staff reductions, reduction of administrative costs, review of resource consumption standards, and digitisation of services.
- **Stage 4:** Implementation and monitoring. Rigorous implementation of approved plans and continuous monitoring of their implementation. Regular public reports on the savings achieved and the reallocation of freed-up funds.

**3. “Zero-based budgeting”:** Applying the principle of ‘zero-based budgeting’ to certain items of expenditure, where each ministry/department must justify every hryvnia of its expenditure, rather than simply requesting an increase in the budget based on previous years.

**4. Public control:** Involving the public and experts in the process of analysing and monitoring public expenditure through open platforms and consultations.

**5. Strengthening accountability:** Introducing strict personal accountability for heads of state bodies for misuse of funds, inefficient spending and failure to comply with optimisation plans.

**6. Experience of international partners:** Study and implementation of best international practices in the field of public expenditure optimisation, especially from countries that have been in similar crisis situations and have successfully reformed their budgetary processes.

Optimization of government expenditures is not merely “tightening the belt,” but a strategic necessity for building a more efficient, transparent, and resilient state capable of meeting challenges and addressing the needs of its citizens.



# STIMULATING DOMESTIC PRODUCTION AND INVESTMENT

In the context of war and post-war reconstruction, **stimulating domestic production and attracting investment is critical for economic recovery, job creation, meeting defence needs and reducing dependence on imports.** This is not only a source of additional revenue for the budget through taxes and fees, but also the foundation for long-term sustainable economic development. The government should create the most favourable conditions possible for Ukrainian and foreign businesses that are ready to invest in production in Ukraine.

## The essence of the problem:

- **War risks:** High military risks significantly reduce Ukraine's investment attractiveness, scaring away both foreign and some domestic investors.
- **Bureaucratic barriers:** Even in peacetime, investors faced bureaucracy, corruption, complex licensing procedures and unstable legislation.
- **Lack of capital:** Ukrainian businesses often lack sufficient equity capital for large-scale investments, and access to credit remains limited.
- **Loss of production capacity:** A significant portion of production capacity has been destroyed or is located in temporarily occupied territories.
- **Shortage of skilled labour:** Population migration during the war has created a shortage of skilled workers.

## Key areas of promotion:

## 1. Improving the investment climate and protecting investments:

- **Security guarantees:** Development and implementation of mechanisms for insuring military risks for investments, including with the participation of international financial institutions and governments of partner countries.
- **Protection of property rights:** Strengthening judicial reform and ensuring effective protection of investors' rights, preventing raiding and illegal interference in business.
- **Deregulation:** Minimising the number of permits, licences and inspections that are barriers to business.
- **Tax incentives:** Introducing tax holidays or preferential tax rates for new production in priority sectors (e.g. defence industry, energy, construction materials production).

## 2. Access to financial resources:

- **State support programmes:** Expanding and simplifying access to state programmes offering affordable loans ("5-7-9%"), grants and guarantees for investment projects in priority sectors.
- **Assessment of the effectiveness of existing programs:** Current state economic stimulus programs are already showing their effectiveness. In particular, according to the Ministry of Economy, within the «eRobota» project, over 16,000 Ukrainians have already received microgrants through the «Own Business» program, with grants totaling 3.8 billion UAH, which allowed the creation of 35,000 new jobs. This program is especially important for internally displaced persons and veterans.
- Overall, according to analysts' estimates, **state economic stimulus programs (including "5-7-9%," "eRobota," and investment incentives) contributed to GDP growth by 0.64 percentage points in 2023**, with an expected contribution of 0.37 percentage points in 2024. The largest contribution to this growth came from the **"5-7-9%" program (0.45 percentage points in 2023)**. Total budget expenditures on these programs in 2023 amounted to 65.7 billion UAH, highlighting their significant role in supporting the economy.
- **Engagement of international funds:** Active cooperation with international financial organizations (EBRD, World Bank, IFC) and investment funds to

finance the restoration and development of production.

- **Public-private partnership (PPP) mechanisms:** Active use of PPPs to implement large-scale infrastructure and production projects.

### 3. Support for localisation of production:

- **Priority for Ukrainian manufacturers:** Introduction of priority mechanisms for Ukrainian manufacturers in the public procurement system, especially for military goods and reconstruction products.
- **Investments in the defence industry:** Special programmes to support and attract investments in the domestic defence industry, including technology transfer and joint production with foreign partners.

### 4. Infrastructure and logistics development:

- **Reconstruction and modernisation:** Priority restoration and modernisation of transport (roads, railways, ports) and energy infrastructure, which is critical for production and export.
- **Industrial parks:** Creation and development of industrial and technology parks with ready-made infrastructure and tax incentives for the establishment of new production facilities.

### 5. Human capital development:

- **Retraining programmes:** Launch retraining and training programmes to meet the needs of new industries, especially in technical and engineering professions.
- **Repatriation support:** Create incentives for Ukrainians to return home, including employment programmes and affordable housing.

### Potential fiscal effect:

Stimulating production and investment does not generate immediate budget revenues, but it is **key to sustainable revenue growth in the medium and long term.**

- **Increased tax revenues:** Growth in production leads to increased revenues from corporate income tax, VAT, personal income tax (through job creation) and other levies. This could amount to tens and hundreds of billions of hryvnia annually once investment cycles are underway. Existing programmes confirm this potential through their contribution to GDP and the creation of new jobs.

- **Reduced import dependency:** Increased domestic production reduces the need for imports, which has a positive impact on the trade balance and exchange rate.
- **Attracting capital:** Foreign direct investment (FDI) provides an inflow of currency, technology and expertise.

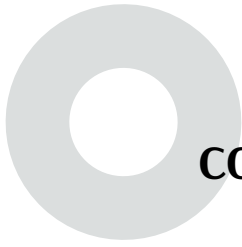
### Challenges and risks:

- **Duration of the process:** Creating a favourable investment climate and launching investment projects takes time.
- **Geopolitical risks:** The ongoing war and the unpredictability of the situation will remain a major deterrent for investors.
- **Corruption:** Residual levels of corruption may deter potential investors.
- **Competition:** Ukraine competes for investment with other countries that also offer incentives.

### Recommendations:

- 1. Develop a National Investment Strategy:** Clearly define priority sectors and regions for investment, taking into account reconstruction needs and security aspects.
- 2. Creation of a ‘single window’ for investors:** Maximum simplification of interaction between investors and state authorities, appointment of personal managers to support large projects.
- 3. Consistent judicial reform:** Ensuring the independence and effectiveness of the judicial system to protect property rights and resolve disputes.
- 4. International cooperation:** Active cooperation with international partners to attract guarantees, investment insurance and financial assistance.
- 5. Priority for the defence industry:** Creation of separate, simplified and fast procedures for investment and project development in the defence industry.

Stimulating domestic production and investment is a long-term investment in the country’s future, which will ensure not only financial stability but also Ukraine’s economic independence and sustainability. Existing programmes are already showing positive results, and their further optimisation and expansion should be a priority.



# CONCLUSIONS

Ukraine faces the challenge of reduced external financial assistance, particularly from the United States in 2025, due to domestic political processes and the election of Donald Trump, as well as the EU's conditional support linked to the implementation of the reform plan. Failure to implement reforms has already led to a shortfall of €1.5 billion in tranches from the EU in 2025, jeopardising further funding. In 2026, Ukraine's budget deficit could reach \$30-40 billion, underscoring the critical need to mobilise domestic resources.

## The main shadow schemes that lead to significant losses to the state budget are:

- **“Black salaries” (in envelopes):** Losses from this scheme increased from 70–110 billion UAH in 2022 to 115–230 billion UAH in 2023, making it the highest among all shadow schemes. This phenomenon is widespread in retail trade, food service, construction, agriculture, and the service sector.
- **Violations of customs rules, smuggling, and border corruption:** Losses from these violations remain consistently high, rising to 120–167 billion UAH in 2023. “Gray imports” and smuggling cause multi-billion losses to the budget, distort the competitive environment, and foster corruption. For example, in the first three months of 2025, about 80% of Apple products were imported illegally, resulting in 1.8 billion UAH in losses from unpaid VAT and customs duties alone. The illegal tobacco market in February 2025 grew to 14.1%, leading to annual budget losses of 24.2 billion UAH.
- **Transit-conversion centers, tax holes:** These schemes show losses increasing from 17–25 billion UAH in 2020 to 30–40 billion UAH in 2023.

- **Counterfeit goods, illegal trade in excise goods:** Total losses in 2023 amounted to 35–40 billion UAH, with tobacco products consistently generating significant losses (17–20 billion UAH in 2023).
- **Abuse of the simplified taxation system (FOP instead of employment, underreporting turnover):** Losses from this scheme increased in 2023 to 11.5–22 billion UAH.

**To minimize the shadow economy and increase domestic financial resources, the following measures are proposed:**

- **Reforming the State Customs Service:** Immediate fulfillment of obligations regarding the “customs reboot,” including the urgent formation and commencement of the selection commission to appoint a new head. It is important to overcome bureaucratic and political obstacles, scale up transparency and automation (electronic customs, video cameras), implement effective KPIs aimed at minimizing schemes and increasing budget revenues. International cooperation for the exchange of customs information should be strengthened, and legislation regarding the criminalization of large-scale goods smuggling should be reviewed.
- **Combating “envelope salaries”:** Reducing the tax burden on the payroll fund (for example, through reform of the unified social contribution and personal income tax), strengthening state control and liability for the use of unofficial labor (administrative and criminal responsibility), and improving mechanisms for detecting shadow payments (IT tools, transaction analysis). It is also important to raise employees’ awareness of their rights and the benefits of official employment, improve FOP regulation for a clearer distinction of employment relationships, and encourage cashless payments.
- **Countering illegal trade in excise goods:** Strengthening control over production and circulation (traceability systems, licensing activities, market monitoring), further combating smuggling (technical equipment for customs, international cooperation), strengthening liability for illegal production and distribution (criminalisation, confiscation of equipment), as well as a balanced excise policy and information and awareness-raising activities.
- **Fighting trade without fiscalization:** Strengthening control over the use of cash registers/online cash registers (RRO/PRRO), especially in online trade, where payments are often made to personal bank cards.

Combating key tax evasion schemes	Minimum, year <b>5.95</b> billion USD	Maximum, year <b>10</b> billion USD
Tax policy optimization	Minimum, year <b>2.4</b> billion USD	Maximum, year <b>4</b> billion USD
Increasing revenues from the management of state-owned assets	Minimum, year <b>0.14</b> billion USD	Maximum, year <b>0.6</b> billion USD
Optimizing public spending and stimulating the economy	Minimum, year <b>1.90</b> billion USD	Maximum, year <b>3.10</b> billion USD
<b>TOTAL EFFECT FROM IMPLEMENTING THESE MEASURES</b>	Minimum, year <b>10.4</b> billion USD	Maximum, year <b>17.69</b> billion USD




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