

FIGHTING A CULTURE OF CORRUPTION IN UKRAINE

THOMAS DE WAAL | APRIL 19, 2016

“Corruption” is an inadequate word to describe the condition of Ukraine. Since the country achieved independence in 1991, the problem is not that a well-functioning state has been corrupted by certain illegal practices; rather, those corrupt practices have constituted the rules by which the state has been run. Ukraine’s political system is best described as state capture.

Since the Euromaidan uprising in 2013–2014, the new Ukrainian authorities have made positive changes in several spheres such as police reform and public procurement. An alliance between the EU and Ukraine’s other international partners, on the one hand, and civil society organizations and some reformist members of the government, on the other, has helped facilitate this progress. However, there is still a poor understanding in wider society of what constitutes corruption on an everyday level. Moreover, the Ukrainian public is increasingly frustrated and cynical, perceiving that much of the old predatory political class has survived into the post-2014 era and that the fundamentals of the old system remain unchanged.

The revelation in the leaked Panama Papers that Ukrainian President Petro Poroshenko, on assuming office in 2014, had passed ownership of his major chocolate business,

Roshen, to an offshore company registered in the British Virgin Islands may not have exposed anything illegal. But the move was at the very least politically insensitive on the president’s part and will have confirmed the impression of many ordinary Ukrainians that their leaders have managed to stay part of a global wealthy elite while the country’s average standard of living has fallen.

Substantial progress on rooting out corrupt practices will not be made without targeted reform of the powerful institutions that still perpetuate corruption. Rather than trying to fix everything at once, Ukraine’s government and international partners should focus on reform of the justice system, especially the Public Prosecutor’s Office and the courts. Change there needs to begin at the top. Another important goal is to continue to clean up the rules governing Ukraine’s parliament, party financing, and electoral regulations.



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New anticorruption agencies can be effective but should not be viewed as a panacea, and the EU's conditionality should not depend on their performance. The EU should make its conditionality less reliant on technical benchmarks and more political, basing it on an overall assessment of real progress in the fight against corruption.

CORRUPTION IN UKRAINE: A SYSTEMIC PROBLEM

For years, Ukraine has had more in common with states in Africa or Latin America than with other parts of Europe. Business and politics have been fused, the rule of law has been weak, and almost all transactions, from visiting the doctor to managing a business to running a political campaign, have incurred informal taxes or rents. Formal political and bureaucratic offices are held on a basis of dependence on powerful masters, who exact rents and pay incomes to members of their networks—thereby robbing the state of revenue at every stage.

The result has been a weak public service culture, while ordinary Ukrainians have learned skills of self-reliance and see the state more as a predator than as a supplier of public goods. At the same time, the public has a poor understanding of where corruption begins and ends. Many Ukrainians accept that everyday bribery is a way to get things done.

This system was shaken but not broken by the 2013–2014 Euromaidan revolution and the fall of the Viktor Yanukovich regime. Much public anger that might have been directed at oligarchs was deflected toward Russia after its military intervention in Ukraine. The two Western-oriented politicians who became Ukraine's president and prime minister, Petro Poroshenko and Arseniy Yatsenyuk, had one foot in the old system and one in the Euromaidan movement.

A comprehensive poll by the Kyiv International Institute of Sociology at the end of 2015 showed the Ukrainian population was confused about corruption: many people believed it was getting worse, while ordinary citizens were also less inclined than in the past to give voluntary bribes. These paradoxical findings can be explained partly by a climate of greater transparency, which has enhanced public knowledge of corruption. "Ukraine is the most open country in Europe," said the prominent anticorruption activist Daria Kaleniuk in an interview, in reference to media coverage of corruption issues. Investigative journalists and civil society organizations such as Kaleniuk's Anticorruption Action Center have taken the lead in the public battle against corruption and have partnered effectively with a few reformist figures in government and with Ukraine's Western partners, an effect that has been called sandwiching.

At the same time, there is not much to celebrate in the fight against grand corruption—defined as the abuse by leading officials of their public positions for personal enrichment—and therefore no demonstration effect that will inspire confidence in wider society. Even senior members of the discredited Yanukovich regime have so far succeeded in avoiding prosecution.

The record of anticorruption efforts in Ukraine is a mixed one, and public expectations in this area are certainly too high. But both the EU and the Ukrainian government have a poor history of communicating what they have done and plan to do. A failure to communicate well with the public carries the risk of ceding the anticorruption agenda to populist politicians with their own priorities.

The public's perceptions and behavior will change slowly. A shift in attitudes will happen faster if assisted by educational initiatives and more media discussion of everyday corruption, especially in Ukraine's regions. Oleksiy Chornyy, who opened a new anticorruption agency in Odessa,

described in an interview how much needs to change among the wider public as well as at an elite level. “People don’t understand what corruption is,” Chornyy said. “At first people came [to our agency] with any old complaints, such as problems with their neighbors or unjust court judgments. After two months we understood it wasn’t working. We realized that the key issue is the abuse of public office.” Chornyy then tried to enlist members of the public into exposing bribe taking by officials. However, people were reluctant to do so, and “95 percent didn’t want to get involved personally.”

Chornyy’s new agency tried to bring two allegedly corrupt officials to justice, but both cases collapsed, despite strong evidence. In one instance, the anticorruption activist said, a regional transportation manager was purportedly allocating routes for public minibuses in exchange for bribes worth \$1,000. The manager drove a sports car despite receiving a salary of 4,500 hryvnia (\$170) a month. After being confronted with evidence of wrongdoing, the manager resigned from the provincial administration—but ended up being rehired to do a similar job by Odessa city hall.

The advice of this ground-level anticorruption fighter is something that Ukraine’s Western partners should keep in mind as they consider the bigger picture: a long-term change of culture is required to fight corruption, and in the shorter term the more responsible parts of the media can serve as a weapon that is just as important as the courts. Chornyy said, “We’ve decided to change strategy again and identify cases of corruption and advertise them through the media.”

POST-EUROMAIDAN SUCCESSES

Since 2014, Ukraine has scored several successes.

Ukrainian Deputy Interior Minister Eka Zguladze (who previously held the same post in Georgia) has led police reform and been credited with an influx of new recruits into the police force who refuse to take bribes. Police reform is popular with the public, although some concerns have been voiced about the accountability of the police force. Zguladze is one of several Georgians recruited into the Ukrainian government who worked with Mikheil Saakashvili when he was Georgian president. The hope is that they can replicate the first phase of Saakashvili’s reforms in 2004–2007, when much positive change was achieved, without repeating the mistakes of the later Saakashvili period, when power was abused and the public was disengaged from elite-level decisions.

Public procurement in Ukraine has also undergone a radical overhaul. Previously, it had been a means to reward political favorites. For example, in 2011, Oleksandr Yanukovych, a dentist and the son of the then president, was allowed to buy the Ukrainian Bank of Development, which then acquired the right to pay the salaries of officials in several government departments. These kinds of abuses should be much harder to perpetrate with the introduction of a new electronic procurement system named ProZorro, which will make Ukraine’s government tenders some of the most transparent in the world. ProZorro is supposed to be mandatory for all public tenders from August 1, 2016.

Another reform that it is hoped will deliver results in the longer term is the creation of the position of a business ombudsman who can report businessmen’s complaints about pressure to pay bribes and can tackle issues such as value-added-tax fraud.

Reform has also begun on some of Ukraine’s more than 3,000 state-owned enterprises, which have enriched and empowered corrupt state officials. The managers of the companies have traditionally been beholden to politicians

who used the businesses to generate semilegal or illegal revenue streams. For example, under a kind of reverse money-laundering process known as *obnal*, the companies deposited legally earned money into specially created funds or paid other businesses for fictitious services rendered—and the money was thereby made available for personal and political uses.

The process has begun of breaking up and giving new management to some of these monster companies, including the big state-owned oil and gas distributor Naftogaz, which was a notorious source of corruption. Responsibility for appointing the management of Naftogaz and of 60 other state-owned enterprises passed in 2015 from the energy ministry to the economic development ministry.

However, a balanced approach is needed. There is a danger of proceeding too quickly with privatizing state-owned enterprises if a proper legal framework is not in place. Ukraine risks repeating the kind of inequitable privatizations that took place in Russia and Ukraine in the 1990s, when state companies were sold off too cheaply to politically powerful businessmen.

THE LEGAL SYSTEM

Judicial reform is pivotal to anticorruption initiatives in Ukraine. Corrupt practices in the country have often been sanctioned by crooked court judgments and are therefore technically legal. This problem hangs over many ongoing legal disputes. For example, the Swiss aviation company Swissport, which formerly ran ground services at Kyiv's Boryspil International Airport, says that in 2013 it was the victim of a corporate raiding attack when it was forced to sell its 70 percent stake in the airport to its minority

shareholder, Ukraine International Airlines, for a fraction of the price it was worth. This was all done in a way that was nominally legal in the courts.

Reforming the whole judicial system will take years. It makes sense to start at the top and replace the 20-member High Council of Justice, the body that appoints judges. Although the council is ostensibly independent, its integrity has been questioned. In the same fashion, if new appointments are made to the Supreme Court of Ukraine and the highest-level appellate court, then final judgments can be made by judges at the top who have authority in society.

Traditionally, the main power in the legal system has lain with the Public Prosecutor's Office, heir to the Soviet-era *prokuratura*. Afforded a section of the constitution to itself, Ukraine's prosecutor's office could call on an army of officials. In 2013, it still had more than 18,000 prosecutors (compared with 10,000 judges), with the number set to fall to a more reasonable 10,000 by 2017.

At the top of the prosecutor's office hierarchy, Ukraine's two most recent prosecutors general, Vitaly Yarema and Viktor Shokin, both had the reputation of having been the president's men. As researchers William Pomeranz and Oksana Nesterenko note, "on close examination, the right to appoint the [prosecutor general] represents one of the few substantive perks assigned to the Ukrainian president outside the area of foreign affairs."

Both Yarema and Shokin are faulted for having failed to carry through important prosecutions of notorious figures from the Yanukovich regime. Whether the issue is primarily structural or personal, it is certainly true that respected senior prosecutors such as Davit Sakvarelidze (another Georgian appointee) and Vitaly Kasko have, in the words

of one international official dealing with Ukraine, been “sandboxed.” Kasko had pursued cases against two high-level colleagues, who became known as the “diamond prosecutors” after diamonds were seized from their offices, but the case was suspended. Kasko resigned on February 15, 2016, saying that he no longer wanted to work for a “dead institution.” On March 29, Shokin fired Sakvarelidze, shortly before being voted out of his job by the Ukrainian parliament.

A recently appointed special anticorruption prosecutor, Nazar Holodnitsky, although respected for his integrity, is judged by experts to have less professional experience in this field than either Kasko or Sakvarelidze and will face similar big challenges in getting major prosecutions moving.

The case of one of Yanukovich’s most notorious cronies illustrates the scale of the problem. Yuriy Ivanyushchenko, a parliamentarian close to Yanukovich whose wealth was estimated by *Forbes* to be \$122 million in 2014, fled Ukraine after the fall of Yanukovich and was the subject of an Interpol Red Notice for internationally wanted persons. In December 2014, Ivanyushchenko was formally accused of embezzling 72 million Swiss francs (\$75 million) earmarked for energy efficiency measures. Assets belonging to him were frozen in Switzerland. However, the prosecutor’s office stopped pursuing the case against him in December 2015.

Why would Ukraine’s new prosecutors not bother to prosecute one of the most despised figures from the previous regime? There are different explanations. Some experts cite sheer incompetence and say that the case may still be reopened. Others say that this proves that senior figures responsible for pursuing these cases are either being paid off or fear that, if he came to trial, Ivanyushchenko could incriminate current senior members of the elite. Whatever the truth, the case augurs badly for the pursuit of grand

corruption and strengthens the argument for institutional reform of the prosecutor’s office to ensure that personal loyalties can no longer be so influential.

NEW AGENCIES

Under Western pressure, the Ukrainian government has set about forming a series of anticorruption agencies and positions. They are the Specialized Anti-Corruption Prosecutor’s Office, headed by Holodnitsky; the National Anti-Corruption Bureau of Ukraine, an agency with investigative and certain law-enforcement powers but whose mandate does not cover past cases; the National Agency for Prevention of Corruption, tasked to expose corruption by senior officials by monitoring their asset declarations and other data; and a National Asset Recovery Office and Asset Management Office, still in the process of formation as of April 2016. An act creating a new agency for identifying, tracing, and managing assets derived from corruption and other crimes, with a mandate to pursue stolen assets both in Ukraine and abroad, was signed into law in December 2015 by the president, but the body has yet to start operating.

In other countries, the fight against corruption is handled by existing institutions. In Ukraine, the advantage of forming new bodies is that they can be staffed by freshly appointed professionals untainted by the old system. However, these new agencies have overlapping mandates and will need to coordinate very professionally with one another to get things done. More worryingly, civil society activists and some Western officials fear that creating special agencies makes anticorruption policy somebody else’s responsibility—that the policy focus revolves around the functioning of these agencies rather than the government’s overall duties in this field.

Certainly, a European Commission progress report on the reforms needed for Ukraine to obtain visa liberalization, published in December 2015, suggests that the EU has accepted this logic to a large extent. While justifiably observing that “progress made on legislative and institutional aspects can only bring significant end results if fully implemented,” the report concludes that “based on these commitments, the anti-corruption benchmark is deemed to have been achieved.”

The dynamic under which the new agencies were formed also raises serious questions, with foreign partners apparently showing a greater commitment to these institutions than the Ukrainian government does. While Western governments pressed for the new agencies to be created as quickly as possible, well funded, and staffed with well-paid professionals, Ukraine’s government and parliament showed no signs of haste, allocated insufficient funding for them, and did not select top professionals to fill positions in the new bodies. For example, the government wanted the annual budget of the National Anti-Corruption Bureau of Ukraine to be 100 million hryvnia (\$4 million), according to a source in the bureau, before the figure was increased to 800 million hryvnia (\$31 million) under international pressure. The bureau has been properly staffed and equipped with computers only thanks to the persistence of Western donors.

ASSET RECOVERY

No issue in Ukraine is more politically explosive than recovering stolen assets. In a country where per capita income is around \$3,000, the fact that members of the previous regime shipped billions of dollars abroad angers the public, while anticorruption campaigners express

frustration that almost nothing has been recovered since 2014. It was reported that as of July 1, 2015, a mere 7,865 hryvnia (\$356) had been returned from abroad to the Ukrainian budget. In November 2015, a more respectable sum—almost \$250 million—was reported to be frozen in foreign bank accounts but had not been recovered.

Asset recovery is a challenging business as stolen assets are concealed in elaborate ownership structures across multiple jurisdictions. Criminals exploit gaps in coordination between different countries with different legal systems.

In the apparently clear-cut case of former Ukrainian prime minister Pavlo Lazarenko, who was given a ninety-seven-month jail sentence in 2009 by a U.S. federal court on money-laundering charges, no stolen assets have so far been returned to Ukraine. That is despite the fact that several governments are trying to recover approximately \$250 million dollars frozen mainly in accounts in the offshore jurisdiction of Guernsey.

More recently, another notorious case of corruption, the huge private estate named Mezhyhirya that Yanukovich had built outside Kyiv, has also proved hard to investigate. After the downfall of the former president, ordinary Ukrainians were granted access to the grand mansion as well as its yacht club, zoo, and garage full of luxury cars. However, despite the publicity the site received, it has so far been impossible to make a case for the legal handover of Mezhyhirya, as its trail of ownership leads through multiple owners registered in Austria and the UK.

This is a challenge to the EU, as many of the shell companies used to hide stolen assets are based in EU countries. Moreover, several banks in Latvia are said to have been weak links and entry points for illegally earned money to get into the EU banking system. In 2015, Latvian and

Ukrainian investigators froze more than \$80 million that had entered Latvian banks from Ukraine. According to the Organized Crime and Corruption Reporting Project, a billionaire named Serhiy Kurchenko who was accused of illegal enrichment and large-scale tax evasion through gas sale schemes channeled millions of dollars into two Latvia-based banks.

TARGETING THE PARLIAMENT

In the 2015 survey by the Kyiv International Institute of Sociology, respondents called the Verkhovna Rada, Ukraine's parliament, the most corrupt political institution in the country, with 60.6 percent of those surveyed saying it was a center of corruption.

Despite the Euromaidan demonstrations and a new parliamentary election in 2014, most old parliamentarians have kept their seats and the Rada remains a millionaires' club in which powerful business tycoons enjoy immunity and use their offices to shape the political process. Several of Ukraine's so-called gray cardinals, who exercise huge informal power, are parliamentary deputies. They include Ihor Kononenko (accused by former economy minister Aivaras Abromavičius of trying to impede his work) and Mykola Martynenko, an ally of former prime minister Yatsenyuk who is being investigated by the Swiss state prosecutor for allegedly accepting a large bribe from the Czech company Škoda JS.

A central task of the new National Agency for Prevention of Corruption is to provide data on asset declarations that will reveal the true wealth of deputies—including many whose assets are considerably higher than their modest salaries. However, the Rada has tried to prevent the agency from achieving this goal.

Legislation setting up the agency dates back to 2014, but the body began operations only in January 2016. Then the Rada passed a controversial bill in February 2016 evidently with the intention of protecting parliamentarians from the agency's attention. The bill postpones until 2017 the date when public officials become criminally liable for submitting false information in their electronic declarations. The law also contains other loopholes, including one in the rules for submitting declarations that will enable corrupt officials to pass illegal assets to family members.

The parliament can be reformed only if the electoral legislation by which parliamentarians are elected is changed. As researcher Anders Åslund has noted, "Ukrainian election campaigns are among the most expensive in the world." A total of 675 million hryvnia (\$52 million) was spent on the 2014 parliamentary election. New legislation passed by the Rada in October 2015 is a big step forward as it makes party financing much more transparent. It puts a limit on private donations to political parties and makes parties that receive at least 2 percent of the popular vote eligible for state funding. The fact that the passage of the law was one condition of an EU package of visa liberalization for Ukrainians traveling to EU member states helped the bill succeed by a narrow margin, despite strong opposition.

However, another piece of legislation will make the parliament less transparent, not more. On February 25, 2016, Poroshenko signed into law a bill that allows parties elected to the Ukrainian parliament to select after the election, not before, which members from the party list will take seats in the Rada. In effect, this takes much of the power of electing deputies from the public and gives it to party leaders. Several civil society organizations as well as the International Foundation for Electoral Systems have condemned the new legislation. The foundation noted that the new law "can open the door to political corruption." The EU should speak up strongly to have this legislation amended or overturned.

CONCLUSION

Corruption in Ukraine is a system that was wounded by the Euromaidan protests but has survived and, to some extent, retrenched. Curing a culture of corruption across society is necessarily a long-term process and requires the inculcation of confidence in the rule of law in the wider public. That will happen as the judiciary and the public administration change and through education of the younger generation.

In the nearer term, more success is needed in tackling grand corruption committed by top officials, to create a demonstration effect. The judiciary, the prosecutor's office, and the parliament in particular are still centers of old corrupt practices. Top-down reform of these institutions

should be a priority. The EU is a key player in moving this process forward and should be robust in applying conditionality. If a culture of corruption is allowed to survive and even flourish, this could discredit the reformist project as a whole in Ukraine and its pro-European sponsors.

The formation of special anticorruption agencies has both pluses and minuses. Now that such an approach has been taken, it is important to ensure that these bodies become key institutions in the system, not just appendages to it. But an EU strategy should not rely too heavily on the new agencies. To help tackle a pervasive culture of corruption, the EU should resist the temptation to make its policies dependent on technical benchmarks and should resolutely keep in mind the big political picture.

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