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## **Approaches to reforming services privileges in Ukraine**

**Prepared for the project:  
Preparation of the strategy for  
social benefits monetization reform in Ukraine**



The Project is co-financed by the Polish aid programme 2008 of the Ministry of Foreign Affairs of the Republic of Poland.



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The publication expresses exclusively the views  
of the author and cannot be identified with  
the official stance of the Ministry of Foreign Affairs  
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## 1. INTRODUCTION

This report presents the main results of the research conducted within the project “Preparation of the strategy for social benefits monetization in Ukraine” realized by the Center for Social and Economic Research CASE Ukraine – with a support of its mother-organization Center for Social and Economic Research CASE located in Warsaw – and co-financed by the 2008 aid program of the Polish Ministry of Foreign Affairs. Irena Topińska and Janusz Szyrmer, senior experts from CASE, gave comments to the present report on the various stages of its preparation.

The issue of social benefits monetization has been discussed in Ukraine for quite a long time. Inherited from the Soviet times, non-monetary or in-kind benefits are still numerous. Examples include privileges for selected groups of population as well as universal price subsidies regarding housing, energy and transportation services. The way many of these benefits are granted reveal various deficiencies, therefore it calls for change. In fact some countries – as Russian Federation for instance – have already introduced such a change implementing (partial) monetization reform. Apparently, the non-monetary benefits absorb a very large share of public funds and at the same time their financing is not transparent. They often cause market distortions sending wrong price signals to major actors: producers, consumers and government agencies. Moreover, the way these benefits are distributed among final recipients is often regarded as unfair for they are usually inadequately targeted. They reach rather the affluent than the poor, while many vulnerable households or individuals are not supported. Monetization reform might help advance market mechanisms, improve controlling public expenditures and benefit targeting. These positive effects would be even more important for Ukraine in recent days, given the crisis that the economy faces.

Preparation of the strategy for social benefits monetization is a multi-aspect task. This study approaches it from the households’ perspective. More specifically, it focuses on the issue of benefit targeting and explores redistributive impacts of hypothetical reform scenarios. Changes of household and individual privileges or subsidies in receiving housing/utility, transportation and sanatorium services are simulated and their impact on inequality and poverty is investigated. This is done with the use of data from the household budget survey conducted by the Statistical Institute in 2006. Main scenarios assume cutting down current benefits received by the rich and targeting them to the poorest groups. Comparison of simple statistical indices - such as decile distributions, Gini coefficients and poverty rates before and after hypothetical scenarios - allows for the assessment of redistributive effects. These types of simulation analysis have often been undertaken with some impact on the actual reform design. As regard countries in the region, Russian and Polish experience may be given (Volchkova et al, 2006; Górecki et al, 1994) as example. In Ukraine, some steps in simulating redistributive impacts of social benefit reform proposals have also been undertaken (World Bank, 2007) but they need extension and updating

Reforms of benefits/privileges regarding housing (and utilities), transportation and sanatorium services are discussed separately because both rules of benefit granting and prospects of changes differ. Housing, including utilities, seems a specific case. First, public support to households for housing and energy services is the most diversified and it includes price subsidies, privileges and means-tested benefits. Housing support reaches the largest share of households and absorbs the largest share of public funds. Also, the need of changes regarding provision of housing and energy services is widely recognized. Contrary to the transportation and sanatorium cases, a hypothetical abolishment of price subsidization has been investigated in one of the scenarios. Increase of tariffs has been carefully calculated and benefits cushioning the decline of the real incomes of the poorest households have been proposed. In addition, international experience regarding housing and energy benefits has been studied and described in two background papers.

The research results presented in this report are organized in five sections, supplemented with Annexes. The analysis starts with the short overview of non-contributory benefits in Ukraine,

giving a description of their evolution and current rules. The second section presents the data used in this study and the methods of their analysis. The following three sections are the core of the report. The third one covers housing and energy, the fourth and the fifth consider transportation and sanatorium services, respectively. Each section provides a detailed description of the current system of service provision and of all relevant benefits and privileges which are granted to households and individuals. Next, it discusses hypothetical reform scenarios and their main distributional effects. Concluding Remarks summarize the report and give specific comments regarding reform implementation. Detailed statistics regarding scenarios are presented in respective Annexes. The last Annex provides institutional background. Selected publications, project background papers and legal acts that have been used at various stages of the research are listed at the end of the report.



## 2. EXECUTIVE SUMMARY

The system of social support has been inherited from the USSR and has been gradually evolving since those times. It consists of a variety of monetary and non-monetary benefits. The latter group includes numerous social privileges as well as consumer price subsidies. In Soviet Union privileges were a part of stimuli system which improved wellbeing of some layers of society under “all equal” ideology and protected those who had proved their loyalty. Independent Ukraine tried to use the soviet privileges as a stylized social safety net for supporting impoverished population.

However, very soon Ukrainian authorities realized that the old system is inefficient for targeting poverty and concentrated on elaboration of an additional social assistance mechanism. Till present the social assistance system remains a complicated mechanism which includes both rudiments of Soviet privilege-stimuli and recently established poverty alleviation programs. Current social programs could be divided into four major categories: (i) Social privileges, (ii) Housing and utilities benefits, so called housing subsidies, (iii) Family benefits, (iv) Support for low-income families. The first two categories are seen as the least efficient and requiring reforms. Therefore they have been selected for the analysis.

Although major attention of the research was allocated to the question of reforming social benefits/privileges, the attempt has also been made to expand the analysis covering also price subsidization reform. So far too little attention has been attributed to comprehensive analysis of these two parts of one system. The project has approached this issue in the context of housing and communal (mostly energy) services. The main target of our work was developing potential scenarios of reforming and simulation of potential outcomes of such initiative.

Housing and communal services are the largest item by the volume of privileges/benefits and price-subsidies. In contrast to other services, discounts on housing services are provided on both occupational/status basis (privileges) and on stylized income test basis (benefits). While housing privileges have a long history going back to Soviet times, housing benefits were introduced only in 1995 for supporting vulnerable population under growing energy prices. Almost 11 million people have been enjoying housing privileges (2006) and more than 2 million people (2007) participated in housing benefits program. The cost of housing privileges/benefits provision comprised about UAH2.2 billion from the Central Budget (2006).

Housing privileges work as a discount system for people with various status or occupation (War Participants, Individuals with Special Merits etc.). The privileged people are eligible for 25%-100% discount for housing and communal bill regardless of their level of income. At the same time housing benefits are provided on a stylized income basis. Household can claim compensation if housing bill exceeds 20% of household income (15% for vulnerable groups).

The price-subsidization mechanism of low utilities' prices is quite complicated. It includes cross-subsidies from different sources. Primarily, all losses from price subsidization are accumulated at the balance of the state energy company NJSC «Naftogaz of Ukraine». The negative financial results of Naftogaz are compensated at the expense of surcharges on industry and direct transfers from the central budget. The mechanism is non-transparent and creates many imbalances, like stimuli distortion at the economy.

In case of housing and utilities we have defined four scenarios of hypothetical reforms. “Zero option” scenario assumes elimination of housing subsidies and privileges for all recipients. This scenario is used as a base for further calculations. Scenario 2 considers housing benefits, and introduces an income test. It sets two thresholds: higher for identification of people who will be deprived of benefits and lower for selecting those who would receive additional cash support. Scenario 3 uses the same principle as scenario 2, but it concerns housing privileges. It is expected to have greater effect on wealth distribution due to bigger part in households' budgets that housing privileges take in comparison with housing benefits. Scenario 4, the most

elaborated, assumes reduction of price subsidies leading to the rise of prices paid by households for energy related services up to the market level, and implementation of compensating cash payments for the poorest households.

Benchmark scenario (abolishment of all housing benefits and privileges) has the most significant impact on richer households. Income test scenario (Scenario 2) resulted with insignificant redistribution of resources and has minor impact on the level of inequality (Gini coefficient). Naturally that higher level of budgets redistribution (Scenario 3) has a more visible impact on incomes of vulnerable layers and on Gini coefficient. Finally, the fourth scenario with the price increase appeared to be the most noticeable in terms of social protection of the poor and improvement of income distribution.

Transportation privileges are the second largest issue after housing services. According to the Ministry of Finance 2006 estimates, funds needed for transportation privileges constituted approx. UAH 8.5 billion. However, in 2006 the State Budget provided UAH 830 million for transportation privileges coverage as subventions to local budgets. Around 24.5 million people (53% of population) are eligible for transportation privileges based on either social or occupational status. Privileges are available for all types of domestic transportations, intra-city and intercity. Although income-test for privileges provision was designed, this tool still has not been enacted.

The mechanism of privileges provision is rather backward. There is no applicable profound mechanism for identifying eligible individuals for all kinds of social benefits and privileges, including transportation. As a consequence, currently, transportation privileges are provided simply based on identity cards of privilege recipients (for example, pensioner or student id), which should be presented directly to the service provider when traveling/buying tickets.

The price-subsidization (privileges funding) scheme is similar to the mechanisms of utilities price-subsidies; however, a bit more simple. Intercity transportation service providers are usually loss-making and authorities cover their balances from local budgets. In their turn, local budgets claim solid volume of privileged services (in transportation) to gain as much central budget subventions as possible for reimbursing public transportation support. For intracity transportation services direct reimbursement from central budget is envisaged.

For simulations we defined three scenarios, similar to those for housing services. The first one, absolutely theoretical, assumes abolishing transportation privileges for all recipients with no exception. The second is based on introduction of income test, which is used to identify 'eligible' people for the privilege abolishment and those deserving support. The third scenario was the most elaborated and realistic. This scenario envisages abolishing privileges and redistribution of the funds to "feasible groups", in our case, poor pensioners.

Among the three scenarios the strongest effect on decrease of inequality and reduction of poverty level has unconditional income-test application. At the same time exclusion of "feasible groups" from income test somewhat dampens the effect of the reform.

The third type of privileged services – sanatorium treatment – is less impressive in terms of budget funding and population affected. However, this area is even worse in terms of efficiency compared to housing and transportation. The system of sanatorium-and-spa treatment remained almost unchanged since Soviet Union. Although there exist some private resorts, today, sanatoria and health resorts are still, predominantly, state-owned. The system is financed through complicated contributory mechanism. The majority of sanatoria in state ownership are degrading. They lack funds for renovation works and new equipment purchase or have no stimuli for any improvements; therefore, the level of services in such places is very low, quality of medical services and equipment is poor. Moreover, the system of granting privileges based on decisions of local officials and, in some cases, doctors creates incentives for corruption and funds theft. Monetization of sanatorium treatment privileges would leave the right of sanatorium

choice to the individual, and create stimuli for sanatoria and health resorts to compete for their clients.

Sanatorium treatment privileges are provided to the majority of recipients once per year, for certain categories – once per two years. The amount of sanatorium vouchers for privileged individuals is determined by the Cabinet of Ministers annually based on the availability of state budget funds. In 2006, the total cost of sanatorium treatment privileges was estimated by the Ministry of Finance at 8.2 billion. However, the State Budget 2006 financed only UAH 1.5 billion.

For simulations with sanatorium treatment services we accepted the same three scenarios as for transportation services. The outcome appeared also very close to that of transportation results. The strongest effect on decrease of inequality and reduction of poverty level has unconditional income-test application.

All in all, the proposed reforms (scenarios) seem to have the strongest effect on service providers rather than targeting social problems. Basically, the main conclusion is that monetization and price leveling (through price subsidy removal) will be the most beneficial for the central budget. At the same time financial stance of vulnerable groups of population will be only slightly improved, if a given reform is successful. Moreover, local budgets and public service providers could be even worse-off at the first stage of the reform. Therefore, we can expect that such reform could be very difficult to implement – not so many beneficiaries of the initiative and a number of losers. And the only chance for the reform to happen if (i) the central government becomes the driving force of these changes, if (ii) the central authorities can guarantee for key players compensation of their potential losses.

Important, current economic problems could be a good platform for proponents of the reform to push through the price-leveling ideas. Through the next several years the number of vulnerable people will be increasing sharply thus creating huge pressure on state budget. On the other hand, price-subsidization mechanisms will also request more and more funding from the budget. At the same time public finance will be under hard budget constraints given global liquidity problems. Naturally that at some stage of the process the Finance Ministry will result with huge arrears at both sides – social privileges/benefits and price subsidies. Under such circumstance arguments for cutting off prosperous privileged groups and price liberalization could come just in good order.

### 3. SOCIAL BENEFITS IN UKRAINE

Ukrainian system of social benefits is well developed. There is a variety of contributory and non-contributory benefits, cash as well as in kind. This section reviews main social benefits which are intentionally designed for supporting the poor and vulnerable, and are financed through the public funds. They form the system of social assistance. First, their evolution in recent years is examined. Next, current rules of social assistance benefits are shortly presented. This would allow seeing all benefits in a comparative perspective and justifying the need for monetization reform.

#### 3.1. Social assistance development

Social assistance system has been inherited from USSR and has been gradually evolving since those times. Soviet ideology did not recognize that some poor people were present at the society. Instead a system of privileges was designed in a way to distinguish those who have made some remarkable contribution for the country or became vulnerable due to state service. Broadly speaking, the privileges were a part of Soviet stimuli system which improved wellbeing of some layers of society under “all equal” ideology and protected those who proved their loyalty. It was financed through enterprises and touched both poor and prosperous citizens. At the beginning of 90s the soviet privileges became a stylized social safety net which supported impoverished population. Naturally that independent Ukraine became responsible for the burden of social programs which requested more than 2/3 of budget proceedings<sup>1</sup>. Although the system was clearly inefficient and burdensome – vast possibilities for abuse – the government was not able to reform it since privileges were believed indeed to comprise significant part of poor people revenues. Moreover, large part of population has sentiments to privileges since Soviet authorities in this way acknowledged importance of people for the country. Obviously, any talks on reforming privileges system have been perceived suspiciously and even with irritation. Therefore, at the early independence any real steps in social reform could be a political suicide.

Although radical reforms were not possible, the authorities were forced to solve poverty problems at the depressed economy. For this purpose new programs were introduced which expanded social obligations drastically. In 1993 the government proposed benefits to the families with children<sup>2</sup> since such families were among the most vulnerable. The program was financed through enterprises till 1999 (later on through social welfare offices). It proved to be efficient in terms of poverty pockets targeting<sup>3</sup>.

Later on with increasing prices for energy resources the government had to pay attention to the housing services costs. In 1995 means-tested housing and utility benefits program was approved<sup>4</sup>. By 1999 about ¼ of population were among the housing benefits recipients. The benefits were compensated to the service providers thus for household they were in-kind. Local budgets were responsible for the program financing (as well as for the housing services tariffs). This program is not seen as successful since the benefits did not manage to target the poor while non-poor households were the main recipients under the program.

In addition to the two above the Cabinet of Ministers launched another program for social assistance of low income families<sup>5</sup>. The program was means-tested and targeted to support poor individuals. The program has strict eligibility criteria which made it very efficient in terms of

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1 Tausz Katalin (2002), The Impact of Decentralization on Social Policy, The Ukrainian Social Protection System and the Methods of Governance.

2 The Law on “State Assistance to Families with Children”, January 1993.

3 World Bank (2001), Ukraine: Social Safety Nets and Poverty Vol.1, Report #22677.

4 The Housing and Municipal Service Benefits Program was approved in February 1995 and launched in May 1995. The Decree of the Cabinet of Ministers #89, February 4, 1995

5 The Decree of the Cabinet of Ministers # 238 “On Implementation of Targeted Social Assistance to Low Income Families”

poverty eradication. However, the benefits under the program were financed from the local budgets and, according to the World Bank (2001), were significantly underfinanced. Usually, the regions with high level of poor populations were among those which were not able to finance the program.

On top of significant changes to the social benefits system, Ukrainian authorities produced hundreds of regulations, laws and decrees which were expected to improve the system. However, the magnitude of small updates only complicated the situation preserving the key mechanisms unchanged.

Through later periods the government has been trying to cut some excessive privileges and to improve the mechanisms of social benefits' programs. In particular a set of reforms was undertaken through 2000-2001. In 2000 subsidies for fuel and natural gas purchases under housing benefits program were cashed out so that payments were arranged directly to households.

In addition to that in 2001 fiscal decentralization reform also improved mechanisms of social protection system financing. Local budgets of second and third level got direct access to the central subventions on social protection i.e. became more efficient in protecting social needs of the communities.

Through the period social privileges were also under attention. However, the privileges reform was related mainly to cutting expenses while there were poor updates to the mechanisms of privileges provision.

Considerable steps were made towards improvement of means monitoring system. In 2001 the government established institute of social inspectors. Later on it was renamed on "public social inspector". The inspectors are responsible for monitoring and ensuring targeting of social assistance to eligible families or individuals. Although efficient, public social inspectors are of relatively low level of competence, which dampens their institutional role at the social assistance system.

### **3.2. Current social assistance system**

By the mid of 2008, the social assistance system was a complicated mechanism which included both rudiments of Soviet privilege-stimuli and recently established poverty alleviation programs. The World Bank divides social programs into four major categories<sup>6</sup>:

- (i) Social privileges;
- (ii) Housing and utilities benefits (housing subsidy);
- (iii) Family benefits;
- (iv) Support for low-income families;

The first category was inherited from Soviet times while the rest was created through the transition period. To large extent the categories overlap between each other by the types of provided services. However, the recently introduced benefits usually are means tested and target poverty problems while the Soviet privileges are traditionally granted based on special merits, occupational and social characteristics (unrelated to income).

*Social privileges system* is extensive, expensive and complicated. Enormous amount of laws decrees and resolutions defines a palette of different social privileges. The privileges are categorical and are provided both in cash and in-kind. There is no accurate number for

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6 World Bank (200), Ukraine: Social Safety Nets and Poverty Vol.1, Report #22677.

privileged population; according to approximate estimates<sup>7</sup> between one quarter and one half of population enjoys the privileged status. By types of services the privileges are usually categorized in the following way:

- housing and utility services;
- public transportation;
- communication services;
- drugs and medical services;
- sanatorium treatment;
- free cars for invalids;
- repair of dwellings;
- cheap credits;

The system is vulnerable for abuse. There is no unified mechanism for monitoring of eligibility for privileges provision. Traditionally, non-poor households benefit the most of the privileges.

*Housing and utilities benefits* overlap with social privileges; however, the benefits are provided only for those who managed to prove low income level. The benefits include in-kind compensation for utilities and cash payment for solid fuel and natural gas purchases. The latter traditionally is related to rural inhabitants. Housing benefits are provided in case the utilities' costs exceed 20% of family income (15% for vulnerable households). In addition to income level, a household should prove absence potential incomes. In particular, households which have new car or another apartment are not eligible for housing benefits. Even despite strict eligibility criteria more prosperous households benefit of the program. Traditionally better-off families own larger dwellings and subsequently receive higher benefits compared to poor citizens. Therefore, the program protects population from sharp energy-price increase but it is not that much efficient in terms of poverty targeting.

*Family benefits* intend to protect families with children. The program is means-tested (excluding payments for baby birth) and includes five sub-programs:

- (i) support on maternity (on pregnancy);
- (ii) payment on baby birth;
- (iii) support on baby care;
- (iv) support on fostering;
- (v) support to single mothers;

Remarkable is payment on baby birth. Through 2004-2008 it was a hot topic for populist speculations. By the mid of 2008 the law envisages remuneration for birth of first, second, third and all further babies with payment of about UAH 12,000, UAH 25,000 and UAH 50,000, respectively. This program does not define any income test. All other baby care programs are means tested and usually are linked to minimum subsistence level.

The program aimed to reduce child poverty and to stimulate birth rate. The poverty reduction seems to be efficiently targeted for a long period time<sup>8</sup> while the program has not become a real

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7 Nechai Anna (2006), Analysis of Social Privileges in Ukraine, prepared for the World Bank Mission to Ukraine, January 24, 2006

8 World Bank (2001), Ukraine: Social Safety Nets and Poverty Vol.1, Report #22677

driver for population growth. Although through recent years some increase in birth rates was observed it should be attributed to improvement of economic situation. At the same time the baby care programs are reported to be seriously underfinanced.

*Support to low income families* is a kind of program which considers only means for living and was clearly designed to target poor population. An eligible person (family) should prove that s/he does not have income or potential income higher than subsistence level. Broadly speaking, the support is calculated as a difference between subsistence level and the declared income. The program seems to be efficient; however, it has significant drawback –subsistence level used to be underestimated (much lower of real subsistence needs) and thus the program did not solve the poverty problem.

### 3.3. Conclusions

This short discussion of social assistance benefits supports the view that ‘old-style’ benefits, which take a form of privileges based on various merits, reveal the most serious deficiencies. Privileges involving free or discount-rate access to housing and utility services, public transportation and sanatoriums deserve special attention. Therefore, hypothetical reform scenarios for these benefits have been developed and investigated. Methodology of the research is discussed in the next section. The following sections present the main results of the research.

## 4. DATA SOURCE AND METHODS

### 4.1. Data description

For the analysis of importance of privileges and benefits for population of Ukraine and distributional impact assessment of their reforms, Household Budget Survey (HBS) of 2006 has been used.

HBS is a survey conducted regularly by The State Statistics Committee of Ukraine which observes a random sample of over 10,000 private households. The sample contains data on household living conditions, expenditures on goods and services for private consumption, as well as on incomes, housing conditions etc. Collection, processing, analysis and dissemination of data are provided quarterly and annually by national statistical services. The structure of household monetary incomes and consumer expenditures is presented regularly to the public.

HBS is considered to be reliable and representative. In 2005, the assessment of reliability of the HBS data was conducted. It has shown that relative standard errors for the total income and total expenditure were 1.25%, and 1.37% respectively, while any data with this parameter lower than 5% considered being reliable.

HBS of 2006 was the latest available during the project implementation. We consider it appropriate for our research as other statistics for the same year were available as well making data from various sources easily comparable.

#### *Data collection and contents*

All together household budget survey consists of three data components:

1. Data about households collected through the interview and diaries. Interview regards general characteristics of a given household such as listing of its members, housing conditions, ownership of land plots, etc.

Regular incomes and expenditures of a given household are registered for one quarter. This is done using a special diary filled by the household twice per quarter. In the diary household members register all their incomes and expenditures on a daily basis and give their detailed description. In the same diary they register products received as presents and food items grown at the land plots.

Households are distributed evenly among rotational groups that fill diaries in different weeks of a quarter. Under the assumption that two weeks in three months characterize the whole quarter, the data received is subsequently multiplied by the number of weeks in a quarter (6.5) to receive quarterly data. Accounting of food products for consumption during long period of time is conducted on the basis of quarterly interviews.

2. Data collected through quarterly questionnaire. The questionnaire is filled by households during the first month after the quarter under review. At this stage the data on significant and irregular expenditures and incomes are collected. To register the data households are given a special register of quarterly expenditures. One of the main purposes of this part of HBS is registration of the income structure and sources of income of a household. Some incomes are analyzed separately for every household member (salary, pension, stipend, etc), while others are analyzed for a household as a whole. The latter group includes for instance gifts from relatives, privileges and subsidies related to housing, communal services, transport, sanatorium and other transfers. Money value of these incomes are estimated by the households and registered in the questionnaire. The data on social transfers are considered to be reliable as households members are perfectly aware of the value of discounts they are getting.



3. One-time thematic survey. It is conducted with the help of a question list that may refer to households' expenditures on apartment's construction and restoration, ownership of durable goods, households' evaluation of health conditions, etc.

Thus, HBS incorporates observations of all kind of household expenditures except those related to entrepreneurship, farming or other kind of self-supporting activity.

Total expenditures aggregate both consumption and non-consumption expenditures. Consumption expenditures include cash expenditures on food and value of food received as present or grown by household at its personal lot, as well as the value of received privileges and in-kind benefits on housing, communal services, telephone communication, transport, sanatorium, healthcare, medicines, etc. Non-consumption expenditures include cash and in-kind expenditures on help to relatives and others, expenditures on real estate purchase, repairing works, accommodation construction, shares, bonds and currency acquisition, bank deposits, taxes and other payments to the state, etc.

Therefore total expenditures include actually paid cash expenditures, value of in-kind incomes as well as sum of privileges and in-kind benefits. Value of food received as a present from relatives or other people or received from personal subsidiary plot is included in total expenditures due to permanent nature of these comings in. Thus total expenditures characterize the structure of resources usage and reflect real current state of material wellbeing of a household.

#### *Brief Description of the Structure of Data Files*

The domains and areas covered by the survey are listed below. They refer to two different levels.

First level contains information on households. Household is defined as all persons who occupy a housing unit, provide themselves with all means necessary for living and share expenditures fully or partially. A household may be represented by a single family, one person living alone, two or more families living together, or any other group of related or unrelated persons who share living arrangements. Most HBS information is collected on a household basis rather than for selected individuals in the population, because many items of expenditure such as food, accommodation and household goods and appliances relate to the household as a unit. On the basis of various statistical and practical considerations and precision requirements for the most critical variables, the HBS sample size is fixed. Hence, household level file of HBS 2006 contains 10499 confidentialised household records.

HBS 2006 includes the following data:

*Basic data:* degree of urbanization, geographical location, household size, household demographic and employment structure, etc.

*Expenditures data:* very detailed information on all expenditures, on consumer and non-consumer goods and services, including money value of some in-kind items.

*Income data:* disaggregated income information by source of income, as well as comprehensive data on social benefits received by the household (including in-kind components, such as privileges).

*Property data:* information on durable goods owned by household.

Second level of HBS data covers individuals (household members). The HBS 2006 file for individuals contains 26253 records with the following information:

*Basic data:* age; sex; marital status; education characteristics, etc.

*Income data:* detailed information on incomes, by source of income

*Personal data:* personal characteristics of a person with detailed health information

### *HBS data on social assistance*

Data on social assistance collected by HBS are well developed and provide detailed description of all privileges and benefits of interest.

Data on privileges and benefits on housing and communal services is provided in 38 different values given the most detailed distribution of assistance on housing itself, natural gas supply, heating, water supply, electricity, etc. Then, the data is aggregated depending on the type of support (privileges/benefits) and the type of provision of this support (cash/in-kind) up to the following aggregated figures: benefit for solid and liquid fuel in cash (Ex1\_1), privilege for solid and liquid fuel in cash (Ex2\_1), privilege for solid and liquid fuel, in kind (Ex2\_2), housing benefits in kind (Ex3\_2), housing privileges in kind (Ex4\_2), electricity privilege in kind (Ex5\_2). These figures have been explored in our analysis.

Transport privileges include fifteen different kinds of values representing intra-city, suburban and inter-city transport provided by railway and bus companies as well as combination of these transports and different kinds of intra-city travel cards. All the values are subsequently aggregated in one, representing the total value of in-kind transport privileges (e10\_2).

Sanatorium and health resort privileges include: value of privileges for health resorts (Ex6), holiday centres (Ex7) and tourist excursions (Ex8).

Hence, HBS seems to be the best data source for the purpose of our study. It provides the most detailed and reliable description of privileges and benefits as a part of total expenditures registered by population itself. An additional advantage of the survey is that no data is added or imputed by the Statistics Committee, but everything is received directly from the households (respondents). These data allow estimating the impact of changes in social assistance system on households' well-being, poverty and inequality.

## **4.2. Methodology**

Methodology of the research conducted within this project consists of the two main parts. The first part involves a detailed description of the current rules and statistics of social benefits/privileges which have been selected for the analysis. It includes discussion of the eligibility rules, financing and administration, as well as overview of the main statistical data on total expenditures, number of beneficiaries and benefit targeting. This step of the investigation is based on the legislative acts, household budget survey data, as well as on some findings from the previous studies.

The second part of the research involves a simulation exercise. In fact, it is crucial for our research. It starts from setting hypothetical scenarios of monetization reforms. For each benefit considered, three or four scenarios are set. Main scenarios assume cutting down current benefits or privileges received by the rich, and targeting them to the poorest households as cash payments. Targeting rules and thresholds adopted depend on the benefit discussed. In each case, however, a benchmark scenario involving cutting off all benefits and privileges with no further redistribution (called 'zero option') is examined.

Housing services are treated in a special way. For housing, an additional scenario assuming a hypothetical abolishment of price subsidization has been designed. In this scenario, tariffs would increase up to the market level, and cash compensation of the welfare decline to the poorest households has been proposed.

All scenarios are run on the data from the household budget survey (HBS 2006). Changes of privileges are simulated and their impact on household material status, inequality and – for some

cases - poverty is investigated. For the assessment of redistributive effects of the hypothetical reforms a number of simple statistics before and after hypothetical scenario are calculated and compared. These statistics include: decile or quintile distributions, Gini coefficients and poverty rates.

All statistics – deciles, Ginis, etc - are based on the total monthly expenditure per equivalent unit. It is calculated for each household with the use of official equivalent scales of the Ukrainian State Statistics Committee (household head = 1, other household members = 0.7). Expenditures are taken as a proxy indicator of household's wellbeing for the following reasons: (a) information on expenditures from HBS are more reliable than on incomes, (b) official poverty measure in Ukraine relies on expenditure, with a threshold set at 75 % of median equivalent expenditure.

Examination of inequality relies on Gini coefficients and decile distribution. The Gini coefficient is derived from the Lorenz Curve. It equals 0 when expenditures are distributed equally. Gini equal to 1 indicates the highest level of inequality (the richest individual/household takes the whole amount of expenditures). In other words, the lower the inequality, the closer to zero is Gini coefficient.

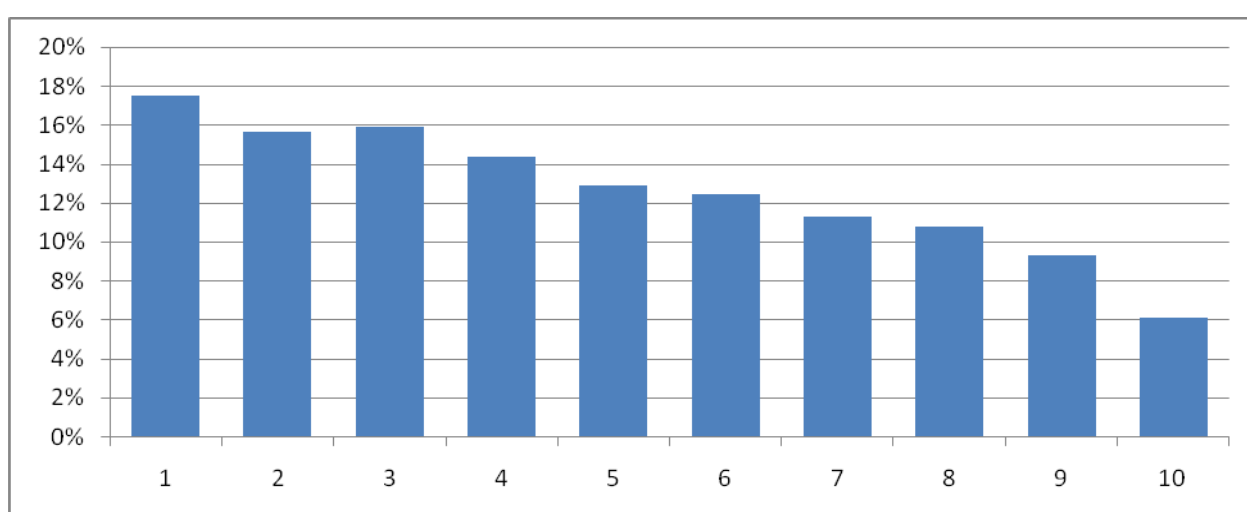
Simulation results are displayed in the text and Annex tables, as well as on the graphs. Most of them show the distribution of the total amount of benefits studied by decile or quintile of the total equivalent expenditure. This type of graphs is a convenient instrument for the analysis of benefit targeting.

## 5. HOUSING SERVICES

Housing plays a special role in the social and political dialogue in Ukraine and protection of lower tariffs has always been proclaimed crucial by different political forces.

Payments for housing and communal services represent a large part of households' expenditures, especially those in poorer deciles (see Figure 5.1) According to the HBS, 49% of the households (5,143 of the sample) were receiving different kinds of discounts/social assistance in 2006. This represents 25% of population or 11.3 mln people. Out of total of UAH 4,086 mln of social assistance payments reported by HBS, UAH 1,766 mln was received as housing privileges and UAH 197 mln as housing benefits, which makes them the most important of all the social payments.

**Figure 5.1 Share of housing services expenditures in total expenditures of households, by deciles.**



Source: HBS, 2006

Communal service companies (mostly energy enterprises) subsidized heavily by the government, straggle for both payments from final consumers and subventions from government authorities while at the same time they are not allowed to change tariffs.

### 5.1 Housing services description

According to the law of Ukraine “On housing and communal services” (1875-15) housing and communal services are defined as a result of economic activity, directed on providing conditions for living and staying of persons in inhabited and unoccupied apartments, houses and buildings, as well as in complexes of houses and buildings in accordance with norms, standards, orders and rules.

By functional destination, housing and communal services are divided into:

- 1) Communal services (central heating, water, gas and electricity supply, waste removal, etc)
- 2) Services directed on housing maintenance and upkeep (cleaning of communal in-house premises, plumbing works, in-house networks maintenance, etc)
- 3) Housing management (keeping a building on balance, formation of contracts for services provision, control over execution of contracts, etc)

- 4) Repairs of housing (replacement and reinforcement of structural component, reconstruction and renewal of buildings load-carrying ability)

By principle of tariffs setting, housing and communal services are divided into:

- 1) those set by central executive authorities,
- 2) set by local executive authorities,
- 3) set by contracts between parties.

Minimal norms of housing and communal services provision are established with the purpose of ensuring hygiene and sanitary conditions necessary for people and securing technical requirements for building exploitation.

Control over maintaining standards, norms and rules in sphere of communal services is carried out by the central authorities of executive power and other specially authorized authorities of executive power, and also authorities of local self-government in accordance with their plenary powers.

The mechanism of tariffs setting on maintenance services of houses and buildings was established by the order, ratified by the decision of Cabinet of Ministries of Ukraine on July 12, 2005 (# 560). The order established that tariffs (normative charges, related to maintenance of houses, buildings and near-house territories) are determined separately for every house depending on the quantitative indexes of actual service provision. While calculating the index several factors are taken into account: providing proper of the sanitary-hygienic, fire-prevention, technical state of houses and buildings in accordance with the typical list of services.

Housing services executor may be represented by any economic player that have provision of corresponding services as an object of activity and have capability to provide services. Housing services executor is determined by local authorities, besides cases when a building owner insist on determining an executor himself.

One of basic normative documents in relation to housing and communal services in Ukraine it is "Program of reformation and development of housing and communal services for 2002 – 2005 and up to 2010". In this program sets as main directions improvement of the sector functioning and upgrading quality of service. Priority is also given to the development of effective energy-saving policy.

On June 23, 2006, the Cabinet of Ministers of Ukraine adopted the order "About top priority measures in relation to reformation of housing and communal services". It declares that the current state of maintenance of housing fund, upkeep of sanitary and veterinary rules, rules of equipping with modern amenities, norms and standards of architecture, level of communal services in Ukraine needs revision. With the purpose of improvements on the market of communal services, creation of competition in the field of communal services provision, providing of the proper control after quality of such services the government approved the complex of measures for the year 2007 directed on the improvement of functioning of housing and communal services economy. Among them are the following:

- introduction of the institute of managers of houses with the aim creation of the market of services in a management of apartment houses;
- providing the selection on competitive principles of services providers in order to create competitive environment at the market of services in maintenance of houses and buildings;
- privatization of housing and communal enterprises;
- carrying out explanatory work among population on questions of reformation of relations related to the management and maintenance of housing fund;

- formation of community consultative centers of assistance to housing reform;
- creation of institutions of the communal investing at the local level into building of the centralized water supply and overflow-pipe systems;
- development of city plans of consumers provision with heat energy, optimization of charts of heat supply with the purpose of technical retooling and realization of energy-saving measures;
- making an inventory of communal property, overvalue of capital assets of communal enterprises with the purpose of introduction of the economically grounded tariffs.

Problems that currently exist in housing services sector of Ukraine are bound to the inheritance of morally outdated capital assets, depreciation of which reaches 60-70%, destruction of the single system of energy supply, delays in reforms and use of loss-making forms of management.

The crisis of housing services sector came at the beginning of 90th, and is now aggravated by new problems. As budgets are unable to provide current requirements in reconstruction and development, it results in growth of volume of outdated production funds on the enterprises of housing and communal service, more rapid dilapidation of engineering networks, decline of quality and continuity of communal service provision as well as increase in operating costs

In 2007 the cost of communal services provided around Ukraine reached UAH 18.75 bln (See table 5.1). While payments increased up to 94.1% of the amount charged, the ministry for housing and communal services claims that in 2007 tariffs covered 84% of services' costs.

**Table 5.1. Payments for housing and communal services, 2005-2007.**

	Amount charged, bln UAH	Amount paid, bln UAH	Level of payment, %
2005	9.62	10.69	111.2*
2006	13.27	12.02	90.6
2007	18.75	17.65	94.1

\*Including debts repayments for previous years  
Source: State Statistics Committee

On 28 of December 2007, president of Ukraine signed the strategy of pricing in housing and communal sector (#1324/2007). It includes, among other principles, a step-by-step replacement of housing benefits and privileges by cash payments to population.

## 5.2 Mechanism of housing benefits

Up to the year 1995 Ukraine had a system of direct state subventions to producers of housing services. The total sum of the subventions at that time reached 8% of the budget.

The housing benefits (subsidies) program, being a crucial part of the program of socioeconomic reforms in Ukraine, gave opportunity for the population to compensate more than 60 percent of the cost of payments for public utilities. Its role is even more significant in a time when prices and rates for these utilities were in constant growth. Nevertheless the whole procedure of the existing system of granting benefits is very complex and contested for its social inequality and injustice. According to this system, citizens with better social and residential conditions were in more favorable situation as they benefit the most from the government assistance.

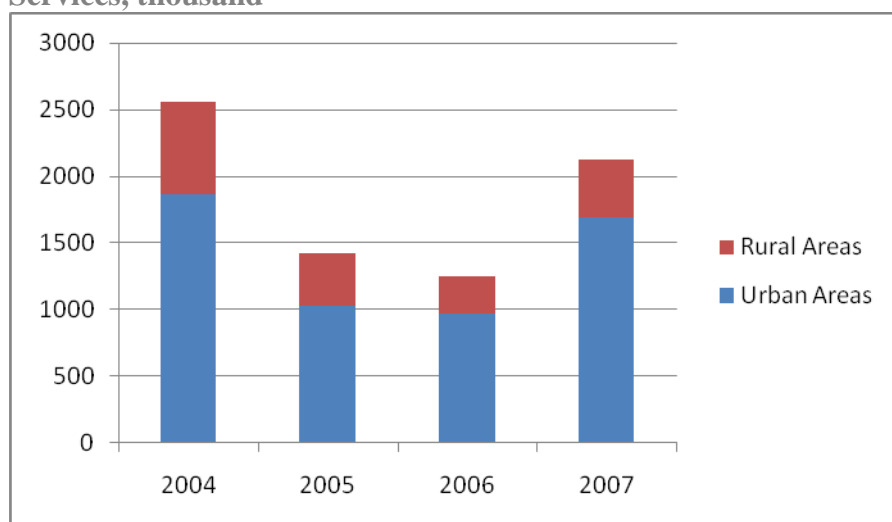
The housing and communal sector reform program was launched in 1994. The main feature of this program consisted in full indemnification of the cost for housing and communal services by those households who had a sufficient income level. With the increase in tariffs for housing and communal services the problem of inability to pay by low income households arose. To ensure

“safety net” for these households the Government launched the Housing Benefits Program in 1995. This social protection program guaranteed the cashless assistance for low income households.

The program was launched by CM Resolution # 89 “On Granting Benefits to the Population for Reimbursement of Housing and Communal Service Costs”, dated February 4, 1995. Households that came within this program started to pay not more than 15 percent of their average total monthly income for housing and communal services including water supply and disposal, heating, waste and sewage collection, housing maintenance. The granting aid applications started to be accepted throughout Ukraine in 756 housing benefits offices in May 1995.

The number of households receiving the housing benefit reached its peak in 1997 with more than 7mln households benefiting from the system. This number has been decreasing gradually down to 1.24mln in 2006, before going up to 2.12mln in 2007 due to tariffs increase at the end of 2006. (See Figure 5.2.)

**Figure 5.2. Number of Households Allocated Social Benefits for Housing and Communal Services, thousand**



Source: State Statistic Committee of Ukraine

The right to claim benefits in kind for housing and communal services payment and cash benefits for purchasing of liquefied natural gas, liquid or solid fuel have those living in state or communal flats (houses), including dormitory accommodation. Cash benefits for purchasing of liquefied natural gas, liquid or solid fuel is given to those living in premises which is not supplied by central heating, electricity and gas for heating. If several kinds of fuel are used for heating, then the benefit is granted for just one kind.

Benefits are granted when payment for housing and communal services, liquefied gas and solid fuel consumed within norms established by the Cabinet on Ministries exceeds approved percentage of obligatory payment. Currently, obligatory payment constitutes 20% of the total income of a family. For the most vulnerable groups it is lowered to 15%. Among vulnerable are: households composed of disabled citizens only (pensioners, invalids, children); households with invalids of 1-2 groups; households with children under age 18 years when the average monthly total income on one family member in household does not exceed 50% of minimum level of subsistence. While calculating the sum, privileges for communal services are taken into account.

**Table 5.2. Norms of consumption within which benefits for communal services can be received.**

<b>For benefits for electricity</b>	
In flats (houses) besides those equipped with fixed electric cooker or electric heating	For a family of one or two persons - 75 Kwt per month; For every additional family member – 15 Kwt per month, but not more than 150 Kwt per month per family
In flats (houses) which equipped with fixed electric cooker	For a family of one or two persons - 100 Kwt per month; For every additional family member – 25 Kwt per month, but not more than 200 Kwt per month per family
In flats (houses) which equipped with fixed electric heating	28 Kwt per per square meter of area during heating season, within norms (21 square meter per person and additional 10.5 meter per family)
<b>For benefits for natural gas</b>	
If gas is utilized for heating of habitation with a general area within the limits of norm (21 square meter per person and additional 10.5 meter per family)	11 cubic meteres per square meter of area during heating season.
If central heating is used and gas is used for cooking only	9.8 cubic meteres per person per month
If natural gas is used for cooking and heating, but not for hot water supply.	18.3 cubic meteres per person per month
If natural gas is used for cooking, heating and for hot water supply	23.6 cubic meteres per person per month

Source: Cabinet of Ministers Resolution # 89 “On Grating Benefits to the Population for Reimbursement of Housing and Communal Service Costs”

**Total income considered includes:**

*Work cash payments* (salary including overtime pay, second job pay and holiday premium; bonuses and allowances of all kinds independently of periodicity and sources of their payment; long-service increments and yearly premiums; other cash payments that are systematic including those for travelling type of work, but excluding subsistence money when at business trips; all of types of rewards, which are paid regular to literary workers, artists, press-photographers and other persons and also rewards which are paid for public execution of works; actual earnings of persons which worked for physical persons (natural part of the earnings also counts in their gross income); )



*Non-cash payments* (in kind salary)

*Compensation* (cash payments to servicemen, except for the servicemen of statutory service; sums, which are paid in order of compensation for the harm to the health of worker, which is related to fulfilling by him labour duties; sums of indexation of money profits of population and compensations for losses of part of earnings related to violation of terms of their payment; payments received in accordance with the law “About status and social defense of citizens which suffered because of the Chernobyl catastrophe”)

*Entrepreneur profit* (income received from entrepreneurial activity and other independent professional activity, including profits of advocates, private notaries, profits from artistic, musical, artistic and by other creative activity; profits from the personal peasant activity, lot lands, given for the conduct of the farming, gardening, , pasture of cattle, and landed share)

*Social payments* (scholarship, pensions, research grants, excluding those received as credits; unemployment benefits; earnings of students and students which combine studies with permanent work)

*Other kind of profit* (profits from renting property; alimonies receivable)

To be granted a housing benefit claimants have to submit an application itself, certificate about people living in a flat (house), their income certificates for the last six month as well as property certificates for everybody. A necessary condition for a benefit to be granted is an absence of arrears for communal services, which has to be proved by special certificate received from service providers. Claimants will also need their ID, social security number, work record card for unemployed and pensioner certificate for pensioners

In kind benefit for housing and communal services payments is granted for six months, while the benefit for liquid and solid fuel is granted from the month of a claim till the end of the heating season. If in a flat (house) only non-working pensioners and other disabled persons are registered, the source of existence of which are only pensions, profits from the personal peasant activity and other social payments, the benefit is granted for twelve months.

Upon termination of the term for which the benefit was granted claimants must confirm their right to receive the benefits for a next period. For this purpose they need to submit only certificates about the incomes of the registered people and statement in which absence of changes in composition is confirmed. In case tariffs rise for natural gas, solid and liquid fuel the benefit is changed within the two months since the increase in prices.

Benefits allocation and control over its usage for purpose is done by benefits departments of district state administrations as well as by executive powers of cities and regions.

### 5.3. Mechanism of housing privileges

Privileges for housing and communal services are provided according to a batch of laws devoted to social protection of every specific kind of privileged people. The list of privileged people with their number in 2005 is given in a table below.

**Table 5.3. Privileges for Housing and Communal Services, Solid and Liquid Fuel**

Category of privileged people	Number of privileged people (Register)	% discount
Individual with special merits	2 875	100%

War invalids	282 951	100%
Combat veteran	376 274	75%
War Participant	2 834 611	50%
Children of War (communal services only)	6 129 300	25%
Chornobyl (total) (only housing and utility services)	383 566	50%
Military veterans	181 084	50%
Pardoned people	16 982	50%
Other categories of privileged people*	66 950	50%
People with privileges in a rural area	3 339	100%
Retired teacher who worked and resides in a rural area	104 602	100%
Teacher residing in rural area	242 627	100%
Medical specialist residing in rural area	65 780	100%
Specialist of culture residing in rural area	27 547	100%

Source: A. Nechai "Analysis of special privileges in Ukraine"

Those eligible for privileges by several laws have the right to choose the law in accordance with which they will receive a discount.

Housing and communal services privileges cover also those members of families who live together and registered at the same premises as a person entitled to a benefit. Members of a family include:

- A spouse and under-age children
- A person that lives together and takes care of an invalid of war of group 1 under condition that the invalid is not married.
- Disabled parents
- Unmarried adult children, that recognized to be handicapped from birth of group 1 or group 2 or invalids of group 1.
- Persons that are looked after by a person entitled to a benefit under condition that they reside together.

The state compensates losses of communal enterprises originating from privileges provision. At the same time privileges exist that are financed from local budgets. They are different from region to region and are granted in accordance with decisions of city council.

#### 5.4 Cost of the benefits and privileges

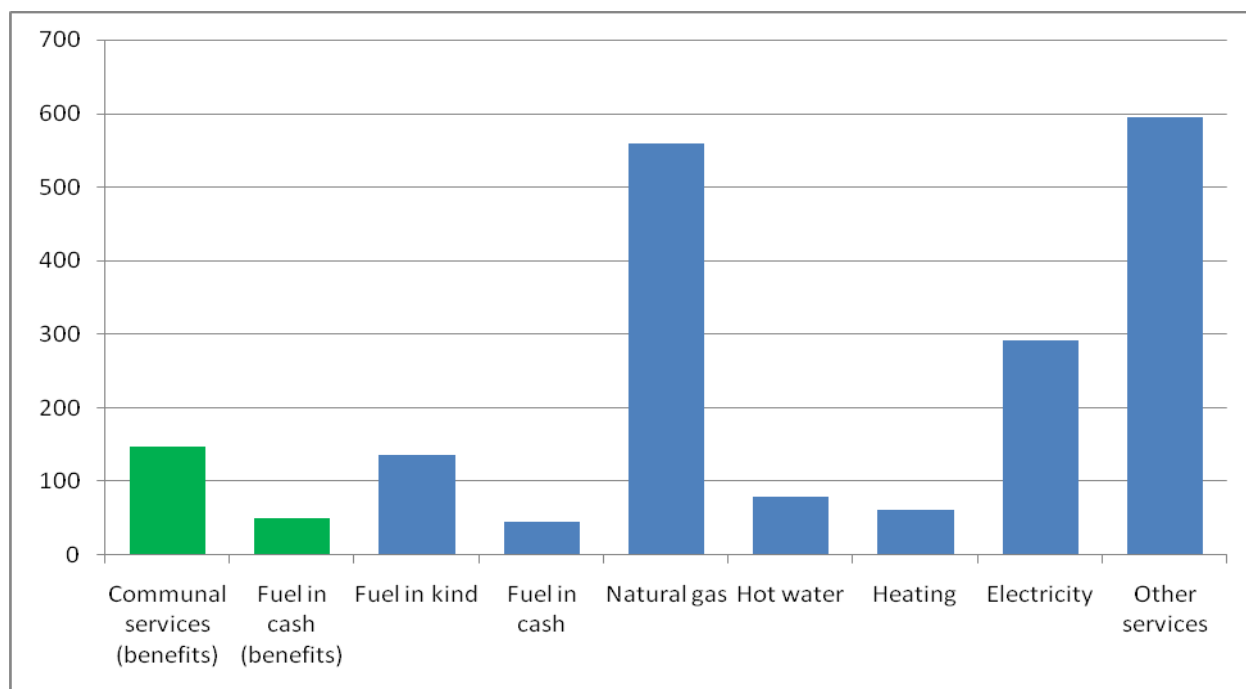
During the year 2007, 2.3 mln households claimed benefits for housing and communal services, out of them 2.12 mln households were granted the benefit, 79.6% of actual beneficiaries were residing in rural area. Total sum of housing and communal benefits in 2007 reached UAH 188.9mln, which is 2.2 times more than in 2006. Out of them UAH 161.8mln was granted to urban citizens and UAH 27.1 mln to the rural.

Benefits for solid and liquid fuel in 2007 were received by 456.6 thousand households (90.5% of those who claimed them). The total sum of these cash payments constituted UAH 218.6 mln, which was divided between rural and urban population as UAH169.6 mln and UAH49.0 mln correspondingly. Thus the average sum of the benefit reached UAH469.3 per household per year in rural area and UAH514 in urban.

In case of privileges, it is not possible to determine actual per capita costs of privileges for housing and utility services from information in statistical bulletins. A. Nechai in her report “Analysis of special privileges in Ukraine” estimated the costs of these privileges to be UAH 3,538 mln in 2006. At the same year, the budget of UAH 2,200 mln was set for both housing privileges and housing benefits.

On the other hand, HBS allows to see the money value of privileges reported by population, as well as their distribution among different categories, and to compare them with housing benefits (see Figure 5.3.)

Figure 5.3. Distribution of housing benefits and privileges in 2006, mln UAH



Source: HBS, 2006

#### 5.5 Mechanism of price-subsidization of the services

Ukrainian population receives natural gas for lower price than industry. The government using administrative power forces companies extracting Ukrainian natural gas with more than 50% of state share to provide gas for population. Those companies are SC Ukrgasproduction, OJSC Ukrnafta and SJSC Chornomornaftogaz.

For the year 2008, National Electricity Regulation Commission (NERC) established profitability of the above mentioned companies at the level of 10%. As the result the largest producer Ukrgasproduction has to sell its gas to the state for UAH182 per thousand cubic meters (without VAT), the price for Ukrnafta is UAH 272.6 and for Chornomornaftogaz – UAH289. Taking into account the forecasted volume of gas extraction by those companies, the average price of Ukrainian gas for population can be calculated. This price would amount to UAH 202.7 per one thousand cubic meters (see table 5.4.).

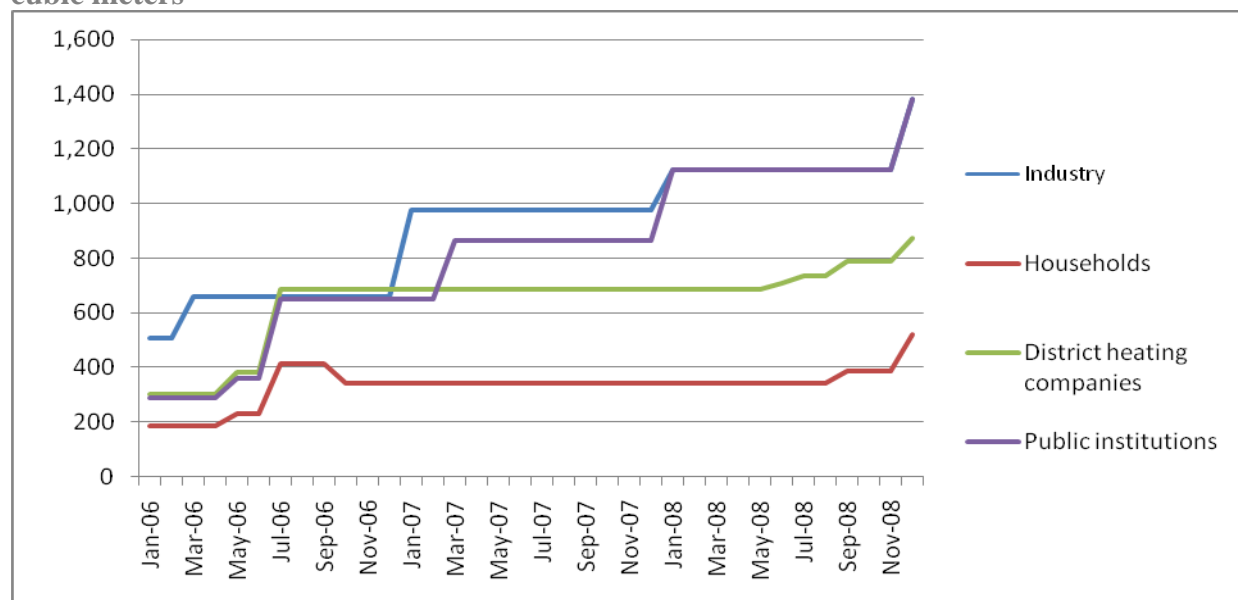
**Table 5.4. Gas extraction by state owned enterprises**

	Price UAH per thousand cm	Production in 2008, bcm (Forecast)	Total value
SC Ukrgasproduction	182	14.25	2593.5
OJSC Ukrnafta	272.6	2.72	741.5
SJSC Chornomornaftogaz	289	1.21	349.7
Average /Total	202.7	18.18	3684.7

Source: Companies' data, CASE Ukraine compilation.

In 2006, the annual average price of natural gas paid by population was 2.19 times lower than the price paid by the industry (UAH 288 vs UAH 632). This difference was growing over the next months (see Figure 5.4.)

**Figure 5.4. Gas Prices for Different Consumer Groups\*, Jan 2006-Jun 2008, UAH per 1000 cubic meters**



Source: SC Gas of Ukraine.

\* - gas price for households, district heating companies and public institutions includes VAT, transportation and supply fee; gas price for industry includes only VAT.

In addition to the discounted natural gas, households are also supported through cheaper gas supplies to heating companies. (See Figure 5.4.) On average (depending on weather conditions) housing and communal services sector consumes 40% of natural gas burned in Ukraine, out of this amount 11 to 14 bcm of gas is assigned for the heating sector. This high level of gas

consumption is explained by the fact that natural gas constitutes 76% to 80% of the fuel used by the heating sector.

In January 2007, import prices for Russian gas increased by 35%. This was followed by a further 38% rise in January 2008. In order to prevent these price rises causing a financial crisis, tariffs for population and heat generating companies were kept artificially low. This created a significant challenge for the latter and has resulted in debt accumulation among heating companies. Operators complain that these low tariffs have created conditions in which gas distributors are increasingly failing to service and maintain their networks properly.

### Grey Box 1. Tariff increase calculation for price-subsidies elimination

In 2006, annual average of natural gas tariffs per 1000 cubic meters were as follows:

- Population – UAH 288,
- Heat generating companies – UAH 508,
- Industry – UAH 632.

The price for households and heating companies includes VAT, transportation and supply fee; gas price for industry includes only VAT. The price for industries without the increment assumed to be a market price for natural gas. Thus to eliminate price subsidies the tariffs for population should be increased by 119% and for heat generating by 24%. The tariffs increase for heating enterprises is assumed to be fully transmitted to population through hot water and heating services price increase.

Electricity tariffs for population in 2006 were as follows (UAH per 100 Kwt)

	January-April	May-December
Large cities	15.6	19.5
Small towns	15.1	18.9
Rural area	14.4	18

Source: NERC, CASE Ukraine compilation

Thus making the weighted average UAH 17.4 per 100Kwt. At the same time an average tariff for bulk consumers of second class (set by Oblenergos) reached UAH 29 per 100 Kwt. Thus the necessary price increase was estimated to be 67%.

### Grey Box 2. Calculation of the amount compensating price subsidies elimination

The amount that would be needed to compensate for an average household the expenditure increase resulting from price subsidies elimination is calculated by multiplying the initial unit price by the price increase and consumption norms of goods and services considered, and summarizing the results afterwards.

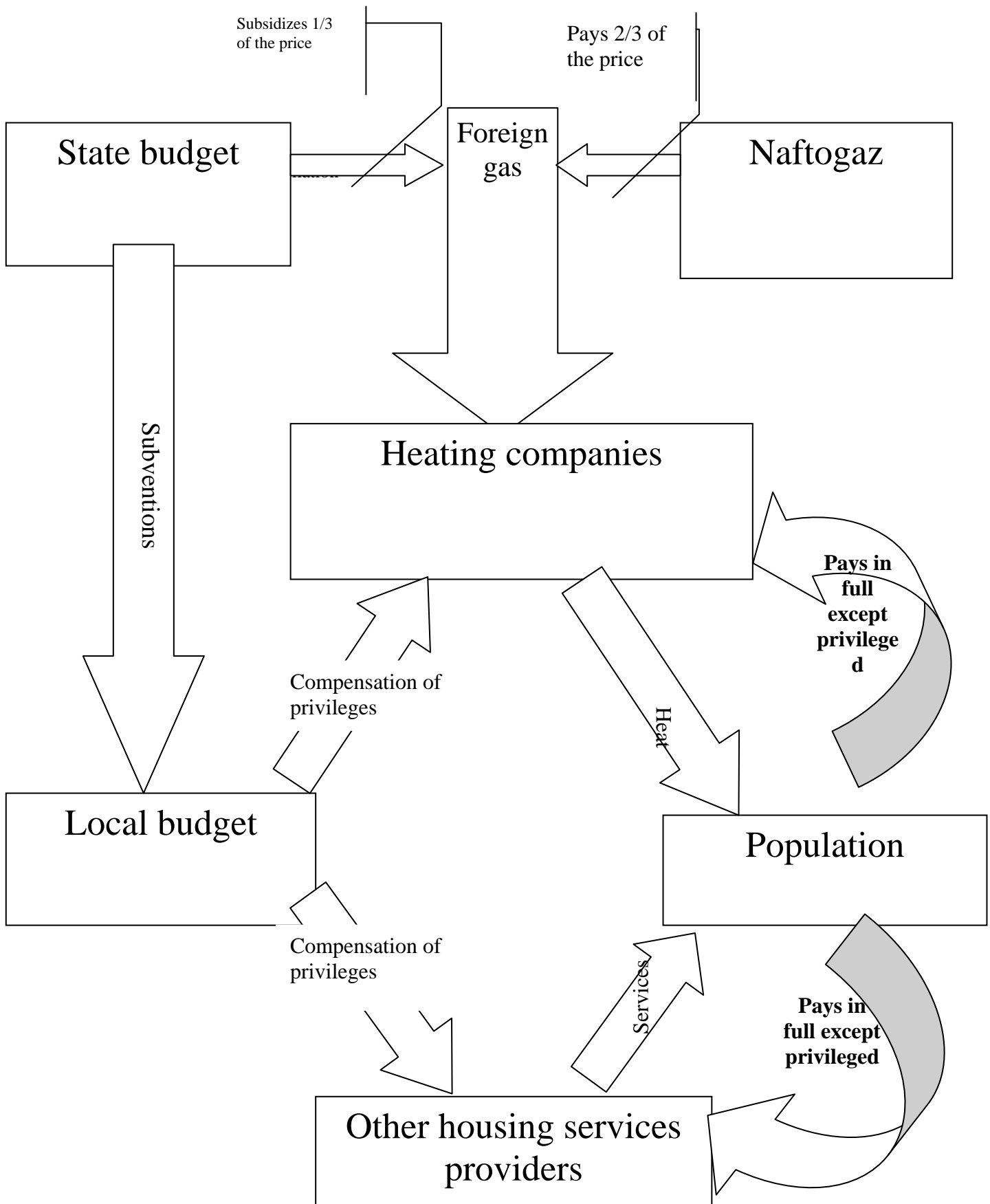
As a base for calculation, a conventional household with standardized characteristics was taken. This household is supposed to be equipped with central heating and central hot water supply, and using natural gas alone for cooking. These characteristics were used as a base for calculations according to the consumption norms used for granting housing benefits. Hot water consumption norm was taken as a 40% of the total water consumption norm which stands at 4500 liters per person, per month.

Calculation of adequate compensation for the tariffs increase

		Consumption norms	Price increase	Initial price, UAH per unit	Compensation for the price increase, UAH
<b>Household head</b>	Natural gas	9.8 cubic m.	<b>119%</b>	0.29	3.38
	Electricity	75 KWt	<b>67%</b>	0.17	8.72
	Heating	31.5 Sq. m.	<b>24%</b>	0.78	5.90
	Hot water	1.8 cubic m.	<b>24%</b>	3.48	1.50
					<b>19.50</b>
<b>Other household members</b>	Natural gas	9.8 cubic m.	<b>119%</b>	0.29	3.38
	Electricity	25 KWt	<b>67%</b>	0.17	2.91
	Heating	21 Sq. m.	<b>24%</b>	0.78	3.93
	Hot water	1.8 cubic m.	<b>24%</b>	3.48	1.50
					<b>11.72</b>

Source: CASE Ukraine estimates

Figure 5.5. Scheme of price-subsidization of heating services for population



Source: CASE Ukraine compilation

## 5.6 Simulation scenarios description

In order to investigate redistributive impacts of the monetization of housing benefits, privileges and price subsidies, four scenarios have been developed. All of them have been simulated using the household budget survey of 2006.

### 1. SCENARIO: 'ZERO OPTION'.

“Zero option” scenario assumes elimination of housing benefits and privileges for all recipients. This scenario is used as a base or a benchmark for further analysis. Also, it may show the importance of various types of housing support for different groups of population.

The scenario envisages that privileges, unlike benefits, are mostly received by households of the upper deciles (See Table 5.5.)

**Table 5.5. Share of households receiving housing benefits and privileges, by deciles**

	1	2	3	4	5	6	7	8	9	10
Benefits	10.10%	10.60%	12.30%	10.50%	11.00%	14.30%	8.90%	7.70%	8.40%	6.20%
Privileges	3.30%	7.10%	8.80%	9.70%	9.40%	10.70%	11.60%	13.00%	12.10%	14.20%

Source: HBS, 2006

### 2. INCOME TEST SCENARIO FOR BENEFITS MONETIZATION.

Scenario 2 implements an income test for identifying households who would continue to receive housing benefits after their monetization and those who will no longer receive this kind of support. The implementation of an income test is intended to improve targeting of benefits to the poor, i.e. to those who need social support most of all. Although means testing officially exists for households claiming state support, HBS data show that even in the wealthiest deciles there are recipients of housing benefits. Thus a direct income test is needed. In fact, two different thresholds have been assumed (i) a threshold equal to UAH 930, that is twice a subsistence level of 2006, for screening out households that would be deprived of benefits, and (ii) a threshold of UAH 430, equal to the official poverty line in 2006, for indicating those who would receive additional cash payments. These cash payments would be taken out of ‘savings’ that result from the elimination of benefits for the richest households, staying above the higher of the two thresholds. In other words, we assume redistribution of funds from the rich to the poor. The unit (per household) amount of the cash payment would be calculated accordingly. It should be noticed that wellbeing of households between the two thresholds would remain unchanged but they would receive housing benefits paid in cash. Annex B provides more detailed description of this scenario.

### 3. INCOME TEST SCENARIO FOR PRIVILEGES MONETIZATION.

Unlike benefits, privileges have an adverse effect on income distribution for various society strata. As HBS data suggests, the biggest advantage of privileges receive for the most part those, who have better living conditions, supplied with wider range of communal services and spend more on these services. Therefore, a change of the rules for granting privileges is needed. In our simulation exercise, it is implemented through the hypothetical scenario 3. This scenario assumes the same income test as scenario 2, considering the use of two thresholds and the



redistribution of funds from the rich to the poor. As well as in previous scenario, households with monthly equivalent expenditures less than poverty line (UAH 430) per equivalent unit per month will receive additional payments, those with expenditures greater than a double subsistence level in 2006 (UAH 930) will be deprived of all privileges. This time, however, greater effect on the wellbeing inequality is expected due to bigger share of housing privileges than benefits in households' budgets.

#### 4. PRICE SUBSIDIES ELIMINATION SCENARIO.

Ukraine has heretofore enjoyed preferential pricing on natural gas that allowed it to subsidize energy related services; however, changing conditions of energy supply coupled with budgetary constraints put the reform of energy-related communal services high on the political agenda. Therefore we have designed scenario 4 based on the suggestion to increase prices paid by households for energy related services up to the market level (see Grey box 1). This implies that unless they are accompanied by increases in income, future tariff increases could create large potential consumer welfare losses—as well as large revenue gains for the utility companies. As this step will significantly disadvantage those below the poverty line, households with monthly expenditures below UAH 430 per unit will receive fixed sum of money calculated according to the consumption norms (See Grey box 2). The scenario does not cover all housing subsidies, but rather focuses on those related to energy prices, as the most remote from market principle. We presume consumption remains highly inelastic, especially for the very poor. As this scenario leaves untouched privileges that are currently received by other population, their expenditures are increased proportionally to the housing privileges received previously.

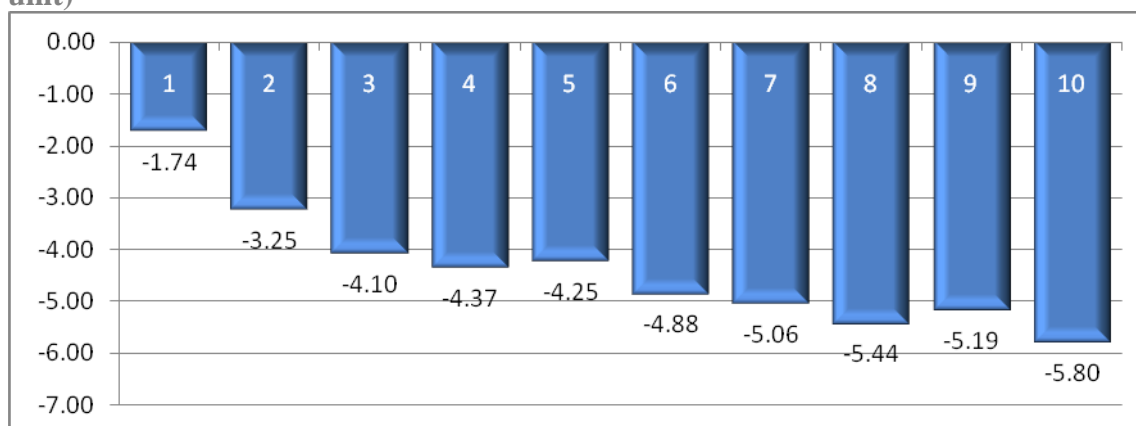
### 5.7 Results of simulations

Results of the scenarios – described in the previous section -- are discussed below. Appendix B displays them in details.

#### 1. SCENARIO: 'ZERO OPTION'.

Benchmark scenario (abolishment of all housing benefits and privileges) has the most significant impact on richer households. The results show very small absolute losses in lower deciles while the top decile loses the largest share. See Figure 5.6.

**Figure 5.6. Average decrease of the household wellbeing (measured with the total equivalent expenditures) after housing support elimination, by deciles (UAH per equivalent unit)**



Source: HBS, 2006.

## 2. INCOME TEST SCENARIO FOR BENEFITS MONETIZATION.

According to this simulation scenario UAH 25.7mln would be redistributed among 12.737 mln people, which resulted in insignificant payoffs of UAH 2.52 per unit per year (UAH0.21 per month). Unimportance of these payments is demonstrated by a very small reduction in Gini coefficient (by 0.01pp). Although attractive by the principle, this scenario appeared to have a very small effect on the welfare distribution and can be considered only in combination with other measures.

## 3. INCOME TEST SCENARIO FOR PRIVILEGES MONETIZATION.

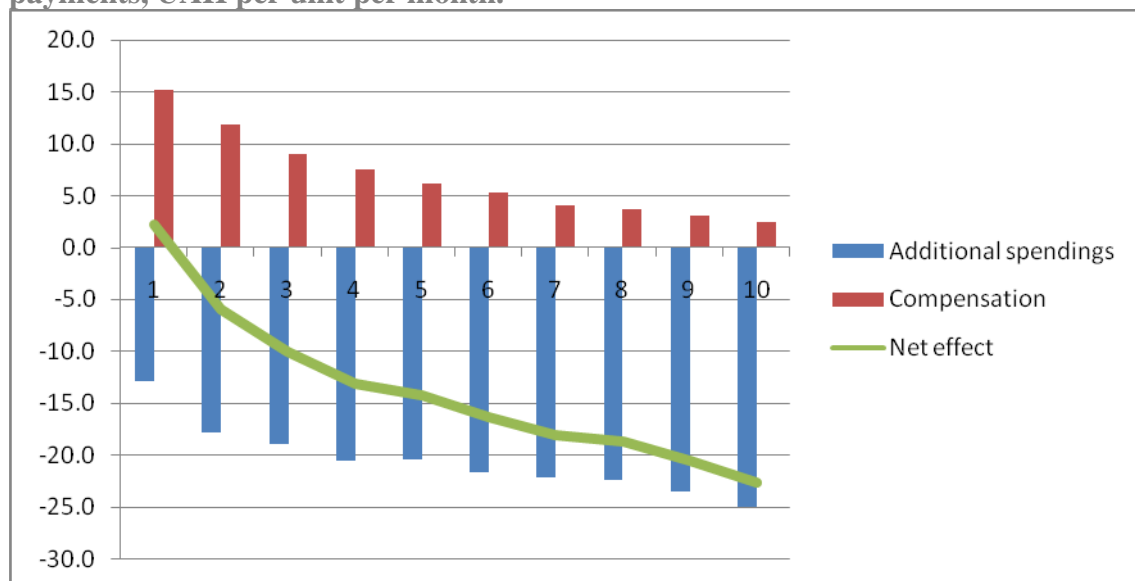
By the result of this scenario 7.8 mln people were deprived of UAH 396mln. of privileges that were distributed among 12.7 mln people. This would give cash payment of UAH 3.24 per unit per month – the fact that decreased Gini coefficient by 0.2pp. The scenario has bigger effect on inequality than the previous one, especially on the welfare of the first decile, where total expenditures grew by 1.4% in the result of simulations.

## 4. PRICE SUBSIDIES ELIMINATION SCENARIO.

This scenario would result in additional spending on energy bared by households at the level of UAH 762,896,881. Out of this amount, UAH 246,348,558 would be paid back to households in order to protect the most vulnerable. In the result, the first decile appeared to be better off after the simulation, while the upper deciles are the most negatively affected. See Figure 5.7. The results demonstrate very clear trend of smaller compensations for top deciles. They bare the far bigger burden of the price increase, while those in the middle are not so affected. This fact illustrates expected protection of the poorest in the situation of increased tariffs.

This scenario also allows reducing inequality among population as Gini coefficient reduces by 0.13pp down to 29.6. That is a smaller change than expected, as high discrepancy in communal services spending distorts the effect of compensation payments.

**Figure 5.7. Net effect of price subsidies elimination and subsequent compensation payments, UAH per unit per month.**



Source: HBS, 2006, CASE Ukraine calculations

Our main findings derived from the four simulation scenarios may be summarized as follows. Top deciles of the population are the largest beneficiaries of housing benefits and privileges. This is proved by the fact that in the result of social assistance abolishment they are the most affected in absolute terms. Contrary to our expectations, redistribution of housing benefits does not have any tangible effect on well-being due to insignificant resources being distributed. On the other hand, redistribution of privileges has the largest effect on equality in the society. The price increase scenario (cutting off price subsidies) illustrates possibility to avoid welfare losses for the poorest population groups and decrease inequality.

## 6. TRANSPORTATION

This section focuses on the transportation sector. Several factors justify the choice of transportation services for our investigation. First, privileges in transportation sphere are among the most cost-absorbing and cover significant shares of population. According to the Ministry of Finance 2006 estimates, funds needed for transportation privileges constituted approximately UAH 8.5 billion. Second, transportation privileges along with maintenance of low transport tariffs discourage sector development and lead to degradation of the public transport. Third, the sector of public transportation calls for financial and administrative reforms. Transport sector of Ukraine is predominantly in state ownership. The entire national road network, railway system, ports and airports are state-owned; urban transportation (except for taxi and mini-buses) is in communal ownership. Such strong state presence may lead – and in fact has led - to frequent management changes and absence of long-term development programs. Not to mention the problem of adequate financing. Being a subject to state regulation, transportation tariffs are far below the costs. Consequently, the sector's assets are eroding, while indebtedness rising. Monetization reform should lead to a more efficient sector operation. The need for reform was recognized by the Ministry of Transport, which in June 2008 announced initiating monetization of public transportation privileges.

### 6.1 Transportation privileges

Transport privileges are regulated by 22 legislative acts, 13 of which regulate privileges based on social status, and the remaining 9 – based on occupational status. According to this legislation, transport privileges are provided within the following categories of transportation services:

- Intracity public transportation including metro, bus, trolleybus, and tram (except for taxi);
- Local transportation in rural areas (bus);
- Bus, railway, and water transportation of local routes (within oblast);
- Intercity travel by bus, railway, water, and air transport (in most cases, once per year round trip).

The largest category of the above is intracity public transportation, which accounts for all pensioners and students of Ukraine, not to mention the rest (less numerous) categories of privilege recipients.

All recipients of transportation privileges can be conditionally divided into social group and occupational group. Social group consists of vulnerable categories of population and individuals who have rendered great services to Ukraine, which in most cases tend to be a vulnerable group as well. Occupational group consists of several categories of government employees, such as military and court personnel (see Table 6.1). Table 6.1 lists all categories eligible for transportation privileges and gives detailed description of privilege types. Intercity transportation privileges, as a rule, are provided with some limitations: either only once per year, or during specific period of time. The exceptions are exclusively occupational status categories: members of Parliament, Court personnel, Public Prosecutors' office personnel, Ukrzaliznytsya employees (only railway transport), military personnel (specific cases stipulated by the law, but covering almost all possible needs for transport).

It is worth noting, that in 2008, several legislative changes introduced income-testing criteria for certain social benefits/privileges, including transportation. These legislative changes were to enter into force May 1, 2008; however, to the best of our knowledge, in practice nothing has changed. Nevertheless, income-testing exists, at least, on paper; Table 6.1 highlights those cases when simple income-test is used (890 UAH of monthly income per family member, taking into

account the precedent six months); and when a multiplication coefficient of 1.1 is used ( $890 \times 1.1 = 979$  UAH of income per family member).

**Table 6.1 Transportation privileges by category of recipients and type of transport**

Category of privilege recipients	Intracity and local routes		Intercity	
	Rail	Others	Rail	Others
<b><i>Social Privileges</i></b>				
War veterans*	+	+	50%/1	50%/1
Chornobyl accident victims (Category I, II)	+	+	100%/1	100%/1
Individuals with special merits and their spouses or parents (after individuals death)	+	+	100%/1	100%/1
Individuals with special labor merits and their spouses or parents (after individuals death)	+	+	100%/1	100%/1
Labor veterans	+	+		
Victims of Nazi repressions and their spouses (after victims death)	+	+	50%/1	50%/1
Children of war**	+	+		
Rehabilitated victims of political repressions (if retired or invalids)		+		
Invalids and attendants of children-invalids or invalids of Group I**	+	+	50% (1.10 - 15.05)	50% (1.10 – 15.05)
Orphans (during school holidays)			+	+
Children of large families (only for school trips)		+		
Pensioners	+	except metro		
<b><i>Occupational Privileges</i></b>				
Members of Parliament	+	+	+	+
Members of Parliament (when retired)			100%/1	100%/1
Deputies of local radas	+	+		
Military personnel	+	+	50%	50%
Personnel of Public Prosecutors' Offices	+	+	+	+
Ukrzaliznytsya employees			+	
Court (judges)	+	+	+	+
Veterans of the Ministry of Defense, National Security Service, Ministry of Interior, other executive agencies and military units, Veterans of the state fire fighting service and their spouses (after veterans death)	+	+	100%/1	100%/1
Students	50% (29.09– 29.06)	50% (29.09– 29.06)	50% (29.09–29.06)	50%*** (29.09–29.06)

Source: CASE Ukraine

+ - free use of transport without restrictions

50% - with 50% discount

50%/1 – with 50% discount once per year

100%/1 – with 100% discount once per year

■ – income tested (890 UAH per family member)

\* - category includes participants in combat operations, war invalids, war participants, individuals with status comparable to war participants, widows(ers) of war veterans.

\*\* - income tested and multiplied by 1.1 coefficient (890\*1.1=979 UAH per family member)

\*\*\* - only auto-transport

## 6.2.Privileges provision mechanism

The main problem that hinders effective privilege provision in Ukraine is the lack of a unified database comprising all eligible individuals for all kinds of social benefits and privileges, including transportation. First steps towards compiling such database were taken in 2004. Before that, the amount of funding for transportation privileges was estimated based on previous year budget data, availability of funds, and was dependent on the service providers lobby. Today, a unified register exists; it is being compiled by the Ministry of Labor and Social Policy (hereinafter – MLSP Register). However, the register is still incomplete. Namely, it does not account for (1) people receiving privileges under Resolutions of the Cabinet of Ministers (which include the largest category - pensioners); (2) people, eligible based on occupational status. Another problem with the MLSP Register is that it is not personificated, and, therefore, might contain duplications on privilege recipients: one individual might be eligible to privileges on the basis of several different laws.

Currently, transportation privileges are provided simply based on identity cards of privilege recipients (for example, pensioner or student id), which should be presented directly to the service provider when traveling/buying tickets. Under current system of transportation privilege provision, the actual amount of transportation services consumed by privileged individuals cannot be exactly determined.

Early 2008, the Government came up with an initiative to solve the problem of poor register system of transportation privileges. This initiative envisaged providing special travel documents to all privileged individuals. In order to obtain these travel documents, privilege recipients have to apply to the corresponding social security departments with all needed documentation to prove their privilege rights. In such a way, all privileged individuals can be counted and properly registered. However, to the best of our knowledge, this initiative has not been given a tryout in practice.

## 6.3.Cost of privileges

According to the official data, currently, the total of 24.5 million<sup>9</sup> of people (which constitutes 53% of population) are entitled to free or discounted transportation service. Such a big number - 24.5 mln – is formed mostly at the account of intracity privileges, which cover the largest groups of privilege recipients: pensioners and students. Indeed, just these two categories give us an estimate of 22.4 million people, which is the number of pensioners (14 mln) and students (8.4 mln) in Ukraine<sup>10</sup>. According to the MLSP Register, there are 15.5 million of individuals eligible for intracity transportation privileges and about 4.4 million – for intercity transportation privileges. However, as it was stated above, this Register is somewhat problematic: on the one hand, it is incomplete, on the other, contains duplications.

In 2006 the State Budget provided UAH 830 million for transportation privileges coverage as subventions to local budgets. Household Budget Survey (HBS) data of 2006 gives a bit lower figures: about UAH 609 million was received as transportation privileges by around 5 million of Ukrainian households. According to HBS data, 4.8 million households received intracity transportation privileges in 2006, while only slightly over 200 thousand households got intercity privileges.

The Ministry of Finance, when calculating total privilege cost, uses its own estimates of travel cost per person per month. These estimates vary depending on the category of privilege recipient. Thus, for war and labor veterans, as well as for military invalids the monthly cost is

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<sup>9</sup> Source: Ministry of Transport and Communications.

<sup>10</sup> According to State Statistics Committee 2006 data.

estimated at UAH 25.4, assuming that individual makes 22 trips by intracity transport (UAH 0.64<sup>11</sup> per trip) and 4 trips by suburban transport (UAH 2.82 per trip) per month. The travel cost for children-invalids and for Chernobyl victims Category 1 is estimated at UAH 16.2 per month. The monthly cost of travel for Chernobyl victims Category 2 is UAH 50.7, since it is an able-to-work category. The military service veterans' travel cost is estimated at UAH 36.6 per month. What concerns intercity transport – the Ministry of Finance uses here only three standardized annual costs: UAH 200 for people, which have rendered great services to Ukraine (travel in a 1<sup>st</sup> class compartment), UAH 120.5 for war invalids and Chernobyl victims, and UAH 60.3 for all other categories of privilege recipients. Using these estimates of the Ministry of Finance and the number of people eligible for privileges under each category (according to MLSP Register), we calculated weighted average cost per person for intracity and intercity transportation (see Table 6.2). For the purpose of comparison, Table 6.2 also contains estimates from HBS 2006 database. The intracity privilege figure, based on HBS, apparently, is lower than Ministry's estimates – this might be due to the respondents' underestimation of their real travel costs.

**Table 6.2 Transportation privilege cost estimates**

Privileges	Weighted average cost per household (HBS), UAH	Weighted average cost per person*, UAH
Intracity and local transportation	10.2 per month	20.7 per month
Intercity (bus, railway, water, air) transportation	60.6 per year	68.5 per year

Sources: Household budget survey 2006;

\*Estimates from A. Nechai report "Analysis of special privileges in Ukraine", Case Ukraine calculations.

#### 6.4. Privilege funding schemes

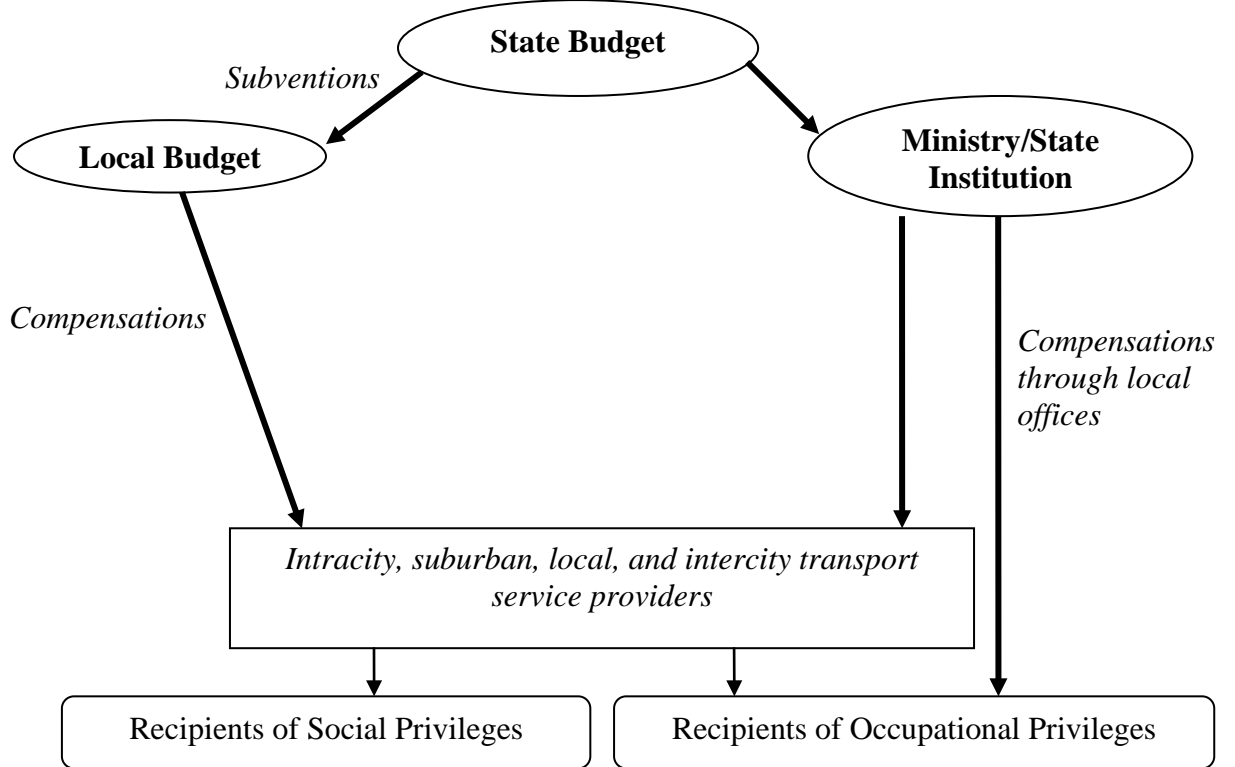
According to the articles 89 and 102 of the Budget Code, transportation service providers receive compensations for free/discounted travel of privileged individuals from the local budgets; the local budgets, in turn, receive subventions from the State Budget specifically for the purpose of these compensations (see Scheme 6.1). However, during the last years privileged travel is funded, predominantly, through clearing operations (offsetting of debts). Such mechanism enables transportation service providers to pay only for their electricity debts, and makes them accumulate wage arrears and tax debts. Local budgets receive subventions mainly for those categories of recipients, which are based on social status. Funds for privileges based on occupational status are distributed through the corresponding ministries or other state institutions.

For the category of students this payment scheme is a bit different. First of all, there is a division between intracity and other student transportation privileges based on the source of funding: intracity transportation privileges for students are compensated from the local budgets, while State budget compensates intercity and suburban transport(see Scheme 6.2). The Ministry of Education receives funds from the State Budget and allocates them to (1) educational institutions for suburban and bus intercity service providers and to (2) Ukrzaliznytsya for railway intercity trips.

<sup>11</sup> These rates will soon have to be revised, since intracity transport tariffs are rising. For example, in Kyiv starting from November 1, 2008 intracity tariffs constitute UAH 2 for metro and UAH 1.5 for surface transport (based on 30 September, 2008 decision of Kyiv Rada).

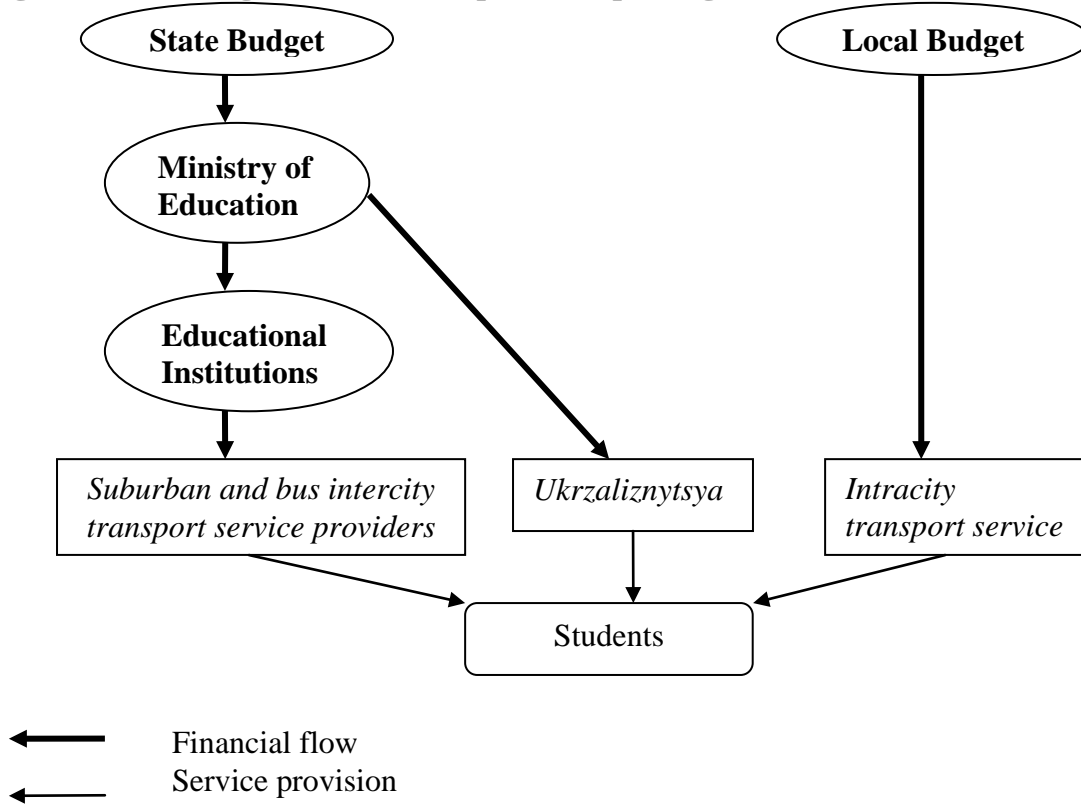


**Figure 6.1 Funding scheme of transportation privileges**



Source: CASE Ukraine compilation

**Figure 6.2 Funding scheme of transportation privileges for students**



Source: CASE Ukraine compilation

## 6.5 Distribution of transportation privileges

According to Household Budget Survey, over 4.9 million of households reported that they were using in-kind transportation privileges in 2006. The total amount of transportation privileges used by this population equals approx. 609 million UAH. It is worth noting, that only 14.8% of total transportation privilege recipients reside in rural areas; while the rest 85.2% are urban residents.

**Table 6.3 Transportation privilege incidence, by locality**

Privilege	urban		rural	
	# of hhs recipients	share in total recipients, %	# of hhs recipients	share in total recipients, %
Transportation	4,205,725	85.21	729,976	14.79
Intracity	4,159,464	85.60	699,467	14.40
Intercity	132,600	65.06	71,219	34.94

Source: HBS 2006

Transportation privileges are distributed very unevenly, concentrating in richest 30% of population. The wealthier are the households, the more transportation privileges they receive. This trend is clearly seen in the table below, where the number of recipients and amounts of privileges received are given by deciles.

**Table 6.4 Transportation privilege incidence, by expenditure deciles**

Decile	Min	Max	# of hhs recipients	share in total hhs recipients, %	total privilege amount, UAH
1	81.08	308.73	224.233	4.54	16 745.609
2	308.79	378.75	302.651	6.13	35 981.049
3	378.76	442.96	435.038	8.81	43 543.759
4	443.03	505.77	379.641	7.69	37 747.174
5	506.01	573.82	500.526	10.14	60 822.873
6	573.82	649.87	551.985	11.18	68 542.669
7	650.00	743.34	577.663	11.70	59 018.845
8	743.57	874.84	607.564	12.31	74 417.053
9	874.86	1 122.49	642.892	13.03	97 208.801
10	1 122.54	24 807.05	713.508	14.46	114 725.996
total	81.08	24 807.05	4 935.701	100.00	608 753.828

Source: HBS 2006

## 6.6 Simulation scenarios description

Using HBS data three basic scenarios were developed to calculate the effect of a hypothetical monetization of in-kind transportation privileges on poverty and inequality.

### 1. SCENARIO: 'ZERO OPTION'.

'Zero option' scenario assumes abolishing transportation privileges for all recipients with no exception. Scenario 1 is viewed as a benchmark. All other scenarios are developed based on this benchmark scenario. For monetization simulations, all non-cash transportation privileges

are selected; correspondingly, HBS variable 'e10\_2', described as "the cost of in-kind transportation privileges", is used in our calculations.

## 2. INCOME TEST SCENARIO.

Scenario 2 is developed based on an income test, which is used to identify 'eligible' people for the privilege abolishment. As our income test, we use the official income test introduced for transportation privileges in legislation in 2008, which equals 890 UAH of monthly income per family member, taking into account the precedent six months. However, since this income test was introduced in 2008, but we use 2006 data, we deflate it by cumulative CPI of 2006 and 2007 (30%)<sup>12</sup>:  $890/1.3=684$  UAH. Therefore, we end up with 684 UAH of total monthly expenditures per equivalent unit<sup>13</sup> as a threshold to identify those to be deprived of transportation privilege.

The amount of money collected from this abolishment we redistribute to the population with monthly expenditures per equivalent unit less than 684 UAH. Thus, scenario 2 monetization results will be the following: (1) for the privilege recipients with total monthly expenditures per equivalent unit higher than 684 UAH transportation privilege is abolished; (2) for the recipients with total monthly expenditures per equivalent unit less than 684 UAH transportation privileges are increased and monetized.

## 3. 'FEASIBLE GROUP' SCENARIO.

Scenario 3 is aimed at developing an easy-to-implement scheme of monetization and redistribution of cash to a specific category of population. In this scenario, first, we abolish transportation privileges for all (our benchmark), then redistribute the collected amount to the vulnerable and at the same time 'feasible group', in our case, pensioners with the lowest pensions. Under the current system, pensioners are the major group of transportation privilege recipients. Poor pensioners deserve social support and they are relatively easy to reach. As poor pensioners we select recipients of any type of pensions (retirement, invalid, for long service, social) but with annual pension lower than 4,500 UAH.

Thus, monetization scenario 3 will be the following: (1) transportation privileges are abolished for all; (2) pensioners with annual pensions below 4,500 UAH receive cash handout as pension supplements.

In all transportation scenarios inequality is measured by calculating Gini coefficient for total monthly expenditures per equivalent unit; poverty rate is measured based on official poverty line in 2006.

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<sup>12</sup> Cumulative CPI calculated as  $1.116*1.166=1.3$ , where 11.6% - 2006 CPI; 16.6% - 2007 CPI. Source of CPI: State Statistics Committee.

<sup>13</sup> According to State Statistics Committee methodology, equivalent unit scale is used, where household head = 1 and other household members = 0.7

## 6.7 Results of simulations

Below we describe the results of simulations based on our three transportation scenarios defined in the previous section. Detailed results for all scenarios can be viewed in the Appendix C.

### 1. SCENARIO: 'ZERO OPTION'.

Benchmark scenario (abolishment of transportation privileges for all) gives us an increase in inequality – Gini coefficient increases by 0.01 percentage point from 29.73 to 29.74. In fact, such small change in Gini coefficient can be viewed as negligible. This gives us grounds to say that the present system of transportation privileges (the way they are distributed) does not affect inequality in society. With or without transportation privileges – the overall inequality picture does not change.

### 2. INCOME TEST SCENARIO.

As a result of our income test, we have 2,610,688 households, which are granted transportation privileges in monetary form. The total amount of money to be redistributed evenly among them equals 608,753,828 UAH. Thus, we end up with cash handouts of 233 UAH per household per year, or 19.40 UAH per household per month.

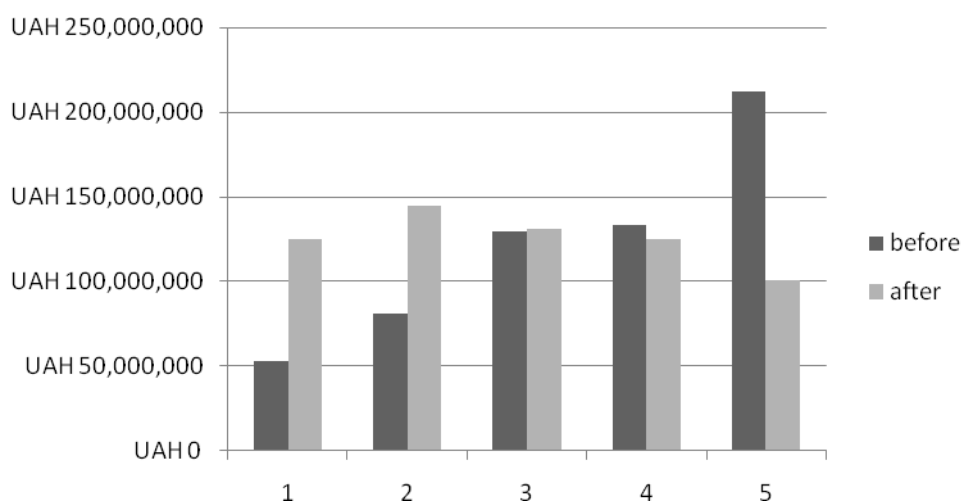
This scenario results in lowering inequality to 29.63, which is a 0.1 percentage point decrease compared to initial stance (Appendix C). The effect on poverty is also downward: poverty rate decreases by 0.17% from 28.08% to 27.91%.

### 3. 'FEASIBLE GROUP' SCENARIO.

This scenario, just as 'income test' scenario redistributes the total amount of 608,753,828 UAH. Our feasible group, pension recipients with annual pensions below 4,500 UAH, totals 5,219,457 individuals. Thus, even distribution of the given amount results in cash handouts of 116 UAH per person per year.

'Feasible group' scenario results in more even distribution of transportation privileges. The Figure 6.3, where privilege distribution by quintiles before and after the reform is shown, demonstrates this very well.

**Figure 6.3 Transportation privileges/cash handouts distribution before and after Scenario 3 reform, by expenditure quintiles**



Source: CASE Ukraine calculations

Indeed, we see that after the reform privileges are distributed more evenly. In fact, the first two quintiles (poorest 40%) now receive two times more 'privilege money' than before the reform.

With regard to poverty and inequality, this simulations scenario decreases both of them: Gini coefficient drops by 0.06 percentage points to 29.67; and poverty decreases by 0.07% (Appendix C).

Summing up, we should emphasize that quite expectedly our monetization scenarios have positive – although rather slight -- effect on poverty and inequality in society. We manage to decrease Gini coefficient and poverty rate, operating with relatively small amounts of privilege money. Understandably, 'income test' scenario demonstrates the most sizable effects on poverty and inequality. However, this scenario is not so easy to implement: problems arise when it comes to household's income assessment. 'Feasible group' scenario compensates for this shortcoming by an easy-to-implement mechanism of monetization and redistribution of cash to a specific category of population.

## 7. SANATORIUM AND HEALTH RESORT TREATMENT

The system of sanatorium-and-spa treatment is inherited from the Soviet Union, when they were solely in state ownership. Today, sanatoria and health resorts are still, predominantly, state-owned, but there are private resorts as well. State-owned sanatoria are either under control of the Ministry of Health or within the jurisdiction of other ministries or state institutions, such as the Ministry of Internal Affairs, Ministry of Defense, Security Service of Ukraine, etc. A substantial number of Ukraine's sanatoria and health resorts are within the jurisdiction of "Ukrprofozdorovnytsya", which was founded in 1992 by the Trade Union Federation of Ukraine and Social Insurance Fund. "Ukrprofozdorovnytsya" unites 81 sanatoria and 66 tourist resorts, which are located in different parts of Ukraine. The traditional health resorts zones of Ukraine are Crimea and Carpathians.

The majority of sanatoria in state ownership are degrading. They lack funds for renovation works and new equipment purchase or have no stimuli for any improvements; therefore, the level of services in such places is very low, quality of medical services and equipment is poor. Moreover, the system of granting privileges based on decisions of local officials and, in some cases, doctors creates incentives for corruption and funds theft. Monetization of sanatorium treatment privileges would leave the right of sanatorium choice to the individual, and create stimuli for sanatoria and health resorts to compete for their clients.

### 7.1 Sanatorium and health resort privileges

Sanatorium treatment privileges are provided to the majority of recipients once per year, for certain categories – once per two years. The amount of sanatorium vouchers for privileged individuals is determined by the Cabinet of Ministers annually based on the availability of state budget funds.

Sanatorium privilege recipients are conditionally divided into two groups based on their status: social and occupational (see Table 7.1). The largest groups of privilege recipients based on social status are war veterans, labor veterans, and Chernobyl victims. Social privilege recipients receive their sanatorium vouchers either from the local social protection administration offices, or at their place of work/former work. Individuals receiving privileges based on their occupational status obtain sanatorium treatment services in the corresponding departmental sanatoria or health resorts. For example, military servicemen and their family members get treatment in the health resorts of the Ministry of Defense, while Ministry of Internal Affairs veterans - in the sanatoria of the Ministry of Internal Affairs.

**Table 7.1 Sanatorium privileges by category of recipients and conditions of provision**

Category of privilege recipients	Privilege provision	
	Discount	Times per year
<b><i>Social Privileges</i></b>		
Chornobyl accident victims (Category I, II, III, IV)	100%	once
War invalids	100%	once
Combat operations participants	100%	once
War participants	100%	once per 2 years
Individuals with special merits and their widows	100%	once
Individuals with special labor merits	100%	once
Labor veterans	100%	once
Rehabilitated victims of political repressions	100%	once
Invalids and children-invalids	100%	once
Pensioners*		once
<b><i>Occupational Privileges</i></b>		
Members of Parliament	100%	once
Military servicemen and their family members, military invalids	75%	once
Court (judges)	100%	once
Veterans of the Ministry of Defense, National Security Service, Ministry of Internal Affairs, State Service of special communication and information protection of Ukraine, Civil Protection Service, State fire fighting service and their family members	100%	once

Source: Ukrainian laws and Government resolutions

\* Pensioners' sanatorium privileges (specifically the amount of discount) are subject to decisions on trade unions level or enterprise level.

## 7.2 Cost of privileges

In 2006, the total cost of sanatorium treatment privileges was estimated by the Ministry of Finance at 8.2 billion. However, the State Budget 2006 financed only UAH 1.5 billion. Thus, there is a huge underfinancing of sanatorium privileges or substantial overestimation of privilege costs. The latter is very likely due to numerous duplications in the recipients registering system. Table 7.2 below provides costs estimates per person of the Ministry of Finance (depending on the category of sanatorium treatment recipients) and total costs for each category. The total cost is calculated based on the number of privilege recipients from the MLSP Register. It has to be mentioned that table 7.2 is incomplete as it includes only certain categories of social status recipients, however it already gives a total cost of over UAH 6.7 billion. On the other hand, the Ministry of Finance estimates do not account for possible duplications in the MLSP Register data. Therefore, total costs are most likely to be overestimated.

**Table 7.2 Sanatorium privilege costs by category of recipients**

Category of privilege recipients	Cost per person (UAH)	Total cost (ths. UAH)
Chornobyl accident victims (Category I, II, III)	1700	1,429,303.00
Chornobyl accident victims (Category IV)	850	650,125.00
Combat operations participants	2367	712,723.00
War participants	2367	2,684,603.00
Individuals with special merits and their widows	2367	7,578.00
Military service veterans	2367	462,056.00
Rehabilitated victims of political repressions	2367	32,166.00
Invalids	2367	724,883.00
<b>Total</b>		<b>6,703,437.00</b>

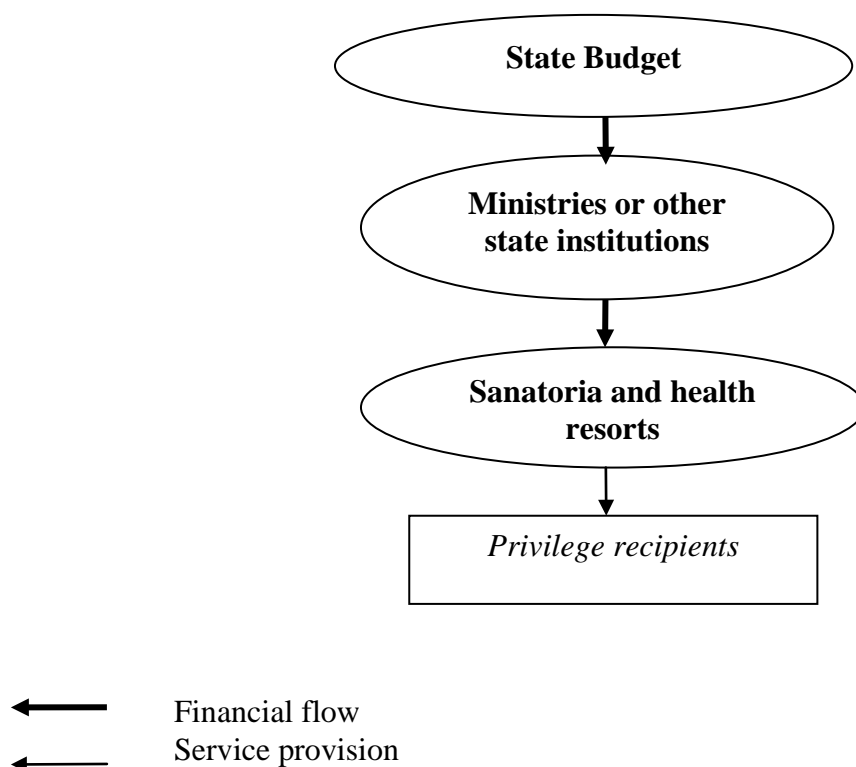
Source: A. Nechai report "Analysis of special privileges in Ukraine"

For the purpose of comparison, we provide data from the HBS 2006 on sanatorium and health resort treatment privileges. Thus, according to HBS data, 481,545 households received sanatorium treatment privileges in 2006; weighted average cost of sanatorium treatment privileges per beneficiary equals UAH 2,065 per year. Also, HBS accounts for those households, which received compensations for the unused right of privileged sanatorium treatment – the total of 197,341 households. On average, these compensations are equal to approx. UAH 135.

### 7.3 Sanatoria funding schemes

State-owned sanatoria and health resorts are funded by the State Budget. Sanatoria receive compensations for providing privileged treatment through corresponding Ministries or other state institutions. Thus, occupational privileges are compensated directly from the controlling state institutions. For example, if sanatorium is within the jurisdiction of the Ministry of Defense, compensations are received from this Ministry. Privileges based on social status are compensated either from the Ministry of Health, or Ministry of Labor and Social Policy. All ministries or other state institutions receive subventions from the State Budget.

**Figure 7.1. Funding scheme of sanatorium treatment privileges**



Source: CASE Ukraine compilation



What concerns the sanatoria within the jurisdiction of “Ukrprofozdorovnytsya”; their privileged visitors are most likely funded by the “Ukrprofozdorovnytsya”, probably at the expense of enterprises. Unfortunately, more reliable information is not available, since “Ukrprofozdorovnytsya” is a closed corporation, which is not transparent.

#### 7.4 Distribution of sanatorium privileges

According to HBS 2006 data, the total amount of sanatorium privileges constituted approx. 995 million UAH. Over 480 thousand households received sanatorium privileges in 2006. In total structure of recipients rural population comprises only 14.2%, the rest 85.8% - are urban residents. Sanatorium privileges share common patterns of distribution with transportation privileges. Over 60% of sanatorium privilege recipients also concentrate in richest 30% of population. In terms of money, distribution pattern gets even worse: over 68% of sanatorium privilege money settle in deciles 8, 9, and 10 (richest 30%). Table below demonstrates the distribution of sanatorium privileges by expenditure deciles.

**Table 7.3 Sanatorium privilege incidence, by expenditure deciles**

Decile	Min	Max	# of hhs recipients	share in total hh recipients, %	total privilege amount, UAH
1	81.08	308.73	4,370	0.91	4,650,200
2	308.79	378.75	11,273	2.34	14,541,987
3	378.76	442.96	20,266	4.21	23,394,466
4	443.03	505.77	21,646	4.50	35,924,716
5	506.01	573.82	32,035	6.65	57,953,685
6	573.82	649.87	39,297	8.16	79,993,550
7	650.00	743.34	50,801	10.55	100,152,153
8	743.57	874.84	43,269	8.99	68,197,233
9	874.86	1122.49	100,881	20.95	206,125,197
10	1122.54	24807.05	157,707	32.75	403,602,252
total	81.08	24807.05	481,545	100.00	994,535,438

Source: HBS 2006

#### 7.5 Simulation scenarios description

Using HBS data we develop three basic scenarios to calculate the effect of a hypothetical monetization of in-kind sanatorium privileges on poverty and inequality.

##### 1. SCENARIO: 'ZERO OPTION'.

'Zero option' scenario assumes abolishing sanatorium privileges for all recipients with no exception. Scenario 1 is viewed as a benchmark. All other scenarios are developed based on this benchmark scenario. For monetization simulations, all sanatorium privileges are selected; correspondingly, HBS variables 'ex6', 'ex7', and 'ex8', described as “the cost of privileges for sanatorium, health resort, and tourist vouchers”, are used in our calculations.

##### 2. INCOME TEST SCENARIO.

Scenario 2 is developed based on an income test, which is used to identify 'eligible' people for the privilege abolishment. As our income test, we use double subsistence level in 2006:

465UAH\*2=930UAH. In other words, we choose 930 UAH of total monthly expenditures per equivalent unit as a threshold to identify those to be deprived of sanatorium privilege. Higher threshold for sanatorium compared to transportation is explained by health resorts services being more expensive than transportation – only families with higher level of income and, consequently, expenditures can afford a health resort vacation.

The amount of money collected from this abolishment we redistribute to the population with total monthly expenditures per equivalent unit below 930 UAH. Thus, scenario 2 monetization results will be the following: (1) for the privilege recipients with total monthly expenditures per equivalent unit more than 930 UAH sanatorium privileges are abolished; (2) for the recipients with total monthly expenditures per equivalent unit lower than 930 UAH sanatorium privileges are increased and monetized.

### 3. 'FEASIBLE GROUP' SCENARIO.

Scenario 3 is aimed at developing an easy-to-implement monetization and redistribution of cash handouts as supplements to some other social payments. In this scenario, first, we abolish sanatorium privileges for all (our benchmark), then redistribute the collected amount to the 'feasible group'. For sanatorium privilege scenario, as 'feasible group' we select disadvantaged families which receive special social assistance for such poverty-stricken households. Thus, monetized privileges would be treated as cash supplements to social assistance benefits already granted.

In all sanatorium scenarios inequality is measured by calculating Gini coefficient for total monthly expenditures per equivalent unit; poverty rate is measured based on official poverty line in 2006.

## 7.6 Results of simulations

Below we describe the results of simulations based on our three sanatorium scenarios defined in the previous section. Detailed results for all scenarios can be seen in the Appendix D.

### 1. SCENARIO: 'ZERO OPTION'.

Benchmark scenario (abolishment of sanatorium privileges for all) gives us a decrease in inequality – Gini coefficient declines by 0.07 percentage point from 29.73 to 29.66. In other words, without sanatorium privileges, in their present pattern of distribution, there would be slightly less inequality in society. Therefore, simple abolishment of all sanatorium privileges is already a step forward towards greater equality.

### 2. INCOME TEST SCENARIO.

As a result of our income test of double subsistence level, we have 254,396 households, which are granted sanatorium privileges in monetary form. The total of sanatorium privileges in the amount of 994,535,438 UAH is redistributed evenly among them. We end up with cash handouts of 3,909 UAH per household per year.

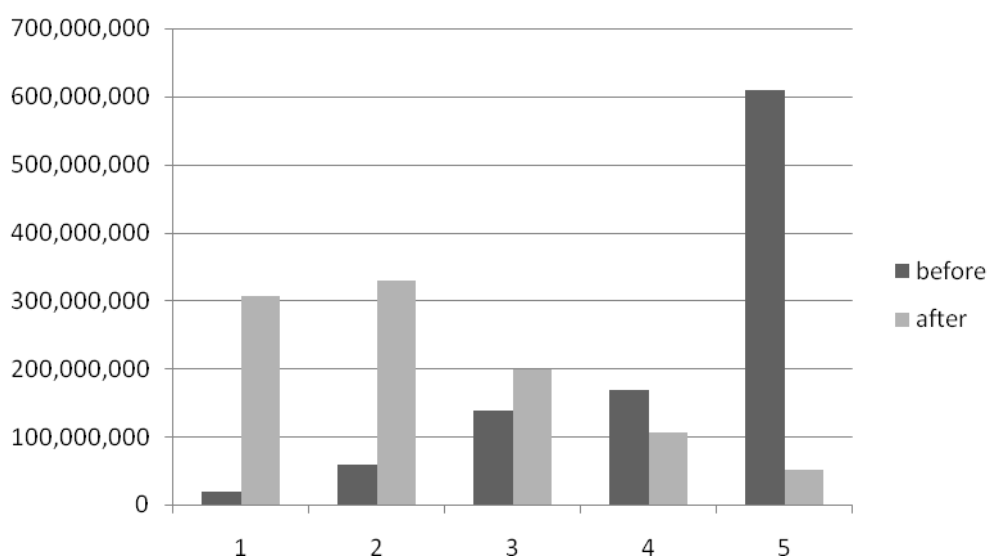
Such redistribution lowers inequality to 29.61, which is a 0.12 percentage point decrease compared to initial stance (Appendix D). Income test scenario also leads to a decrease of the poverty rate by 0.13 p.p., from 28.08% to 27.95%. It is worth noting, that this scenario results do not differ much from simple abolishment scenario, in terms of its effect on inequality. This is explained by relatively small number of households (compared to total population), which receive sanatorium privileges and are involved in sanatorium simulations.

### 3. 'FEASIBLE GROUP' SCENARIO.

As our 'feasible group' we choose – low-income households, which are poverty-stricken households receiving special social assistance. According to HBS, there are a total of 360,436 such households, which is approx. 2% of the total population. We distribute evenly among these households the total amount of sanatorium privileges = 994,535,438 UAH. Thus, each household is entitled to 2,759 UAH of cash handouts per year.

'Feasible group' scenario results in more even distribution of sanatorium privileges. The Figure 7.2, where privilege distribution by quintiles before and after the reform is shown, demonstrates this very well. We see that before the reform (present situation) sanatorium privilege money is distributed extremely unevenly, with two thirds of all money concentrating in the fifth quintile. Scenario 3 reform changes this distribution tangibly, locating over USD 600 mln. to the first two quintiles.

**Figure 7.2. Sanatorium privileges/cash handouts distribution before and after Scenario 3 reform, by expenditure quintiles**



Source: CASE Ukraine calculations

As a result of this scenario, we observe a record inequality decrease by 0.3 percentage points from 29.73 to 29.43 (Appendix D). Poverty also decreases by a record 0.52 p.p. from 28.08% down to 27.56%.

In conclusion, all our sanatorium scenarios have positive but small effects on inequality and poverty: Gini coefficient and poverty rate slightly decrease throughout the simulations. It is worth noting, that as expected 'feasible group' is the most efficient and easiest to implement scenario. Poverty rate and Gini coefficient decrease the most as a result of this scenario.

## 8. CONCLUDING REMARKS

During the last decade Ukraine has made an impressive progress in reforming its economy, enforcing diverse market-support institutions, and strengthening its civil society. However the speed of reforms has been quite uneven. In some areas, such as private sector development and advances of the banking sector, the progress has been very impressive, while in some other areas no much change has occurred. Socio-economic privileges, granted by the state to a large number of occupational and social groups, continue to operate in roughly the same way as they did two decades ago during the Soviet times.

The main objective of this project has been to study the current system of social assistance in selected sectors of the economy and assess impacts of several hypothetical scenarios for reforming this system in order to improve benefit targeting to the lowest income echelons of the population.

While not being at a position to prescribe concrete reforms of the system, we have designed several variants of the benefit monetization in order to consider alternative hypothetical directions of reforms and assess their effects on the recipients of social assistance. Main scenarios imply replacement of in kind transfers (privileges or price subsidies) by the new schemes of cash benefits clearly supporting the poor. A potentially important contribution of this study is the elaboration of a methodology which, after further conceptual and technical refinements, could be used to support social assistance reforms as well as to assist social policy monitoring and evaluation efforts. As byproducts of our project, we have compiled a few studies on the experience in the area of reforming social assistance in Russia and several Central European countries, as well as collected and analyzed data and legislation related to social assistance and poverty issues in Ukraine.

In our opinion, the need for social assistance reform is reinforced by current financial crisis, which is expected to inflict a negative impact on budget revenue while increasing budgeting needs. In addition to longer-term trends, such as the increase of pension age population and decline of active labor force, the short-term shifts in labor employment and households' incomes, brought about by the upcoming recession, may result in impoverishing large numbers of population and requiring a substantial increase in state aid in order to support the growing number of families living below a poverty level. This will require redirecting large amounts of funds to support low income families and improve the targeting of this aid.

As indicated in our study, there are many shortcomings of the current system, including its poor targeting, high costs of implementation, low transparency, substantial market distortions, support for "soft budget constraints" in organizations and enterprises delivering services to the population (in housing utilities, public transportation, sanatoria, etc.), and continued support for local monopolists subsidized by the state. The deficiencies of state social aid targeting, excessive price subsidization, and softness of budgets of social service providers makes the Ukrainian economy susceptible to diverse tribulations, such as overconsumption of certain goods and services (e.g., energy), low quality and/or underconsumption of other goods and services (e.g., healthcare), deficient allocation of housing, etc.

Both policymakers and population at large seem to understand that the current system is consistent with neither a notion of social justice nor the needs of an advanced market economy and can not sustain during a longer period of time. The bulk of budget transfers are effectively delivered to the upper income layers of the Ukrainian population and only a small fraction end up supporting those the most needy. In Table 8.1 we present the amounts of privileges and benefits granted to the poorest and richest quintiles of population in the three sectors covered by our study.

**Table 8.1. Total amounts of benefits and privileges granted to households in three sectors (housing, transportation and sanatoria), by income quintile, 2006, million UAH**

<b>Sector</b>	<b>Lowest income quintile</b>	<b>Highest income quintile</b>
Housing Benefits	37.9	30.7
Housing Privileges	178.5	467.8
Transportation	52.7	211.9
Sanatoria	19.2	609.7
<b>Total</b>	<b>288.3</b>	<b>1320.2</b>

Source: HBS 2006

Additionally, the still practiced (in some cases quite complex) price subsidies are supporting indiscriminately all consumers regardless of their income. Since higher income population affords more consumption (e.g., of energy) it tends to absorb a larger share of subsidies than the low income people.

As emphasized in our study, the system is “extensive, expensive, and complicated”. Most of Ukraine’s residents are eligible for some kinds of benefits and privileges and the provision of these benefits/privileges requires a costly bureaucratic machine, although no accurate estimates of the total cost of the maintenance of this system is available.

Many operations of the social assistance system are highly nontransparent. Under budgeting pressures some areas of social assistance are underfinanced and commercial enterprises are forced to subsidize their deliveries to the public sector, which undermines their competitiveness and healthy growth, promulgating arrears and murky barter deals. As a result, some monopolists are taking advantage of the social assistance system by overcharging for their services. The monitoring of social transfers spending remains weak. Still no comprehensive database of social assistance exists, which provides opportunities to some people and enterprises to abuse the system. Anet result of the current system is dilapidation of sanatoria, decay of housing, and slow modernization of the public transportation.

An extensive experience of Russia, Poland, and other countries of the region suggests that while struggling with similar systemic deficiencies, these countries were only partially successful in reforming their social policies. These countries appear to be, at best, at a mid-point of reforms and are expected to undertake more efforts in order to improve targeting and the overall efficiency of their social assistance systems. It seems that useful lessons may be drawn from this experience which could help Ukraine, and other countries which are followers rather leaders in these reforms, in formulating their own reform strategies.

Reforms of social assistance belong to a highly sensitive area, of potentially great impacts on politics, economic growth and overall socio-economic welfare. The cost of mistakes is very high. The governments tend to be slow in reform implementations due to strong resistance of those who either could lose as a result of these reforms or even could gain but they are not well informed and consulted. The main lesson is that an extensive due diligence is needed before any reform in the social assistance area may be implemented. Data collection, several feasibility studies, cost-benefit analyses and pilot experiments must be undertaken, followed by a consensus building (broad information campaign, extensive consultations with experts and all stakeholders), and creation of appropriate technical capacity of state organizations responsible for this implementation (financing, database, training, legislative acts and detailed regulations).

The monetization reforms in Russia, hurriedly implemented a few years ago in the form of “shock therapy”, are not believed successful. They ended up with confusion and a lack of both financial and technical capacities for enacting the changes. In most Central European countries, a sequence of consecutive reforms have been introduced, each of them intended to amend a

predecessor reform each of which considered deficient. This “evolutionary” approach to reforming has been done at an unnecessarily high cost and was responsible for confusion and instability.

Our hypothetical reform simulation scenarios have provided several insights into a potential direction of social assistance reform in Ukraine. It has been demonstrated that there are ways for simplifying the system, improving its targeting and reducing costs to the budget. While implementation of a single particular reform scenario, analyzed by our project, has proven not very significant in terms of reducing overall income inequality and poverty, the total systemic effect of introducing several reforms at the same time (or gradually) would be considerable. Perhaps the indirect effects of this reform may be even more important than short-term reduction in poverty and income inequality. A well designed reform will streamline and simplify the system, make it more transparent and less prone to abuse and corruption, reduce cross-subsidization, barter and payments arrears, and cut the costs of assistance delivery.

In our project we have considered selected in-kind benefits which monetization may be helpful, to some extent, in reforming the entire system. A convenient aspect of monetization is its monetary valuation principle which enables one to disentangle the existing quandary of complex administration and financing of the system, involving billions of hryvnia from diverse sources, different intricate deals between commercial companies, state agencies, and central and local governments, high cost of maintenance and delivery, and at the end a far from perfect targeting of social assistance.

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## LAWS AND NORMATIVE ACTS

Budget Code of Ukraine # 2542 – III dated June 21, 2001

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Cabinet of Ministers Decision “On Free Public Transport Travel for Students of Institutions of Higher Education” # 541 dated April 5, 1999

Cabinet of Ministers Decision “On Free Public Transport Travel for Local Rada Deputies” # 1738 dated November 16, 2002

Cabinet of Ministers Decree “On Implementation of Targeted Social Assistance to Low Income Families” # 238 dated February 22, 1999

Cabinet of Ministers Decree “On the Housing and Municipal Service Benefits Program” #89, dated February 4, 1995

Constitution of Ukraine # 254k/96-BP dated June 28, 1996

Law of Ukraine “On Heating Supply” # 2633-IV dated June 2, 2005

Law of Ukraine “On Housing Services” # 1875-IV dated June 24, 2004

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Law of Ukraine “On State Assistance to Families with Children”, # 2811-XII, dated November 21, 1992.

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Law of Ukraine “On Social Protection of Labor Veterans and Other Elderly Citizens” # 3721-XII dated December 16, 1993

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Law of Ukraine “On Status of Judiciary” # 2862-XII dated December 15, 1992

Law of Ukraine “On Victims of Nazi Repressions” # 1584-III dated March 23, 2000



## APPENDIX A. DISTRIBUTIONS OF HOUSING PRIVILEGES AND BENEFITS

Initial state of households' expenditures and housing benefits per month per equivalent unit

		Min	Mean	Median	Max	% of total
decile 1	Total Expenditures	81.1	247.3	255.9	308.7	3.67%
	Housing privileges	0.3	8.6	4.9	52.0	3.31%
	Housing Benefits	1.9	14.7	11.4	36.4	10.07%
decile2	Total Expenditures	308.8	346.0	345.6	378.7	5.14%
	Housing privileges	0.1	11.7	6.8	68.4	7.09%
	Housing Benefits	2.6	18.0	14.8	52.1	10.56%
decile3	Total Expenditures	378.8	410.6	410.3	443.0	6.09%
	Housing privileges	0.1	15.3	8.1	150.0	8.80%
	Housing Benefits	0.5	13.0	8.5	79.1	12.30%
decile4	Total Expenditures	443.0	475.3	475.7	505.8	7.05%
	Housing privileges	0.3	16.0	9.0	151.3	9.75%
	Housing Benefits	0.8	15.8	12.3	57.1	10.55%
decile5	Total Expenditures	506.0	539.1	538.8	573.8	8.01%
	Housing privileges	0.1	14.3	7.6	164.4	9.41%
	Housing Benefits	0.8	14.5	10.0	73.3	11.01%
decile6	Total Expenditures	573.8	610.9	609.7	649.9	9.06%
	Housing privileges	0.4	14.0	7.8	150.0	10.69%
	Housing Benefits	1.2	18.0	12.3	69.4	14.28%
decile 7	Total Expenditures	650.0	694.2	691.0	743.3	10.31%
	Housing privileges	0.2	16.5	10.3	98.7	11.64%
	Housing Benefits	1.5	19.2	15.6	88.2	8.90%
decile8	Total Expenditures	743.6	805.6	802.7	874.8	11.96%
	Housing privileges	0.3	18.3	12.3	132.8	13.00%
	Housing Benefits	1.5	14.4	9.1	65.4	7.70%
decile9	Total Expenditures	874.9	983.6	978.3	1122.5	14.59%
	Housing privileges	0.4	20.4	14.0	152.1	12.13%
	Housing Benefits	0.2	16.5	9.9	90.7	8.44%
decile10	Total Expenditures	1122.5	1623.4	1366.4	24807.1	24.12%
	Housing privileges	0.7	26.3	20.1	164.4	14.19%
	Housing Benefits	1.8	18.4	15.9	91.0	6.19%
Q10/Q1	Total Expenditures	13.8	6.6	5.3	80.4	

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## APPENDIX B. HOUSING PRIVILEGES

### Housing Privileges. Initial stance

#	Step	Scenario	Comments																																																																	
1	Select impact	Effect of monetization and redistribution of housing privileges and benefits on poverty and inequality																																																																		
2	Select data	Ukraine HBS 2006 annual																																																																		
3	Select unit of analysis	Equivalent unit, calculated as weighted average of household members when household head is taken as 1 and other hh members are taken as 0.7																																																																		
4	Use person weights to translate sample data into total population	Sample = 26 253 persons and 10 499 households Population = 45 359 944 persons and 17 417 477 households																																																																		
5	Use total expenditures to derive deciles	<p>Table: Total monthly expenditures per equivalent unit, UAH</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>81.08</td> <td>255.93</td> <td>247.31</td> <td>308.73</td> </tr> <tr> <td>2</td> <td>308.79</td> <td>345.62</td> <td>346.03</td> <td>378.75</td> </tr> <tr> <td>3</td> <td>378.76</td> <td>410.30</td> <td>410.63</td> <td>442.96</td> </tr> <tr> <td>4</td> <td>443.03</td> <td>475.71</td> <td>475.25</td> <td>505.77</td> </tr> <tr> <td>5</td> <td>506.01</td> <td>538.82</td> <td>539.11</td> <td>573.82</td> </tr> <tr> <td>6</td> <td>573.82</td> <td>609.74</td> <td>610.86</td> <td>649.87</td> </tr> <tr> <td>7</td> <td>650.00</td> <td>691.01</td> <td>694.22</td> <td>743.34</td> </tr> <tr> <td>8</td> <td>743.57</td> <td>802.66</td> <td>805.56</td> <td>874.84</td> </tr> <tr> <td>9</td> <td>874.86</td> <td>978.30</td> <td>983.63</td> <td>1 122.49</td> </tr> <tr> <td>10</td> <td>1 122.54</td> <td>1 366.39</td> <td>1 623.43</td> <td>24 807.05</td> </tr> <tr> <td>Total</td> <td>81.08</td> <td>573.82</td> <td>673.65</td> <td>24 807.05</td> </tr> <tr> <td>q10/q1</td> <td>13.84</td> <td>5.34</td> <td>6.56</td> <td>80.35</td> </tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	255.93	247.31	308.73	2	308.79	345.62	346.03	378.75	3	378.76	410.30	410.63	442.96	4	443.03	475.71	475.25	505.77	5	506.01	538.82	539.11	573.82	6	573.82	609.74	610.86	649.87	7	650.00	691.01	694.22	743.34	8	743.57	802.66	805.56	874.84	9	874.86	978.30	983.63	1 122.49	10	1 122.54	1 366.39	1 623.43	24 807.05	Total	81.08	573.82	673.65	24 807.05	q10/q1	13.84	5.34	6.56	80.35	<p>Median expenditures in Decile 10 is 5.34 larger than that in Decile 1; Mean expenditures in Decile 10 is 6.56 larger than that in Decile 1.</p> <p>Gini coeff = 29.73</p>
Decile	Minimum	Median	Mean	Maximum																																																																
1	81.08	255.93	247.31	308.73																																																																
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q10/q1	13.84	5.34	6.56	80.35																																																																

### Housing Privileges. Monetization Scenario 2: Income Test: Benefits

#	Step	Scenario	Comments																																																																	
1	Select an in-kind benefit	Housing benefits Ex1_1 and Ex3_2 are selected																																																																		
2	Abolish in-kind subsidies for all	Benchmark scenario																																																																		
3	Recalculate expenditures without the selected benefits	<p>Table: Total monthly expenditures per equivalent unit, (net of Ex1_1 and Ex3_2 UAH)</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>81.08</td> <td>259.08</td> <td>249.40</td> <td>308.73</td> </tr> <tr> <td>2</td> <td>276.67</td> <td>345.77</td> <td>345.14</td> <td>378.75</td> </tr> <tr> <td>3</td> <td>323.30</td> <td>410.36</td> <td>410.21</td> <td>442.96</td> </tr> <tr> <td>4</td> <td>409.45</td> <td>474.01</td> <td>473.79</td> <td>505.77</td> </tr> <tr> <td>5</td> <td>473.18</td> <td>537.28</td> <td>538.39</td> <td>573.82</td> </tr> <tr> <td>6</td> <td>534.74</td> <td>608.45</td> <td>609.01</td> <td>649.87</td> </tr> <tr> <td>7</td> <td>592.38</td> <td>691.92</td> <td>693.75</td> <td>743.34</td> </tr> <tr> <td>8</td> <td>693.17</td> <td>801.29</td> <td>804.59</td> <td>874.84</td> </tr> <tr> <td>9</td> <td>845.42</td> <td>976.09</td> <td>982.79</td> <td>1 122.49</td> </tr> <tr> <td>10</td> <td>1 108.95</td> <td>1 377.27</td> <td>1 630.28</td> <td>24 807.05</td> </tr> <tr> <td>Total</td> <td>81.08</td> <td>593.50</td> <td>702.18</td> <td>24 807.05</td> </tr> <tr> <td>q10/q1</td> <td>13.68</td> <td>5.32</td> <td>6.54</td> <td>80.35</td> </tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	259.08	249.40	308.73	2	276.67	345.77	345.14	378.75	3	323.30	410.36	410.21	442.96	4	409.45	474.01	473.79	505.77	5	473.18	537.28	538.39	573.82	6	534.74	608.45	609.01	649.87	7	592.38	691.92	693.75	743.34	8	693.17	801.29	804.59	874.84	9	845.42	976.09	982.79	1 122.49	10	1 108.95	1 377.27	1 630.28	24 807.05	Total	81.08	593.50	702.18	24 807.05	q10/q1	13.68	5.32	6.54	80.35	
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q10/q1	13.68	5.32	6.54	80.35																																																																
4	Calculate the total amount of the abolished privilege	Ex1_1 and Ex3_2 total annual: 197 090 588UAH																																																																		
5	Decide how you want to redistribute this amount in cash and calculate the size of cash handouts	<p>We assume that each with monthly expenditures less than 930 UAH per equivalent unit will be granted cash:</p> <p>Those 12.737 mln people that are represented by 10.2mln of equivalent units receive additional UAH 25.7mln or UAH 2.52 per unit per year.</p>	Income test used: double subsistence level in 2006=465*2=930 UAH																																																																	

6	Add cash, as assumed and calculated in Step 10, to total expenditures and recalculate the deciles	Table: Total monthly expenditures per equivalent unit, after redistribution of Ex1_1 and Ex3_2 to poorer hhs				Gini coeff = 29.72	
		Decile	Minimum	Median	Mean		Maximum
		1	81.29	256.14	247.73		308.94
		2	309.00	345.83	346.25		378.96
		3	378.97	410.57	410.86		442.96
		4	443.03	475.62	475.20		505.77
		5	506.01	538.56	539.11		573.82
		6	573.82	609.74	610.80		649.87
		7	650.00	691.46	694.23		743.34
		8	743.57	802.66	805.47		874.84
		9	874.86	978.14	983.55		1 122.49
10	1 108.95	1 369.17	1 628.19	24 807.05			
Total	81.29	594.60	702.86	24 807.05			
q10/q1	13.64	5.35	6.57	80.30			

### Housing Privileges. Monetization Scenario 3: Income Test: Privileges.

#	Step	Scenario	Comments																																																																	
1	Select an in-kind benefit	Housing privileges Ex2_1,Ex4_2,Ex2_2, Ex5_2 are selected																																																																		
2	We abolish privileges for all	Benchmark scenario																																																																		
3	Recalculate expenditures without the selected privilege and derive new deciles for the population in the case this privilege is abolished for all	<p>Table: Total monthly expenditures per equivalent unit,</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>81.08</td> <td>257.17</td> <td>247.56</td> <td>308.57</td> </tr> <tr> <td>2</td> <td>253.00</td> <td>342.31</td> <td>342.07</td> <td>378.75</td> </tr> <tr> <td>3</td> <td>291.89</td> <td>406.09</td> <td>405.97</td> <td>442.96</td> </tr> <tr> <td>4</td> <td>330.04</td> <td>470.35</td> <td>469.24</td> <td>505.77</td> </tr> <tr> <td>5</td> <td>380.68</td> <td>534.76</td> <td>533.94</td> <td>573.79</td> </tr> <tr> <td>6</td> <td>429.13</td> <td>604.19</td> <td>603.94</td> <td>649.87</td> </tr> <tr> <td>7</td> <td>577.49</td> <td>686.20</td> <td>688.06</td> <td>743.34</td> </tr> <tr> <td>8</td> <td>639.35</td> <td>796.59</td> <td>799.13</td> <td>874.84</td> </tr> <tr> <td>9</td> <td>772.77</td> <td>973.58</td> <td>977.07</td> <td>1 122.49</td> </tr> <tr> <td>10</td> <td>1 013.91</td> <td>1 372.69</td> <td>1 624.69</td> <td>24 775.52</td> </tr> <tr> <td>Total</td> <td>81.08</td> <td>589.79</td> <td>697.51</td> <td>24 775.52</td> </tr> <tr> <td>q10/q1</td> <td>12.51</td> <td>5.34</td> <td>6.56</td> <td>80.29</td> </tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	257.17	247.56	308.57	2	253.00	342.31	342.07	378.75	3	291.89	406.09	405.97	442.96	4	330.04	470.35	469.24	505.77	5	380.68	534.76	533.94	573.79	6	429.13	604.19	603.94	649.87	7	577.49	686.20	688.06	743.34	8	639.35	796.59	799.13	874.84	9	772.77	973.58	977.07	1 122.49	10	1 013.91	1 372.69	1 624.69	24 775.52	Total	81.08	589.79	697.51	24 775.52	q10/q1	12.51	5.34	6.56	80.29	
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q10/q1	12.51	5.34	6.56	80.29																																																																
4	Calculate the total amount of the abolished privilege	Ex2_1,Ex4_2,Ex2_2, Ex5_2 total annual: 1 766 598 187 UAH																																																																		
5	Decide how you want to redistribute this amount in cash and calculate the size of cash handouts	<p>We assume that each household with monthly expenditures less than 430 UAH per equivalent unit will be granted cash:</p> <p>Those 12.737 mln people that are represented by 10.2mln of equivalent units with monthly expenditures less than UAH 430 per unit receive additional UAH 396 mln or UAH 38.88 per unit per year.</p>	Income test used: double subsistence level in 2006=465*2=930 UAH																																																																	

6	Add cash, as assumed and calculated in Step 10, to total expenditures and recalculate the deciles	Table: Total monthly expenditures per equivalent unit, after redistribution of Ex2_1,Ex4_2,Ex2_2, Ex5_2 to poorer hhs				Gini coeff = 29.53	
		Decile	Minimum	Median	Mean		Maximum
		1	84.32	259.17	250.76		311.97
		2	312.04	348.87	349.28		381.99
		3	382.00	413.60	413.30		442.96
		4	443.03	475.62	475.20		505.77
		5	506.01	538.56	539.11		573.82
		6	573.82	609.74	610.80		649.87
		7	650.00	691.46	694.23		743.34
		8	743.57	802.66	805.47		874.84
		9	800.62	976.00	980.63		1 122.49
		10	1 013.91	1 363.24	1 622.95		24 775.52
Total	84.32	594.60	702.55	24 775.52			
q10/q1	12.02	5.26	6.47	79.42			

### Housing Privileges. Monetization Scenario 4: Price subsidies elimination.

Concept: Use of HBS data in order to calculate the effect of price subsidies elimination with subsequent compensations to the most vulnerable groups

#	Step	Scenario	Comments																																																																	
1	Select an in-kind benefit or privilege (one or more) to be monetized and calculate amount of this benefit per unit of analysis	Expenditures on electricity, natural gas, liquid and solid fuel, heating and hot water ( <b>H045</b> ) are selected for elimination of price subsidies. Housing privileges Ex2_1,Ex4_2,Ex2_2, Ex5_2 and Housing benefits (Ex1_1 and Ex3_2) are selected for correction																																																																		
2	Identify 'rich' households to be deprived of privilege	All population is deprived of price subsidies as prices for energy related housing services are increased up to the market level.																																																																		
3	Identify the sum of additional expenditures caused by elimination of price subsidies.	New price level for expenditures of interest is set equal to prices for industry according to the data provided in Grey Box 1. Thus additional expenditures will equal sum of (h04511*0.67),(h04521*1.19), (h04551*0.24) taken per unit per month.	Price elasticity at this stage is taken as zero																																																																	
4	Recalculate expenditures without price subsidies	<p>Table: Total monthly expenditures per equivalent unit, after energy price increase</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>73.52</td> <td>242.72</td> <td>234.35</td> <td>307.41</td> </tr> <tr> <td>2</td> <td>223.16</td> <td>331.67</td> <td>329.96</td> <td>376.79</td> </tr> <tr> <td>3</td> <td>250.68</td> <td>392.12</td> <td>391.81</td> <td>438.54</td> </tr> <tr> <td>4</td> <td>326.32</td> <td>456.52</td> <td>455.17</td> <td>503.80</td> </tr> <tr> <td>5</td> <td>414.47</td> <td>520.13</td> <td>519.24</td> <td>571.83</td> </tr> <tr> <td>6</td> <td>481.27</td> <td>589.56</td> <td>589.25</td> <td>645.61</td> </tr> <tr> <td>7</td> <td>536.55</td> <td>670.84</td> <td>672.36</td> <td>736.85</td> </tr> <tr> <td>8</td> <td>650.03</td> <td>779.54</td> <td>782.98</td> <td>871.49</td> </tr> <tr> <td>9</td> <td>758.13</td> <td>954.85</td> <td>959.59</td> <td>1 111.01</td> </tr> <tr> <td>10</td> <td>1 055.69</td> <td>1 341.77</td> <td>1 597.86</td> <td>24 779.27</td> </tr> <tr> <td>Total</td> <td>73.52</td> <td>551.82</td> <td>653.30</td> <td>24 779.27</td> </tr> <tr> <td>q10/q1</td> <td>14.36</td> <td>5.53</td> <td>6.82</td> <td>80.61</td> </tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	73.52	242.72	234.35	307.41	2	223.16	331.67	329.96	376.79	3	250.68	392.12	391.81	438.54	4	326.32	456.52	455.17	503.80	5	414.47	520.13	519.24	571.83	6	481.27	589.56	589.25	645.61	7	536.55	670.84	672.36	736.85	8	650.03	779.54	782.98	871.49	9	758.13	954.85	959.59	1 111.01	10	1 055.69	1 341.77	1 597.86	24 779.27	Total	73.52	551.82	653.30	24 779.27	q10/q1	14.36	5.53	6.82	80.61	
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5	Calculate the total amount of the abolished privilege	Total additional spending of households: UAH 762 896 881. Out of this sum of money UAH 246 348 558 to be distributed back to hhs.																																																																		
6	Identify households to be compensated for the price increase	Those below the poverty line (430 UAH expenditures per unit per month in 2006) are given fixed sum of money to compensate for the price increase according to the consumption norms. Compensation equals UAH 19.50 per month for the household head and UAH 11.72 for other hh members according to the calculations given in Grey Box 2. Those having greater expenditures, but receiving housing privileges are also compensated the price increase proportionally to the privileges they were receiving before, as this scenario does not assume privileges elimination. I.e. for those receiving housing privileges they will increase by the sum of $(ex4\_2\_4 * 1.19)$ , $(ex4\_2\_5 * 0.24)$ , $(ex4\_2\_6 * 0.24)$ and $(ex5\_2 * 0.67)$	The sum of compensation does not depend on the sum of money received from price increase, but solely on the sum of additional expenditures.																																																																	
7	Add cash, as assumed and calculated in Step 10, to total expenditures and recalculate the deciles	<p>Table: Total monthly expenditures per equivalent unit, after compensation of the price increase</p> <table border="1" data-bbox="763 895 1491 1347"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr><td>1</td><td>91.15</td><td>260.50</td><td>252.10</td><td>325.78</td></tr> <tr><td>2</td><td>242.66</td><td>349.62</td><td>347.81</td><td>395.15</td></tr> <tr><td>3</td><td>270.18</td><td>407.62</td><td>406.84</td><td>524.41</td></tr> <tr><td>4</td><td>326.32</td><td>459.08</td><td>457.38</td><td>552.21</td></tr> <tr><td>5</td><td>414.47</td><td>521.77</td><td>521.22</td><td>659.85</td></tr> <tr><td>6</td><td>481.27</td><td>591.98</td><td>591.50</td><td>687.93</td></tr> <tr><td>7</td><td>536.55</td><td>672.42</td><td>674.91</td><td>807.03</td></tr> <tr><td>8</td><td>650.03</td><td>783.64</td><td>785.27</td><td>881.99</td></tr> <tr><td>9</td><td>758.13</td><td>957.76</td><td>962.07</td><td>1 130.52</td></tr> <tr><td>10</td><td>1 055.69</td><td>1 343.81</td><td>1 599.94</td><td>24 787.26</td></tr> <tr><td>Total</td><td>91.15</td><td>555.13</td><td>659.95</td><td>24 787.26</td></tr> <tr><td>d10/d1</td><td>11.58</td><td>5.16</td><td>6.35</td><td>76.09</td></tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	91.15	260.50	252.10	325.78	2	242.66	349.62	347.81	395.15	3	270.18	407.62	406.84	524.41	4	326.32	459.08	457.38	552.21	5	414.47	521.77	521.22	659.85	6	481.27	591.98	591.50	687.93	7	536.55	672.42	674.91	807.03	8	650.03	783.64	785.27	881.99	9	758.13	957.76	962.07	1 130.52	10	1 055.69	1 343.81	1 599.94	24 787.26	Total	91.15	555.13	659.95	24 787.26	d10/d1	11.58	5.16	6.35	76.09	Gini coeff = 29.60
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## APPENDIX C. TRANSPORTATION PRIVILEGES.

### Transportation privileges. Initial stance.

#	Step	Scenario	Comments																																																																	
1	Select impact	Effect on poverty and inequality of monetization and redistribution of transportation privileges																																																																		
2	Select data	Ukraine HBS 2006 annual																																																																		
3	Select unit of analysis	One person	Equivalent units (1- household head and 0.7 – other hh members) used for deriving deciles																																																																	
4	Use person weights to translate sample data into total population	Sample = 10 499 households and 26 253 persons Population = 17 417 477 households and 45 359 944 persons																																																																		
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7	We abolish the privilege for all	Benchmark scenario																																																																		

8	Recalculate expenditures without the selected privilege and derive new deciles for the population in the case this privilege is abolished for all	<p>Table: Total monthly expenditures per equivalent unit, (net of e10_2 UAH)</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>81.08</td> <td>255.31</td> <td>246.87</td> <td>307.84</td> </tr> <tr> <td>2</td> <td>308.07</td> <td>345.04</td> <td>345.16</td> <td>378.45</td> </tr> <tr> <td>3</td> <td>378.51</td> <td>409.32</td> <td>409.70</td> <td>442.27</td> </tr> <tr> <td>4</td> <td>442.32</td> <td>474.79</td> <td>474.41</td> <td>504.68</td> </tr> <tr> <td>5</td> <td>504.78</td> <td>536.91</td> <td>537.68</td> <td>572.19</td> </tr> <tr> <td>6</td> <td>572.27</td> <td>608.48</td> <td>609.42</td> <td>648.73</td> </tr> <tr> <td>7</td> <td>648.89</td> <td>690.23</td> <td>692.93</td> <td>741.70</td> </tr> <tr> <td>8</td> <td>741.74</td> <td>800.22</td> <td>803.90</td> <td>872.14</td> </tr> <tr> <td>9</td> <td>872.24</td> <td>976.07</td> <td>981.57</td> <td>1 119.45</td> </tr> <tr> <td>10</td> <td>1 120.37</td> <td>1 365.45</td> <td>1 621.05</td> <td>24 807.05</td> </tr> <tr> <td>Total</td> <td>81.08</td> <td>572.27</td> <td>672.33</td> <td>24 807.05</td> </tr> <tr> <td>q10/q1</td> <td>13.82</td> <td>5.35</td> <td>6.57</td> <td>80.58</td> </tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	255.31	246.87	307.84	2	308.07	345.04	345.16	378.45	3	378.51	409.32	409.70	442.27	4	442.32	474.79	474.41	504.68	5	504.78	536.91	537.68	572.19	6	572.27	608.48	609.42	648.73	7	648.89	690.23	692.93	741.70	8	741.74	800.22	803.90	872.14	9	872.24	976.07	981.57	1 119.45	10	1 120.37	1 365.45	1 621.05	24 807.05	Total	81.08	572.27	672.33	24 807.05	q10/q1	13.82	5.35	6.57	80.58	<p>After the abolishment of e10_2 privileges Gini coefficient increased by 0.01 percentage points</p> <p>Gini coeff = 29.74</p>
Decile	Minimum	Median	Mean	Maximum																																																																
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9	Calculate the total amount of the abolished privilege	e10_2 total annual for all households: 608 753 828 UAH																																																																		

## Transportation privileges. Monetization Scenario 2: Income Test

Concept: Use of HBS data in order to calculate the effect of a hypothetical monetization of an in-kind transportation privilege

#	Step	Scenario	Comments																																																																	
1	Decide how you want to redistribute this amount in cash and calculate the size of cash handouts	<p>We assume that each household receiving transportation privilege with monthly expenditures less than 684 UAH per equivalent unit will be granted cash:</p> <p>Total monthly amount of cash benefit: 608 753 828 UAH /12 months = 50 729 486 UAH</p> <p>Number of recipients (number of households receiving transportation privilege with monthly expenditures less than 684 UAH per equivalent unit) = 2 610 688 households</p> <p>Cash handout per household per month: 50 729 486/ 2 610 688 = 19.4 UAH</p>	<p>Income test used: official income test introduced in legislation in 2008 (890 UAH of monthly income per family member, taking into account the precedent 6 months) deflated by cumulative CPI of 2006 and 2007 (30%): <math>890/1.3=684</math> UAH</p>																																																																	
2	Add cash, as assumed and calculated in Step 10, to total expenditures and recalculate the deciles	<p>Table: Total monthly expenditures per equivalent unit, after redistribution of e10_2, UAH</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>81.08</td> <td>258.44</td> <td>249.82</td> <td>309.62</td> </tr> <tr> <td>2</td> <td>309.65</td> <td>346.94</td> <td>346.81</td> <td>380.44</td> </tr> <tr> <td>3</td> <td>380.49</td> <td>412.24</td> <td>412.55</td> <td>444.68</td> </tr> <tr> <td>4</td> <td>444.75</td> <td>476.64</td> <td>476.10</td> <td>506.38</td> </tr> <tr> <td>5</td> <td>506.44</td> <td>540.50</td> <td>540.40</td> <td>575.56</td> </tr> <tr> <td>6</td> <td>575.59</td> <td>611.15</td> <td>612.08</td> <td>651.52</td> </tr> <tr> <td>7</td> <td>651.55</td> <td>691.30</td> <td>693.92</td> <td>741.70</td> </tr> <tr> <td>8</td> <td>741.74</td> <td>800.22</td> <td>803.90</td> <td>872.14</td> </tr> <tr> <td>9</td> <td>872.24</td> <td>976.07</td> <td>981.57</td> <td>1 119.45</td> </tr> <tr> <td>10</td> <td>1 120.37</td> <td>1 365.45</td> <td>1 621.05</td> <td>24 807.05</td> </tr> <tr> <td>Total</td> <td>81.08</td> <td>575.56</td> <td>673.63</td> <td>24 807.05</td> </tr> <tr> <td>q10/q1</td> <td>13.82</td> <td>5.28</td> <td>6.49</td> <td>80.12</td> </tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	258.44	249.82	309.62	2	309.65	346.94	346.81	380.44	3	380.49	412.24	412.55	444.68	4	444.75	476.64	476.10	506.38	5	506.44	540.50	540.40	575.56	6	575.59	611.15	612.08	651.52	7	651.55	691.30	693.92	741.70	8	741.74	800.22	803.90	872.14	9	872.24	976.07	981.57	1 119.45	10	1 120.37	1 365.45	1 621.05	24 807.05	Total	81.08	575.56	673.63	24 807.05	q10/q1	13.82	5.28	6.49	80.12	<p>Cumulative decrease of Gini coeff = 0.1 percentage point</p> <p>Gini coeff = 29.63</p> <p>Poverty rate = 27.91%</p>
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**Transportation privileges. Monetization Scenario 3: ‘Feasible group’.**

Concept: Use of HBS data in order to calculate the effect of a hypothetical monetization of an in-kind transportation privilege

#	Step	Scenario	Comments																																																																	
1	Decide how you want to redistribute this amount in cash and calculate the size of cash handouts	<p>We assume that each pension recipient (all kinds of pensions included: retirement, invalid, for long service, and social) with annual pension lower than 4500 UAH will be granted cash:</p> <p>Number of recipients = 5 219 457 individuals</p> <p>Cash handout per person per year: <math>608\,753\,828 / 5\,219\,457 = 116</math> UAH</p>																																																																		
2	Add cash, as assumed and calculated in Step 10, to total expenditures and recalculate the deciles	<p>Table: Total monthly expenditures per equivalent unit, after redistribution of e10_2, UAH</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr><td>1</td><td>81.08</td><td>256.67</td><td>248.26</td><td>308.89</td></tr> <tr><td>2</td><td>309.27</td><td>345.92</td><td>346.58</td><td>380.10</td></tr> <tr><td>3</td><td>380.10</td><td>411.26</td><td>411.25</td><td>443.79</td></tr> <tr><td>4</td><td>443.81</td><td>476.64</td><td>475.93</td><td>506.85</td></tr> <tr><td>5</td><td>506.92</td><td>538.43</td><td>539.22</td><td>574.26</td></tr> <tr><td>6</td><td>574.31</td><td>610.07</td><td>610.92</td><td>649.78</td></tr> <tr><td>7</td><td>649.81</td><td>691.92</td><td>694.39</td><td>743.67</td></tr> <tr><td>8</td><td>743.79</td><td>800.50</td><td>805.03</td><td>874.35</td></tr> <tr><td>9</td><td>874.45</td><td>976.87</td><td>982.79</td><td>1 121.30</td></tr> <tr><td>10</td><td>1 121.62</td><td>1 367.83</td><td>1 622.62</td><td>24 807.05</td></tr> <tr><td>Total</td><td>81.08</td><td>574.31</td><td>673.69</td><td>24 807.05</td></tr> <tr><td>q10/q1</td><td>13.83</td><td>5.34</td><td>6.54</td><td>80.31</td></tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	256.67	248.26	308.89	2	309.27	345.92	346.58	380.10	3	380.10	411.26	411.25	443.79	4	443.81	476.64	475.93	506.85	5	506.92	538.43	539.22	574.26	6	574.31	610.07	610.92	649.78	7	649.81	691.92	694.39	743.67	8	743.79	800.50	805.03	874.35	9	874.45	976.87	982.79	1 121.30	10	1 121.62	1 367.83	1 622.62	24 807.05	Total	81.08	574.31	673.69	24 807.05	q10/q1	13.83	5.34	6.54	80.31	<p>From the initial stance Gini coeff decreased by 0.06 percentage points</p> <p>Gini coeff = 29.67</p> <p>Poverty rate = 28.01%</p>
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## APPENDIX D. SANATORIUM PRIVILEGES.

### Sanatorium privileges. Initial stance.

#	Step	Scenario	Comments																																																																	
1	Select impact	Effect on poverty of monetization and redistribution of sanatorium privileges																																																																		
2	Select data	Ukraine HBS 2006 annual																																																																		
3	Select unit of analysis	One person	Equivalent units (1- household head and 0.7 – other hh members) used for deriving deciles																																																																	
4	Use person weights to translate sample data into total population	Sample = 26 253 persons and 10 499 households Population = 45 359 944 persons and 17 417 477 households																																																																		
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6	Select an in-kind benefit	ex6, ex7, ex8 - sanatorium and health resort privilege is selected																																																																		
7	We abolish privileges for all	Benchmark scenario																																																																		
8	Recalculate expenditures without the selected privilege and derive new deciles for the population in the case this privilege is abolished for all	<p>Table: Total monthly expenditures per equivalent unit, (net of ex6, ex7, ex8 UAH)</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr> <td>1</td> <td>81.08</td> <td>255.84</td> <td>247.09</td> <td>308.20</td> </tr> <tr> <td>2</td> <td>308.22</td> <td>345.52</td> <td>345.60</td> <td>378.51</td> </tr> <tr> <td>3</td> <td>378.53</td> <td>409.59</td> <td>409.79</td> <td>442.32</td> </tr> <tr> <td>4</td> <td>442.33</td> <td>474.65</td> <td>473.97</td> <td>504.01</td> </tr> <tr> <td>5</td> <td>504.02</td> <td>536.96</td> <td>537.69</td> <td>572.83</td> </tr> <tr> <td>6</td> <td>572.84</td> <td>608.19</td> <td>608.95</td> <td>647.90</td> </tr> <tr> <td>7</td> <td>647.93</td> <td>689.11</td> <td>692.17</td> <td>742.09</td> </tr> <tr> <td>8</td> <td>742.43</td> <td>800.78</td> <td>803.75</td> <td>872.32</td> </tr> <tr> <td>9</td> <td>872.47</td> <td>974.08</td> <td>978.74</td> <td>1 118.15</td> </tr> <tr> <td>10</td> <td>1 118.22</td> <td>1 363.76</td> <td>1 616.31</td> <td>24 807.05</td> </tr> <tr> <td>Total</td> <td>81.08</td> <td>572.84</td> <td>671.40</td> <td>24 807.05</td> </tr> <tr> <td>q10/q1</td> <td>13.79</td> <td>5.33</td> <td>6.54</td> <td>80.49</td> </tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	255.84	247.09	308.20	2	308.22	345.52	345.60	378.51	3	378.53	409.59	409.79	442.32	4	442.33	474.65	473.97	504.01	5	504.02	536.96	537.69	572.83	6	572.84	608.19	608.95	647.90	7	647.93	689.11	692.17	742.09	8	742.43	800.78	803.75	872.32	9	872.47	974.08	978.74	1 118.15	10	1 118.22	1 363.76	1 616.31	24 807.05	Total	81.08	572.84	671.40	24 807.05	q10/q1	13.79	5.33	6.54	80.49	Gini coeff = 29.66
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9	Calculate the total amount of the abolished privilege	ex6, ex7, ex8 total annual: 994 535 438 UAH																																																																		

### Sanatorium privileges. Monetization Scenario 2: Income Test

Concept: Use of HBS data in order to calculate the effect of a hypothetical monetization of an in-kind sanatorium privilege

#	Step	Scenario	Comments																																																																	
1	Decide how you want to redistribute this amount in cash and calculate the size of cash handouts	<p>We assume that each household receiving sanatorium privilege with monthly expenditures less than 930 UAH per equivalent unit will be granted cash:</p> <p>Number of recipients = 254 396 households</p> <p>Cash handout per hh per year = 3909 UAH</p>	Income test used: double subsistence level in 2006=465*2=930 UAH																																																																	
2	Add cash, as assumed and calculated in Step 10, to total expenditures and recalculate the deciles	<p>Table: Total monthly expenditures per equivalent unit, after redistribution of ex6,ex7,ex8 to poorer hhs</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr><td>1</td><td>81.08</td><td>255.93</td><td>247.37</td><td>309.30</td></tr> <tr><td>2</td><td>309.34</td><td>345.72</td><td>346.48</td><td>379.81</td></tr> <tr><td>3</td><td>379.85</td><td>410.93</td><td>411.39</td><td>445.22</td></tr> <tr><td>4</td><td>445.28</td><td>476.90</td><td>476.51</td><td>507.19</td></tr> <tr><td>5</td><td>507.22</td><td>540.54</td><td>540.46</td><td>575.39</td></tr> <tr><td>6</td><td>575.42</td><td>611.45</td><td>612.21</td><td>651.55</td></tr> <tr><td>7</td><td>651.68</td><td>693.15</td><td>696.41</td><td>745.64</td></tr> <tr><td>8</td><td>745.64</td><td>805.54</td><td>807.68</td><td>876.17</td></tr> <tr><td>9</td><td>876.82</td><td>976.07</td><td>981.84</td><td>1 118.15</td></tr> <tr><td>10</td><td>1 118.22</td><td>1 363.76</td><td>1 616.01</td><td>24 807.05</td></tr> <tr><td>Total</td><td>81.08</td><td>575.42</td><td>673.66</td><td>24 807.05</td></tr> <tr><td>q10/q1</td><td>13.79</td><td>5.33</td><td>6.53</td><td>80.20</td></tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	255.93	247.37	309.30	2	309.34	345.72	346.48	379.81	3	379.85	410.93	411.39	445.22	4	445.28	476.90	476.51	507.19	5	507.22	540.54	540.46	575.39	6	575.42	611.45	612.21	651.55	7	651.68	693.15	696.41	745.64	8	745.64	805.54	807.68	876.17	9	876.82	976.07	981.84	1 118.15	10	1 118.22	1 363.76	1 616.01	24 807.05	Total	81.08	575.42	673.66	24 807.05	q10/q1	13.79	5.33	6.53	80.20	<p>Gini coeff = 29.61</p> <p>Poverty rate = 27.95%</p>
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**Sanatorium privileges. Monetization Scenario 3: ‘Feasible group’.**

Concept: Use of HBS data in order to calculate the effect of a hypothetical monetization of an in-kind sanatorium privilege

#	Step	Scenario	Comments																																																																	
1	Decide how you want to redistribute this amount in cash and calculate the size of cash handouts	<p>We assume that each ‘disadvantaged’ household receiving social assistance for poverty-stricken families will be granted additional social payments:</p> <p>Number of recipients = 360 436 households</p> <p>Cash handout per hh per year = 2 759 UAH</p>																																																																		
2	Add cash, as assumed and calculated in Step 10, to total expenditures and recalculate the deciles	<p>Table: Total monthly expenditures per equivalent unit, after redistribution of ex6,ex7,ex8 to poverty-stricken households</p> <table border="1"> <thead> <tr> <th>Decile</th> <th>Minimum</th> <th>Median</th> <th>Mean</th> <th>Maximum</th> </tr> </thead> <tbody> <tr><td>1</td><td>81.08</td><td>261.13</td><td>252.02</td><td>313.44</td></tr> <tr><td>2</td><td>313.72</td><td>350.23</td><td>350.24</td><td>382.49</td></tr> <tr><td>3</td><td>382.52</td><td>413.83</td><td>414.14</td><td>447.58</td></tr> <tr><td>4</td><td>447.60</td><td>477.75</td><td>477.12</td><td>506.78</td></tr> <tr><td>5</td><td>506.92</td><td>540.03</td><td>539.84</td><td>574.13</td></tr> <tr><td>6</td><td>574.20</td><td>609.64</td><td>610.39</td><td>649.10</td></tr> <tr><td>7</td><td>649.33</td><td>689.84</td><td>693.29</td><td>743.32</td></tr> <tr><td>8</td><td>743.34</td><td>802.84</td><td>804.78</td><td>872.90</td></tr> <tr><td>9</td><td>872.93</td><td>974.74</td><td>979.29</td><td>1 118.15</td></tr> <tr><td>10</td><td>1 118.22</td><td>1 363.76</td><td>1 616.78</td><td>24 807.05</td></tr> <tr><td>Total</td><td>81.08</td><td>574.13</td><td>673.75</td><td>24 807.05</td></tr> <tr><td>q10/q1</td><td>13.79</td><td>5.22</td><td>6.42</td><td>79.14</td></tr> </tbody> </table>	Decile	Minimum	Median	Mean	Maximum	1	81.08	261.13	252.02	313.44	2	313.72	350.23	350.24	382.49	3	382.52	413.83	414.14	447.58	4	447.60	477.75	477.12	506.78	5	506.92	540.03	539.84	574.13	6	574.20	609.64	610.39	649.10	7	649.33	689.84	693.29	743.32	8	743.34	802.84	804.78	872.90	9	872.93	974.74	979.29	1 118.15	10	1 118.22	1 363.76	1 616.78	24 807.05	Total	81.08	574.13	673.75	24 807.05	q10/q1	13.79	5.22	6.42	79.14	<p>Gini coeff = 29.43</p> <p>Poverty rate = 27.56%</p>
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## APPENDIX E. INSTITUTIONAL BACKGROUND

### Administrative and budget system of Ukraine

The mechanisms and schemes of social privileges and benefits are closely interrelated with budget system and administrative system of the country. Broadly speaking design of budget system and administrative structure defines efficiency of social and subsidy policy of the government. In this section we will describe institutional fundamentals the social benefits system is based on.

#### *Administrative structure*

According to Constitution of Ukraine, administration of the state is organized through institutions of central government (president, cabinet of ministers, ministers etc.) and three levels of local authorities (oblasts, rayons, cities and villages)<sup>14</sup>. There are also administrative units with special status – Autonomous Republic of Crimea, Kyiv city and Sevastopol city.

At the local level there are present both authorities representing central government and self-governance. The central government appoints its representative only on the levels of oblast and rayon (first and second level, respectively). Mayors of cities (second level) and heads of small settlements (third level) are elected by local communities. Thus we can see that the central government intervenes in administration only through first and second (partially) level of local authorities while it delegates third level of local administration to communities.

The system is highly centralized. The key financial decisions are under control of the central government representatives – head of oblast and rayon state administrations (sometimes named governors in mass-media). Head of state administration is the main manager of local public funds. Importantly, heads of oblast administration distribute funds among rayons and, in their turn, heads of rayon administration distribute their budgets to the third level.

Head of local administrations (both oblast and rayon) are appointed by the president. The candidates for the position are identified and proposed by the prime-minister. Although heads of administrations are the key players on the local level, the authority of central government representatives is balanced by self-governance institutions. We are talking about local councils which are elected by communities.

Interrelation between the local councils and heads of administrations are more or less on peer level. The council approves (or declines) budget projects (including level of tariffs), monitors budget execution and can dismiss head of administration with 2/3 of council votes. However, on the operational level head of administration makes decisions and manages issues for transfers and subventions from the central budget (about 40-50% of local spending). As a consequence, local state administration is viewed as more politically powerful institution vs. local councils.

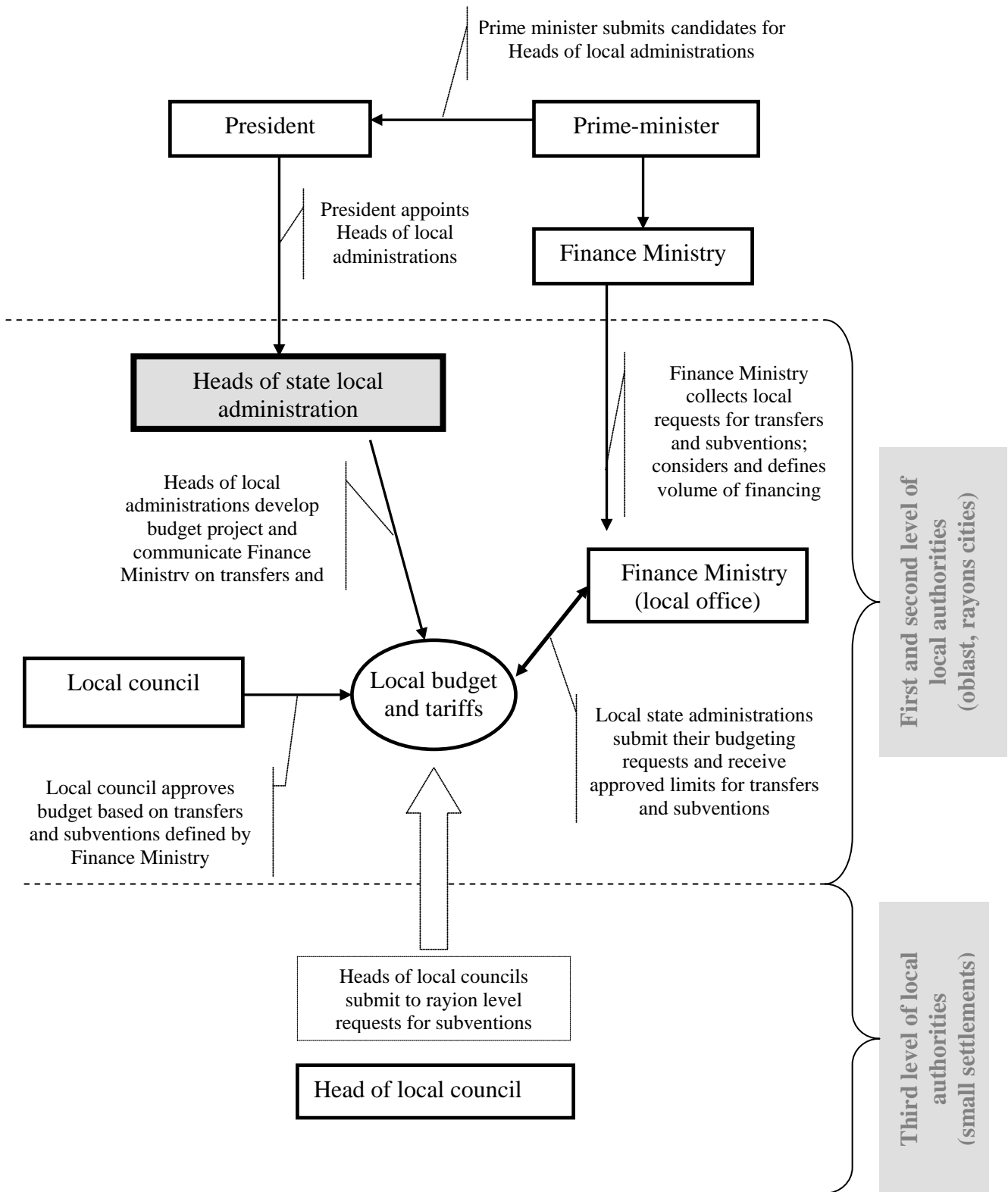
Administration of cities looks a bit different from oblast and rayon. Mayors are elected by communities and, in fact, combine two functions – represent executive power and at the same time mobilize work of local councils. Therefore, mayors concentrate main power at the cities, in addition, they have the same authorities in public funds as the heads of state administrations i.e. develop budgets, communicate Finance Ministry with respect to subventions and perform as the key manager of public funds.

On the third level public administration is equivalent to the cities', with the only difference. Heads of small settlements are financially dependant on state administrations. They do not participate in budgeting process and receive the funds, which were allocated to the third level by rayon state administration.

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<sup>14</sup> The *first* level of local authorities includes 24 oblasts, Autonomous Crimea Republic, Kyiv and Sevastopol city. The *second* level of local authorities consists of 488 rayons and 177 cities. The *third* level is 12000 of towns, urban settlements and villages.

**Figure E.1. Budget process at local level**



Source: CASE Ukraine compilation

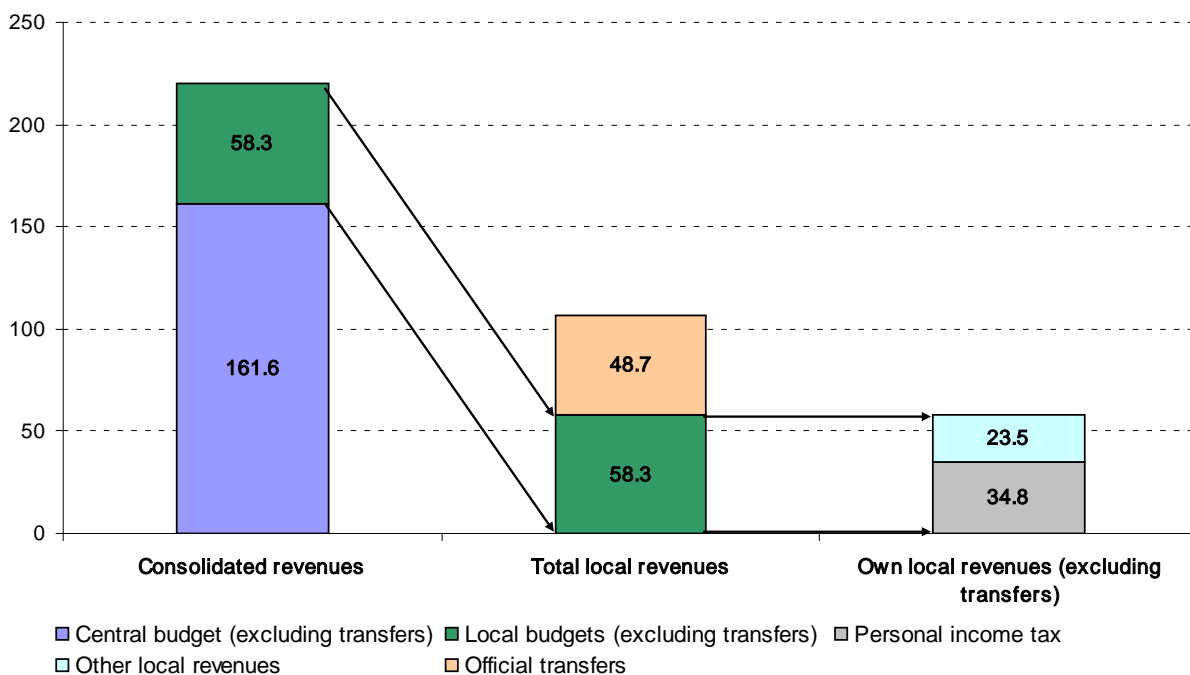
## Budget system

Similarly to administration structure the budget system is organized in a very centralized manner. According to the Budget Code of Ukraine the budget system includes central and local budgets (which comprise consolidated budget) plus special funds like Pension fund.

Almost all revenues (tax and non-tax) are collected to the central budget (almost 75% of proceeds). Local budgets collect some state taxes and fees and also have revenues from their own local taxes. The key revenues come from personal income tax (PIT), which comprises almost 60% of local collections. The tax is distributed between oblast and rayon level in proportion 75% and 25%, respectively. Important, local taxes provide very tiny incomes to the budget and in many cases do not cover the costs of its administration.

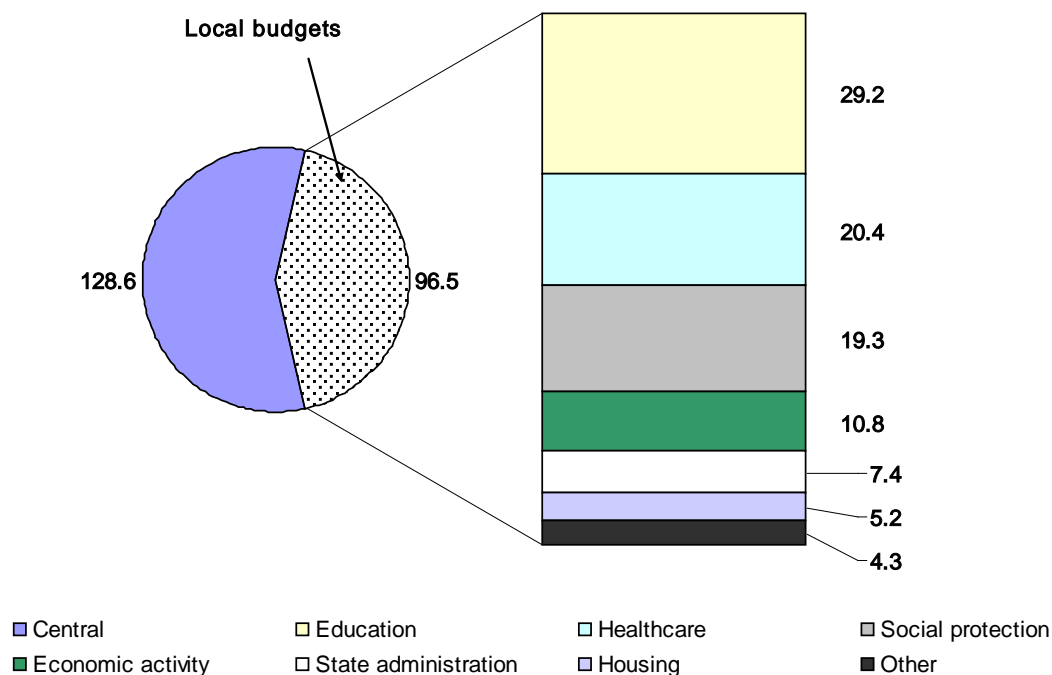
Local budgets are responsible for considerable part of consolidated spending (close to 50%). At the same time they can not generate enough resources with their own capacities (local budgets collect only 1/4 of consolidated proceeds). The fiscal gap is covered from central budget with subventions and leveling transfers. The transfers comprise more than 40% of local spending. The main volume of local outlays is allocated on healthcare system, elementary and secondary education, and social protection. Noteworthy these spending items were delegated to local level by central government.

Figure E.2. Local budget revenues, 2007, billion UAH



Source: Ministry of Finance of Ukraine

Figure E.3. Local budget expenditures, 2007, billion UAH



Source: Ministry of Finance of Ukraine

Budgeting of local spending is an important part of general picture. The process is closely related to the central budget procedures. The Finance Ministry defines framework for local budgeting requests. The local authorities consider the limitations and submit to the Ministry (local offices) their inquiries for subventions. The next iteration includes approval of the budget project by the Cabinet of Ministers (including subventions and transfers). As soon as the parliament approves the budget, local authorities are informed about volumes of subventions and leveling transfers and, consequently, are equipped to approve local spending plans.

As we see, significant part of local public funds is distributed by the central government. The distribution is rather arbitrary. It is based on the volumes of transfers from previous periods, demographic and economic parameters, official standards (*normatives*) and, to large extent, on political lobbying.

Important details are related to the types of transfers that local budgets receive from the central funds. The first one (leveling transfers) are based on the so called “formula of leveling”. The formula was expected to bring transparency and predictability to the process of funds redistribution among budgets; however, eventually the instrument absorbed huge number of coefficients, which are defined arbitrary. As a consequence, local authorities can not predict leveling transfer by themselves thus depending on decisions at the central level. At the budget 2007 the leveling transfers comprised 38.2% of total transfers from the central budget.

The second type (subventions) accounted (in 2007) for 43.8% of central budget transfers. Subventions are defined on the demand-based requests and are allocated for special purpose. The subventions are the very funds which are used for compensation of costs related to provision of privileges and social benefits. The volume of subventions depends on *normatives* and some estimates of privileges and social benefits consumers. However, no clear accounting is provided (see for more details report of Anna Nechai). Under this format, this part of transfers is strongly dependant on ‘goodwill’ of the authority which distributes the subventions (on every level of administration: central government, oblast state administration, rayon state administration).

Therefore, on the one hand local authorities are uncertain what kind of funding will be available for the next year, on the other they always have stimuli to overestimate their needs to claim as much as possible. The overestimation is possible only under non-transparent accounting principles (like “rule of thumb” standards). Naturally, local authorities have very strong interest for approximate estimations.

In the context of the budgeting process it is important that local authorities of first and second level communicate directly to the Finance Ministry – oblast, rayons and cities (692 administrative units). However, this kind of communication is mainly for informational purpose while distribution of transfers and subventions is subject to heads of local state administrations (see *Administrative structure*). The third level of local authorities does not participate in budgeting process directly.

To sum up, we can see from the section that for local authorities their prosperity depends on good relations at the center, political landscape and ability to ground reasonably a requested subvention. For communication and political support the **Head of state administration** plays the key role and, broadly speaking, this person is responsible for lobbying interests of local community during the budgeting process. On the side of inquiries to Finance Ministry, the mechanism of accounting is important. So far state institutions use *normatives* which are a rough estimate and therefore leaves possibility for fraud (overestimate of demand). It is viewed that *normatives* approach is beneficial for local authorities since it brings extra funds to their accounts.