

MANAGEMENT OF AGRARIAN PRODUCTION STRUCTURES IN THE CONDITIONS OF GLOBALIZATION PROCESSES

MANAGEMENT OF AGRARIAN PRODUCTION STRUCTURES IN THE CONDITIONS OF GLOBALIZATION PROCESSES

A monograph

edited by
Scientific and
Leading editors:

Vitalii Nitsenko
Tetiana Mostenska
Abbas Mardani



Chapter 1.2.

DEVELOPMENT OF AGRARIAN SECTOR OF ECONOMY IN THE CONDITIONS OF TRANSFORMATION OF PATTERNS OF OWNERSHIP

Andrii **Dankevich**, Vitalii **Nitsenko**, Abbas **Mardani**, Maryna **Ponomarova**

The process of land reform during the 1990-2014 triggered the transformation of property relations. In agriculture, there were created new market-oriented economic structures in terms of size and specialization, which use the land leased from farmers. At the same time, the issue of forming effective forms of farming in terms of production and investments and resolving important social and economic issues based on this is the important task of economic science.

Thus, L. Zastavnyuk and V. Zigry note that “despite a number of important institutional, economic and legal measures related to the transition to private ownership of land and its transfer to the ownership of farmers, the formation of market-oriented economic structures and achievement of certain positive developments based on this, the agriculture has long been in a critical state” (Zastavnyuk, 2011).

A. Fedoseyeva maintains the same opinion. In her study, she came to the following conclusion: “The current state of both the agro-industrial complex of Ukraine and the economy is not only a consequence of the country’s development in the past decades, but also the result of mistakes made in the reform of the agrarian sector, which resulted in a sharp decline in the economic potential of the state and the living standards of the population” (Fedoseyeva, 2009).

Analyzing the reform of the domestic agricultural sector in the organizational and economic areas, V. Mesel-Veselyak believes that currently in Ukraine there are three forms of business – private farms, farms and market-oriented agricultural enterprises. In terms of size, they correspond to those of many developed countries of the world, ensuring effective agriculture and showing the overproduction: the first – the Japanese-Chinese model, the second – the European, and the third – the US and the former Soviet Union model. Business patterns created in Ukraine meet the requirements of different businesses: large, medium and small (Mesel-Veselyak, 2010).

Large-scale agricultural enterprises are more effective forms of business compared with the medium and small ones. As noted by A. Dankevich, the concentration of capital in the agricultural production in the form of creation of integrated structures ... in accounted for periods of agrarian crisis, in which farmers experienced financial difficulties, and the land

lost its value, thus investments in the agriculture were economically sound (Dankevich, 2011).

Considering and analyzing the impact of external factors on the efficiency of agricultural production, I. Kirilenko and A. Pavlov concluded that currently, the most effective agricultural businesses are private farms and agricultural holdings (Kirilenko, 2010).

Theoretical and methodological problems of change of ownership and creation of effective organizational structures for agricultural enterprises were considered in the works of famous academic economists: P.T. Sabluk, V.P. Sitnik, V.K. Tereshchenko, V.Y. Mesel-Veselyak, N.N. Fedorov, N.Y. Demyanenko, B.I. Paskhaver et al. However, the formation of a market economy requires a further, in-depth study of new approaches to the system of production organization.

The theoretical and methodological summary of the main provisions of the business entities economic activity in the transformation of property relations and the development of proposals aimed at improving the efficiency of agricultural production.

Structural changes in the forms of land ownership during the 1990-2014 in Ukraine has led to the transfer of agricultural land from the state to the collective and private ownership. As of January 1, 2015, the state ownership share decreased to 26.2%. The collective ownership is minimized (Fig. 1).

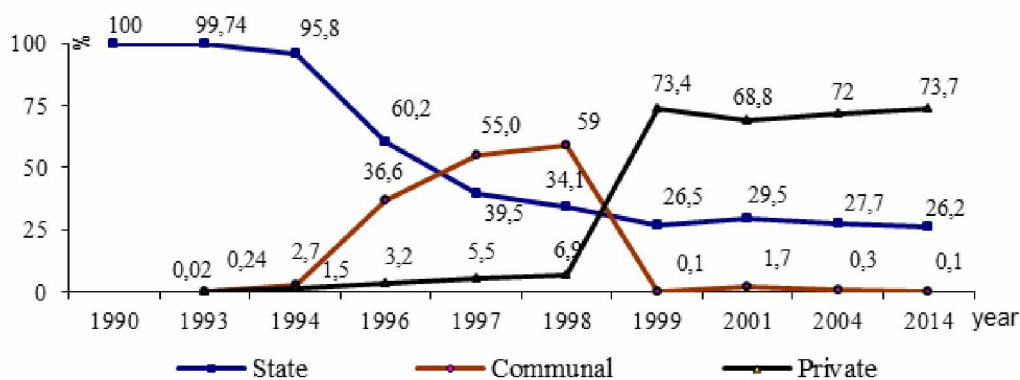


Fig. 1. Distribution of Agricultural Land in Ukraine by Ownership, 1990-2014

Source: built on the basis of Ukraine's State Statistics Committee data.

The turning point in the development of the agriculture was the decree of the President of Ukraine of December 3, 1999 "On Urgent Measures for Accelerating the Agricultural Sector Reform". This decree regulated the lease of land, simplified the procedure for registration of lease agreements, which allowed significantly accelerating the development of new agricultural businesses based on the land private ownership. In accordance with its provisions, since 2000, agricultural enterprises have been representing the leased land in the account, and the rent – in the cost of agricultural products.

As a result of the land reform, there has been created new economy market-oriented businesses based on the land lease. During 2001-2014, the number of businesses in the agricultural sector has increased by almost 22 thousand companies, mainly through the creation of 14 thousand new farms. The land use is dominated by business companies, the sha-

re of which is 49%, and farms, which during this time have managed to extend their land tenure almost 3 times. A significant drop should include the negative dynamics among cooperatives, which have decreased by almost 3 times, and by 6 times for the area (Table 1).

Table 1. Dynamics of Agricultural Enterprises Land Use (April 1, 2001 – January 1, 2014)

Agricultural company forms	Qty.			Land area, thous. ha		
	as of April 1, 2001	as of January 1, 2014	+, -	as of April 1, 2001	as of January 1, 2014	+, -
Business companies	6,641	8,806	2,165	11,222	9,010	-2,212
Private (private-lease) enterprises	3,277	5,690	2,413	4,208	3,198	-1,010
Joint-stock companies	770	677	-93	1650	814	-836
Cooperatives	2845	819	-2026	4999	805	-4193
Farms	1767	15499	13732	907	3000	2093
Other types of agricultural businesses	905	6472	5567	1003	1667	664
Overall	16205	37963	21758	23987	18493	-5495

Source: estimated by the authors according to the State Service of Ukraine for Surveying, Mapping and Cadaster.

Since 2000, the land-lease relations have taken a dominant position in agricultural production, and the rent became an additional lever of social support in the countryside. More than 5.2 million farmers exercise their right to land through leasing arrangements. Proprietors have lost confidence in the businesses where they received land shares and enter into lease agreements with other actors (agricultural holdings) and farms, whose share increased by 41% and 14% in the general structure of agreements, respectively (Table 2).

The size, type and timing of rent payments are set with the consent of the parties and displayed in the agreement. The calculation of the rent is based on inflation indices, unless otherwise stipulated by the lease agreement. The state regulates its lower limit, which is on private lands should not be less than 3% of the land monetary value. The rents can be in cash, kind and time (providing services to the proprietor) forms. Total payments under lease agreements in 2014 reached UAH 11.3 billion, and the average amount of rent for the year was UAH 663 or about \$40 per 1 hectare.

In the lease agreements structure, the share of long-term lease for a period of more than 6 years has increased up to 61%. The short-term lease for up to three years has almost reduced to a minimum and is only 3%. The presence of farms in potential proprietors determines the dominance of the in-kind (agricultural products) rent, which share is 56%.

The largest tenants of agricultural lands are currently agricultural holdings. The examination of expert estimates show that in Ukraine, there are more than 100 large operating holdings, most of which are not allocated to individual business. The formation of agricultural holdings occurs evolutionary, though in a fairly short period of time, which leads to increased social tension in the countryside. The technical refitting of production equipment is accompanied by the optimization of number of employees. At the same time, the sufficient

attention is not always paid to social factors – the adaptation of employees, who are exempt, an individual approach with respect to their possible employment in other positions. For agricultural holdings, the priority is to obtain economic benefit – the profit, and for the society – provide moral and material values of the local community.

Table 2. Lease Agreements and Rent in Agricultural Sector

Index	Ukraine		
	2000	2014	+, –
<i>The share of lease agreements in the context of the entities, %</i>			
With enterprises, where the land was received	85.2	34.0	-51.2
With farmers	4.3	14.4	10.1
With other businesses	10.5	51.7	41.2
<i>The share of lease agreements in the context of their terms, %</i>			
For 1-3 years	45.7	3.1	-42.6
For 4-5 years	41.2	35.5	-5.7
For 6-10 years	11.3	46.4	35.1
For over 10 years	1.8	15.0	13.2
<i>The share in the context of rent payment, %</i>			
money	13.9	41.6	27.7
in kind (agricultural products)	77.4	55.7	-21.7
services	8.7	2.6	-6.1
The rent for 1 ha per year, UAH	73.6	663.8	590.2

Source: estimated by the authors according to the State Service of Ukraine for Surveying, Mapping and Cadaster

The efficiency of an individual enterprise and the public welfare are always in opposition. Under the current conditions, the needs of society in addressing the social issues far exceed the flow of tax payments, which are paid by companies. The analysis points to the poor state of social development of rural areas, which is currently characterized by not only a deep demographic crisis, the decline of the social infrastructure and the extinction of settlements, but also the lack of motivation to work and the high level of unemployment, which is accompanied by an outflow of labor resources.

According to the expert estimates, in 2014, agricultural holdings used 5.6 MIO ha on lease terms, or about 27% of the total land of agricultural enterprises (Rating 20, 2015). It is worth highlighting the first three of them that account for 1.5 MIO ha, incl.: UkrLandFarming – 653 thous. ha, Agroprosperis – 430 thous. ha, Kernel – 390 thous. ha (Table 3).

Table 3. The effectiveness of leased land use by 20 most successful agricultural holdings in Ukraine in 2014

No.	Company name	Leased land area, thous. ha	EBITDA for plant growing, US dollars / hectare of land
1	Svarog West Group	80	700
2	Grain Alliance	50	560
3	Agrospetssservis	41	520
4	Chysta Krynycyia	50	500
5	Industrial Milk Company	137	420
6	Vinnytsia Agribusiness Group	43	347
7	Trigon Agri	49	336
8	UkrLandFarming	653	311
9	Agreyn	130	300
10	Rostock-Holding	60	297
11	Agro Generation & Harmelia	120	244
12	Ukrprominvest-Agro	122	237
13	Agroprosperis	430	231
14	Myronivsky Hliboproduct	380	231
15	Nibulon	82	225
16	KSG Agro	94	200
17	APK-Invest	41	190
18	Ukrainian Agrarian Investments	234	179
19	Agro Invest Ukraine	30	156
20	Astarta	245	124
	Total of 20 agroholdings	3,071	297

Source: estimated by the authors according to the data (Stetsyuk, 2010)

The analysis of the data shown in *Table 3* confirms the thesis that the most effective are agricultural holdings with an area of up to 100 thousand ha. In the case of increasing the area, “the economy of scale starts to work in the opposite direction, and the company’s effectiveness reduces (Rating 20, 2015)”.

A driver for agricultural holdings is the ability to lease the land from farmers for \$40/ha and assign it after a certain period of time on the domestic market for \$100-450/ha to other companies or sell shares of the company for USD1000-1500/ha on the external market (Rating 20, 2015, Stetsyuk, 2010).

For the last few years, the conditions for functioning of agricultural producers have become more complex, as the fiscal pressure from state regulators intensified.

In 2015, the criterion for checking taxes payment by controlling tax authorities was a percentage of turnovers (1% of sales). We conducted a theoretical justification for minimum amounts of taxes based on 1 hectare for main types of crops for 2015. Thus, 1 ha of wheat will create an additional burden of \$4.7, corn – \$6.5, barley – \$4.5, sunflowers – \$7.3, rapeseed – \$7.2 and soybeans – \$3.5. On average, the farmers' expenses per 1 ha will grow by \$5.7. The use of this measure is due to the use of tax evasion schemes by a large number of enterprises (in terms of wages, raw material procurement and product sales).

In addition, it should be noted that according to the amendments adopted by the Law of Ukraine No. 71-VIII "On Amendments to the Tax Code of Ukraine and Some Other Laws of Ukraine Concerning the Tax Reform" dated December 28, 2014, the following tax schemes have been changed for farmers:

- the VAT refund for exporters (grain traders) of crops, except for farmers and enterprises of the trading chain level 1 has been canceled. Thus, the purchase price within the country for different types of products (grain and industrial crops) will be significantly understated (by the VAT amount).

In fact, in Ukraine, there is ban on the refund of VAT on export grain and industrial crops. This is partly explained by the fact that grain producers have to pay the VAT. Therefore, subsidies can occur in the case of VAT refunds from the state budget when grain exports (The Verkhovna Rada offer, 2015).

In turn, the VAT refund to the manufacturer that has self-grown and exported the grain provides only for the refund of VAT actually paid to the state budget. After all, when growing grain, the manufacturer pays the VAT in full without tax incentives in the purchase of seeds, fertilizers, fuels and lubricants and other material and technical resources. It is this amount of VAT that agricultural producers will claim for the refund, like exporting manufacturers of any other products do. In this case, the manufacturer will have no VAT exemptions, since no funds from the direct export will arrive at its special account (The Verkhovna Rada offer, 2015).

In addition, in Ukraine, there are many agricultural producers, who do not enjoy a special scheme and pay VAT on the general grounds. Despite this, in the sale of products directly or through intermediaries abroad, they still will not be refunded the VAT. Thus, the non-refunded VAT on exports of grain for all entities, regardless of whether they use the appropriate privileges or not, is significant tax discrimination (The Verkhovna Rada offer, 2015).

It should be noted that the lack of VAT refund to producers of grain and industrial crops during export is inherently a duty on exports. The actual duty on grain exports violates the Association Agreement between Ukraine and the European Union. For example, the Article 31 of the Agreement states that: "Parties should not impose or maintain any duties, taxes or any other measures having equivalent effect imposed on the export of goods or introduced in connection with the export of goods to another territory". Non-refund of the VAT on exports of grain to its producers is obviously referred to in the Agreement as "the measure equivalent to the export of goods", so it has a direct and serious violation (The Verkhovna Rada offer, 2015).

In today's environment in our country, there are no long-term funding sources. In most cases, banks cannot offer loans for more than a year, and the value of financial resources is very

high, especially when compared with other countries. Therefore, it is evident that the abolition of special schemes will lead to a reduction in capital investments, which in turn will adversely affect the prospects of development of the sector and as a result will have a negative impact on rural development and on the country's ability to compete in global markets (Ribachenko, 2015).

It should also be noted the prolongation of this procedure until the end of 2017.

In general, in 2015, according to our calculations, farmers will not receive about \$1.2 bln in the form of VAT refund in the export of grain and industrial crops, which is approximately equal to \$50 per 1 ha of crops, or \$30 per 1 ton of products sold.

- Cancellation of the fixed agricultural tax (FAT), and transfer of all farmers to the fourth group of the single tax payers as from January 1, 2015. Therefore, from a formal point of view, the FAT has become the fourth group of the single fixed tax. Accordingly, if in 2014, according to the FAT, the farmers paid \$0.46/ha, then since January 1, 2015, they will pay \$5.23/ha, i.e., 11.3 times higher. From this transaction, the government plans to increase revenues to the budget by \$126.4 million, incl. for account of agricultural holdings – by \$23.6 million.
- Increased land tax on farmlands, but no more than 1% of the normative monetary value. According to our estimates, farmers will have to transfer to the budget about \$387.5 million, amounting to approximately \$9.53/ha;
- The tax base for single tax payers from the fourth group is the normative monetary value of one hectare of the farmland (arable land, hayfields, pastures and perennial crops), taking into account the indexation factor of the base (reporting) tax determined as of January 1 in accordance with the procedure specified in chapter XII of the Tax Code. The cumulative value of the land normative monetary value indexation rate in 1995 as of 1 January 2015 is 3.997.

Changes in the regulatory monetary value of land will change the level of lease payments in 2015 as well. In connection with the devaluation of the hryvnia, the farmers will pay not \$40, as a year earlier, but \$28.6.

The enterprises of the agricultural sector that have chosen the regular taxation scheme must pay the income tax. Starting from 2011, the income tax rate was raised from 17% to 18% in 2015.

The negative impact on the final results of economic management was brought by the devaluation of the national currency – hryvnia (four times against the dollar). In general, losses from the exchange rate differences were suffered by domestic farmers focused on the domestic (national) market. At the same time, export-oriented companies (agricultural holdings and traders) have benefited from the national currency rate fluctuations.

In other countries, farmers receive assistance from the state on average of EUR500 per hectare, while in Ukraine, in addition to removing various subsidies, farmers are even taxed. In European countries, for example, the share of government subsidies in the price of food policy amounts to around 36%, in America – 18%, and in Japan, the amount of the subsidy is 60% (Farmers protest, 2012).

If we count all the above novations, we will get not the development trend, but on the contrary, the trend of recession. That is, due to unreasoned state policy, agricultural holdings will suffer losses in the amount of \$100/ha, and even more for some types of products, on 1 hectare of agricultural land.

Accordingly, such measures would increase costs and decrease the net income of agricultural holdings, reduced the area of cultivated land, which will negatively affect the expectations of internal and external stakeholders (Nitsenko, 2012).

The results of the comprehensive study suggest that in order to improve the efficiency of agricultural holdings and to develop the rural area, it is necessary to improve the legal framework for eliminating misunderstandings between them in terms of taxes, namely to regulate their payment within the territories where agricultural holdings operate. The sustainable development of production should be achieved through the harmonization of balance between the value of the resource potential and the ability of land to recreate its fertility. The main directions to improve economic relations between the units of agricultural holdings are the improvement of the human resource system organization and management, optimization of the production structure and development of industry relations optimal models. There is a need to improve lease land relations in terms of introduction of the system of land lease rights market legal regulation and development of mortgage operations.

The State's position on the effective use of agricultural land should be aimed at establishing the legal norms of penalties for failure to use the land. In this case, it is advantageous to use the historical experience of the Ancient Babylon, in particular, to study Hammurabi's laws, according to which, in the case of non-cultivation of the field throughout the year, the law forced the tenant to pay the owner a rent at the level of 33-50% of the harvest and carry out the main cultivation on this field.

The prospect of lease of land relations should be the permanent land use, the proper functioning of the unified system of monitoring the land-lease relations, the rent increase corresponding to the economic growth, the prolongation of lease agreements, the development of sublease and the creation of conditions for the land rational use and protection. It is appropriate to introduce the model of medium- and long-term lease with subsequent renewal of the agreement, succession of rights or redemption of the land. Subject to lifting the moratorium and introducing the purchase and sale of land, it is appropriate to use the scale of motives and restrictions on their resale. The practical implementation of the proposed measures by agricultural enterprises will attract investment in agricultural production and develop it on the innovation basis.

References:

Nitsenko, V.S. (2012). Transformation processes in agriculture in the context of development of agroholdings. *Collection of scientific works of the Taurian state agrotechnological university (economic sciences)*, 2 (18), vol. 6, 169–179.

Farmers are protesting against new taxes. (2012, February). (n.d.). Retrieved from: <http://news.ub.ua/ru/32070-fermery-protestuyut-protiv-novyh-nalogov.html>

Rybachenko, E. (2015, November). *Agro is, undoubtedly, people's business*. (n.d.). Retrieved from: <http://agro-region.com/2015/11/1649/>

Verkhovna Rada propose to exempt from VAT export of grain and industrial crops. (2015, April). (n.d.). Retrieved from: <http://agroconf.org/content/vr-proponuyut-zvilniti-vid-pdv-eksport-zernovih-ta-tehnichnih-kultur>

Stetsyuk, P.A. (2010). Prerequisites and opportunities for the development of integrated agroformations: the financial aspect. *Bulletin of Kharkiv. Nats Tech Un-th agriculture: Economic sciences*, 99, 17–25.

Rating of the 20 most effective agricultural companies in Ukraine (2015, August). (n.d.). Retrieved from: <http://www.svb.org.ua/news/rating-20-naiefektivnishikh-agrokompanii-ukraini>

Kirilenko, I.G. & Pavlov, O.I. (2010). Problems of the Ukrainian village and their solution in the context of agrarian transformations. *Economy of agroindustrial complex*, 7, 24–31.

Dankevich, A.E. (2011). *Development of Integrated Structures in Agriculture: Monograph*. Kyiv, Ukraine: NSC IAU.

Mesel-Veselyak, V.Ya. (2010, February). *Agrarian reform and organizational and economic transformations in agriculture: reports*. The twelfth annual meeting of the All-Ukrainian Congress of Scientists of Economists-Agrarians. Kyiv, Ukraine: NSC IAE.

Zastavnyuk, L.I. & Zygyry, O.V. (2011). Problems of sustainable development of agriculture in Ukraine in the context of agrarian transformations. *Sustainable development of the economy*, 7, 35–38.

Fedoseyeva, O.V. (2009). Formation of the system of socio-economic development of agriculture. *Economic Space*, 23/1, 273–278.