

# COUNTRY REPORT ON INFRASTRUCTURE AND FINANCE UKRAINE

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## I. COUNTRY INFRASTRUCTURE AND POLICY DIRECTIONS

The State program document “Ukraine 2020: Strategy for national modernisation” determines the investment strategies of infrastructure as one of the main policy directions of the Ukraine Government. The program clearly identifies priorities in transport infrastructure development and other infrastructure sectors such as:

- Power supply infrastructure, including electric energy;
- Mining, including coal industry infrastructure;
- Gas and oil industry infrastructure, including networks and stations;
- Housing and utilities infrastructure;
- Communication infrastructure;
- Agriculture infrastructure;
- Touristic infrastructure;

The equivalent policy directions for infrastructure investment are also stated in the 2010-2014 presidents’ program of economy reforms in Ukraine and in the state 2010 program of economic and social development.

### *Transport infrastructure*

Currently Ukraine requires a complex development of its transport networks. First of all, this relates to international transport corridors, motorways, express railways, sea and airports.

This issue is complicated by the fact that the entire transport infrastructure is state-owned, requires substantial investment and largely relies on finance from state and local budgets. Taking into account the lack of budgetary financial means, cooperation is needed between public and private sectors, and new forms of financing need to be explored

It is stated by the Government of Ukraine that the next transport policy principles will pertain to the attraction of investments for infrastructure development. The main policy directions related to transport infrastructure investments are defined as follows:

- Increase in transport network capacity;
- Introduction of high speed railway passenger services, primarily day trains;
- Development of the road network, primarily in relation to express ways and relief roads;
- Development of the sea ports’ capacities;
- Development of transport links and rail and road access routes to sea ports;
- Development of the network of crossing points on the State Border of Ukraine;
- Development of airport network, primarily that coming within the framework of preparation for Euro 2012;
- Creation of the state system for utilisation by the aviation area of Ukraine;
- Improvement and development of the public transport network;
- Increasing the transport network capacity in the capital and oblast centres;
- Further construction, building and urgent overhaul of bridges;

- Creation of a network of logistic centres and dry ports;
- Improvement of the network of transport information and communication technologies;

## 1.1 IMPLEMENTATION PROCESS

There are a set of national legal documents established as rules and procedures for project development and implementation.

Most of the investment projects developed by companies have to be approved by a responsible authority; local or national authorities may perform this function depending on the type of works, project size and type of ownership of the company. Projects which are funded by private capital often follow an investor friendly approval process.

A number of technical and ecological rules and provisions for construction and procurement regulate the transport sector. Most of the infrastructure projects require agreements with city (local) administrations and environmental and project-building authorities.

As aforementioned, the entire transport infrastructure and almost all transport companies are state-owned in Ukraine; this means that companies are a subject to procedures related to the State Budget.

***The Resolution of the Cabinet of Ministers of Ukraine (CMU) N 1269 dated 31.10.2007 established the main methods of project development and approval procedures as follows:***

### ***General conditions:***

The following Investment Projects (Programs) shall be approved:

- By the CMU: Multi sector, interregional and regional if the project is completely or partially implemented using costs from the state budget;
- By Verhovna Rada of Ukraine (Parliament): State guaranteed projects and projects with IFO;
- Local territorial authorities: Projects which are completely or partially implemented with funding from the local budget;
- Projects that are fully funded by other sources and approved in the order determined by the investors (customers), except for projects referred to in paragraph 1.2 – 1.4 of specific conditions.

This method is obligatory for all state owned enterprises and does not depend on the state share in ownership. This means that the CMU regulation applies most of all to transport companies and enterprises.

At the same time there are other documents established as ***rules for investment projects' development and implementation:***

- ***Concession projects:*** The CMU resolution "On approval of the winner of the competition and signing of concession contracts for projects of state and municipal property offered in the concession" dated 12.04.2000 № 642.

- **Investment contracts:** The CMU resolution "On issues of investment by state enterprises, institutions and organizations" dated 17.04.2009 № 530.
- **Agreement on joint activities** - CMU resolution "On the conclusion of some agreements" dated 07.05.2008 № 703-p.
- **Investment agreement for projects of Euro 2012** (List of project Euro 2012 defined in Regulation CMU 22.02.2008 № 107) The CMU resolution: "On approval of investors for the construction and / or reconstruction in preparation and holding in Ukraine the final part of the European Championship 2012" dated, 06.08.2008, № 711.
- **Credit agreement with IFO** (without a competitive selection procedure of creditor) - The CMU resolution: "On the initiation, preparation and implementation of the Project of economic and social development of Ukraine, supported by international financial organizations" dated 26.11.2008 № 1027.

## 1.2 LEGAL AND REGULATORY FRAMEWORK FOR INFRASTRUCTURE

Existing Ukrainian legislation on Investment Activity in Ukraine (main pillars) is as follows:

**Commercial Code of Ukraine** (Code of Ukraine: of 26.12.2008 N 835-VI) This Code defines the fundamentals of commercial activity in Ukraine and regulates commercial relations, which arise in the organisation process and exercise commercial activity between business entities, as well as between these entities and other participants of relations in the sphere of commercial activity.

**Budget Code of Ukraine** (Code of Ukraine: of 21.06.2001 N 2542-III) This Code determines: the fundamentals of the budget system of Ukraine, its structure, principles and legal grounds for functioning; principles of budget process and inter-budget relations; and responsibility for violation of budget legislation. The code envisages delimitation of functions in the budget sphere between executive bodies of state power and executive bodies of local self-government.

**Law on the State Budget of Ukraine** determines revenues and expenditures of the State Budget of Ukraine for year N, including revenues of the General Fund and Special Fund of the State Budget. Also, the present Law will approve the volumes for returning loans to the State Budget of Ukraine, the volumes for granting loans from the State Budget and will establish the marginal size of the deficit of the State Budget, etc.

**Law on Investment Activity** (of 18.09.1991 № 1560-XII) This Law sets forth basic legal, economic and social conditions for carrying out investment activity within the territory of Ukraine.

**Law on the Regime of Foreign Investments** (of 19.03.1996 N 93/96-BP) This Law determines: peculiarities to the treatment of foreign investments within the territory of Ukraine, as well as general provisions and terms. It also establishes protection guarantees for foreign investments, regulates establishment procedures and any peculiarities of activity in enterprises with foreign investments, etc.

**Law on Innovation Activity** (of 04.07.2002 № 40-IV) defines legal, economic and organisational principles of state regulation of innovation activity in Ukraine.

**Law on Concessions** (of 16.07.1999 N 997-XIV) This Law defines the concept and legal principles of regulation of concession relations of state and communal property, as well as conditions of and procedure for their conducting in order to increase the efficiency of use of state and communal property and the provision of needs of the Ukrainian citizens in goods (works, services).

**Law on Concessions for the Construction and Operation of Motor Roads** (of 14.12.1999 № 1286-XIV) this Law defines the peculiarities of granting concessions for the construction of motor (off-city) roads of general use and their subsequent operation for the sake of Ukraine's economy.

**Law on Financial Leasing** (of 16.12.1997 N 723/97-BP) defines the main rules for this activity in Ukraine.

**Law on State and Communal Property Lease** (of 10.04.1992 N 2269-XII) According to the Law lease is a based on agreement and considers aspects such as fixed-date use of property and if the lease is necessary for execution of entrepreneurial and other activities.

## II. GOVERNMENT PERSPECTIVE ON THE ROLE OF PRIVATE SECTOR INVOLVEMENT

The attraction of investments from the private sector has been stated as a key priority by all Ukrainian Governments.

The first attempt by the governmental bodies was to construct the Lviv Krakovets highway on concession principles (by way of experiment) in 1998. Pursuant to the Law of Ukraine "On Concession", passed in 1999, Ukrainian Government found to define the list of objects that were transferable to an investor in concession.

### **Concession activity in Ukraine has the following specifics:**

- It covers areas that have strategic, economic or social value which may not be privatised and where the State is interested to attract private capital;
- In a concession agreement the concessionaire has the possibility to establish conditions for the state property use of the right granted to a concessionaire which will secure high efficiency of its use the required control over the agreement fulfillment and its termination. The agreement may contain any provisions that are not at variance with the current legislation;
- A concession object remains the state property.

In addition, since 1998 a set of legislative and the other regulatory documents have been approved in Ukraine to regulate various aspects of concession creation and concession administration based on the use of state or municipal property.

Concessions are regarded the most attractive way to implement large scale long-term infrastructure projects in Ukraine.

**Today's efforts for further PPP development in Ukraine by central executive bodies** are targeted to increase the scope of private investments and in this way implement significant investment projects of national and regional importance. It is also important to achieve the proper quality of final product in PPP project implementation.

The Government has long been interested in the establishment of concession arrangements, in general, and PPPs in particular for roads construction. In March 2006 EBRD and the World Bank funded the First International Conference, "Perspectives for Ukraine in Implementation of PPP Infrastructure Projects" in Kiev. Since then a number of other conferences have been held. EBRD concluded that it was ready to assist in the development of PPPs in the transport sector in Ukraine with project selection and reviewing tender and concession agreement draft documentation.

As part of a €200 million sovereign loan to Ukraine (with the proceeds to be lent on State road administration Ukravtodor for the rehabilitation of the final 427km stretch of the M06 motorway connecting Kiev with European Union countries such as Hungary, Slovakia and Poland) the EBRD provided technical cooperation funds to finance consultancy assistance for the development of concession legislation and a PPP strategy. This element was described as crucial for the Bank's continued support of transport sector reform in Ukraine. Currently, the road sector is the only the part of Government that is actively pursuing PPPs in Ukraine..

**While implementing PPP in a contractual form, provisions of the following agreements may be used:**

- **Concession;**
- **Lease of the state property;**
- **Leasing;**
- **Production sharing agreement (Joint activity agreement);**
- **Agreement to administrate state property (Management agreement);**
- **Joint venture agreement;**
- **Not prohibited by Ukrainian legislation.**

## **2.1 RESPONSIBLE AGENCY FOR PRIVATE SECTOR INFRASTRUCTURE PROCUREMENT**

**In private procurement there is no rigid, statutory system.** However, from a practical point of view the easiest option for creating a procurement system in the private enterprise is the existing legal framework governing the procurement field.

At the same time, as it is mentioned above, the infrastructure is mostly state-owned and subject to public procurement procedure.

According to the recently adopted **new law about the implementation of public procurement № 2263-1 (unofficial title of "The Law on tenders")**, **the responsible agency for procurements is Department of Coordination of State Procurement of the Ministry of Economy of Ukraine, whilst the appeal body is the Antimonopoly Committee of Ukraine.** The Act establishes the legal and economic framework for the

procurement of goods, works and services for public funds. Its purpose is: to create a competitive environment in public procurement; to develop fair competition; and to ensure the rational and efficient use of public funds, etc.

***In particular, the statute states that the law does not apply to cases where the subjects of procurement are:***

- Goods and services related to design and manufacture of security papers, banknotes and coins; and their storage, transportation and accounting;
- Services for procurement by state-owned banks and banks in the capitalisation of which were attended by the state, solely for their:
  - Banking operations in accordance with the Law "On Banks and Banking Activity";
  - Goods, works and services for procurement by customers located outside of Ukraine;
  - Goods, works and services for procurement of state secrets in accordance with the Law "On State Secrets";
  - Services necessary for the implementation of public borrowing, servicing and repayment of public debt.

***Certain laws of Ukraine are determined by features of the purchase of such goods, works and services:***

- Protected paint, paper and other materials used to manufacture the blanks of securities and strictly accountable documents (records) according to the scheme of protection;
- Services for carriage by rail;
- Natural and petroleum gas and services related to its transportation, distribution and supply;
- Postal services, postage stamps and envelopes marked;
- Telecommunications services, including the retransmission of radio and television (except for mobile services and Internet service providers);
- Centralised water supply and drainage;
- Electric energy, its transmission and distribution;
- Centralised supply of heat energy;
- Nuclear fuel, non-irradiated fuel elements (cartridges) for nuclear reactors;
- Services for transportation of oil and petroleum products through pipelines, and other substances by pipeline;
- Crude oil or petroleum products;
- Service training institutions of higher learning I-IV levels of accreditation by the state order.

## 2.2 LEGISLATIVE CONSTRAINTS REGARDING PRIVATE SECTOR PARTICIPATION

Eventually the Cabinet of Ministers of Ukraine adopted Resolution No 530 dated April 17, 2009 that set out the procedure for making investment agreements in the public sector of Ukrainian economy. The new procedure specifies the auctions to be held in order to attract investors. This requirement applied to all public companies, institutions, and organisations, including the sea ports that do not take absolutely into account the specific nature of the maritime sector.

The Cabinet of Ministers has followed this trend initiated by Instruction No 703 dated May 7, 2008. Pursuant to this instruction, public companies were able to make contracts on joint (investment) business, commission, agency and property management solely on the basis of the Cabinet of Ministers resolution. Thus, referring to the contracts on joint business, commission, agency, property management the procedure has remained the same, while the investment agreement regulation has been materially changed.

The new procedure establishes that a decision to implement an investment project should be taken by the Cabinet of Ministers pursuant to approval made by a regulatory body (i.e. a sector ministry) and expertise provided by the State Property Fund, Ministry for Finance, and Ministry for Economy. The Cabinet of Ministers, having taken a positive decision, can permit the auction to be held.

The main features of the new order include:

- 1) The list of mandatory documentation to be submitted for the project expertise is specified, though this list is not closed. Thus, ministries may request additional documents; neither their number nor the contents are limited.
- 2) The timing for document expertise is either not fixed at all or is not precise. For example:
  - a) A 30-day period fixed for the expertise shall start since the moment of all documents submission. Given that the ministries may request additional documents this process may last for an uncertain time.
  - b) Referring to the Cabinet of Ministers the new procedure does not fix the time assigned for taking a decision on investment project implementation.
- 3) The auction principle itself creates a competitive basis for selling. In this case the right to make an investment agreement is sold.
- 4) The auction may be held in the presence of at least two participants. However, if only one auction participant has registered, the auction commission (set up by the regulatory body) may recognise this single participant a successful buyer.
- 5) The investment draft agreement is included into the mandatory list of documents and is submitted to the regulatory body at an early stage. Assuming that the terms and conditions of investment agreement have resulted from the complicated negotiations between an investor and a public company then the document is amended and adjusted by the regulatory body (the sector ministry), followed by the State Property Fund, Ministry for Finance and Ministry for Economy which finally reviews the draft. The Cabinet of Ministers might add or amend something itself at the phase of taking a decision on approving the investment project implementation. Only after all these steps the auction may be held. There is confusion in that after the auction the sector



ministry 'shall draw out the agreement draft' to be approved again by other ministries and the State Property Fund, the Ministry for Finance and the Ministry for Economy may give their 'recommendations on improving the agreements terms and conditions'.

### **III. SOURCES OF FINANCING**

Ukraine is one of the countries to correctly seek and rapidly receive large scale of finance. The main institution active in the country are:

- International Monetary Fund;
- The World Bank;
- The European Bank for Reconstruction and Development;
- The International Financial Corporation;
- The European Investment Bank;
- Nordic Investment Bank;
- Multilateral Investment Guarantee Agency – MIGA);
- International Development Association – IDA;
- Japan Investment Bank for International Cooperation;
- A range of bilateral donors.