

## ACTION FICHE UKRAINE – ENPI AAP 2008

### 1. IDENTIFICATION

Title	Support to the implementation of Ukraine's strategy in the area of energy efficiency and renewable sources of energy		
Total cost	<i>EC contribution: EUR 70 million (including EUR 6 million allocated from the Governance Facility)</i> <i>Other contributions still under discussion with IFIs. EBRD's expected contribution: US\$ 100 million</i>		
Aid method / management mode	Sector Policy Support Programme: - Budget support (centralised management): EUR 63 million - Project mode for related technical assistance (centralised management): EUR 7 million <b>CRIS n. 19595</b>		
DAC-code	<b>23010</b> <b>23030</b>	Sector	<b>Energy Policy and Administrative Management</b> <b>Power generation / renewable sources</b>

### 2. RATIONALE AND COUNTRY CONTEXT

#### 2.1. Economic and social situation

##### Basic existing preconditions

The three basic pre-conditions for implementing a sectoral energy support programme are currently met:

- there is a Government strategy for the energy sector whose objectives and principles are converging with those of the EU, and which is to be supported by a sector budget support programme under the AAP 2007 for Ukraine
- there is an active policy dialogue between the Government and the EC on energy related issues, that the above-mentioned programme has already contributed to accelerate
- a monitoring mechanism of the co-operation outcomes has been put in place, including an ad-hoc monitoring group to follow achievement of the sector reform targets set forth under the above-mentioned programme<sup>8</sup>.

##### Macro-economic policy and Public finance management

The September 2006 PEFA report assessing Ukraine's PFM system concluded that "Ukraine has in place the fundamental PFM systems for managing macro-fiscal developments and some elements for enabling strategic allocation of resources". A sector readiness assessment study, meant to assess the readiness of the energy sector for the budget support modality, confirmed that Ukraine has an effective PFM structure in spite of improvements needed in reporting and controls. To tackle these issues, the Government adopted on 19 October 2007 a PFM Reform strategy that explicitly aims at setting up modernised systems "in compliance with recommendations on governance issued by the European Commission." The World

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<sup>8</sup> Additionality of the proposed measure with the AAP 2007 programme is discussed below in section 2.4.

Bank is committed to financing its implementation as from 2008 through a loan estimated at US\$ 65 million.

## **2.2. Cooperation policy of beneficiary country**

Ukraine-EC energy cooperation in the field of energy efficiency and renewable energy (EE/RES) is based on the Partnership and Cooperation Agreement, the Energy chapter of the EU-Ukraine Action Plan and the Energy MoU<sup>9</sup>. It has gained considerable momentum in 2006 and 2007, thanks to a structure of sub-sectoral roadmaps and monitoring groups, including one specialised on EE/RES.

The existing EU-Ukraine cooperation framework embraces the entire range of issues of interest to enhance EE/RES policies in Ukraine in the current context of high energy intensity (about three times more than the EU average), the need for diversification of energy resources and increased reliance on domestic sources of energy, and strong forecast GDP growth (estimated at 6% annually in the medium run). This framework includes objectives, deadlines and priorities, more precisely defined in implementing roadmaps signed between the Commission and the Government. In the framework of the Energy MoU<sup>10</sup>, a constant dialogue and monitoring of Energy MoU progress in the EE/RES sector is taken on board by a joint EC/NAER/MFE<sup>11</sup> working group which contributes to annual joint progress reports presented to the EU-Ukraine Summits.

## **2.3. Government Sector Programme**

The current government programme refers to the Energy MoU and the Ukrainian Energy strategy 2005-2030 as the two key strategic documents it will endeavour to implement. Convergence of the objectives and timetables of these two documents guarantee a good ownership of the measure by the Ukrainian stakeholders, as shown during the formulation phase of the measure. In addition, Ukraine's political commitment to full membership in the Energy Community Treaty (ECT), approved by the ECT ministerial conference in June 2007, should set the pace in the coming years for adoption of the whole EU electricity and gas acquis, including acquis on renewable energy as well as rules related to environment and competition. A recent (26-29 Feb. 2008) Commission mission on Ukraine's preparedness for ECT Accession confirmed the importance that the Ukrainian government attaches to ECT Accession, which constitutes a major sector objective of the Ukrainian Energy strategy.

## **2.4. Lessons learnt**

The political priority placed in Ukraine on the EE/RES sector, particularly since the governmental conference on the subject held on 30 November 2007, and the holistic nature of this underdeveloped sector's reform, emphasise the need for a sector-wide approach. It will have to be reflected in the proper choice of the budget support indicators to be identified.

Lessons can be drawn from the experience of past Tacis projects involved in setting up Energy Service Companies (ESCOs). Ukraine presents a series of barriers which negatively affect EE/RES development:

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<sup>9</sup> Memorandum of Understanding between Ukraine and the European Union on enhanced co-operation in the field of energy of 1 December 2005.

<sup>10</sup> The Ministry of Fuel and Energy is the counterpart mandated by the Ukrainian Government to coordinate the Energy MoU, including its Roadmap on energy efficiency and renewable sources of energy. As such, it will co-chair the monitoring group to be established to follow up implementation of this measure.

<sup>11</sup> NAER is the National Agency of Ukraine for Effective Use of Energy Resources, the main Ukrainian institution responsible for the Ukrainian policies dealt with in this measure. As such, it will co-chair the monitoring group to be established to follow up implementation of this measure.

- General barriers to investments in Ukraine’s economy, including energy efficiency investments: political instability, weak regulatory framework for doing business, slow progress in institutional reforms (the judiciary and state bureaucracy reforms are still on the agenda)
- EE/RES-specific barriers: absence of consolidated legislative/executive approach to energy conservation (resulting in repeated Presidential vetoes on EE/RES related laws); slow progress in tariff reform and market liberalisation<sup>12</sup>; failure of existing legislation to stimulate investments in the sector, by lack of implementing regulations or sustainable incentives; lack of business focus on the EE/RES issue (the key challenge is often to convince the client that energy efficiency can generate additional revenues); lack of knowledge on financing energy efficiency and renewable energy, resulting in Ukrainian banks / investors being unwilling to take project risk; lack of skilled energy managers and energy auditors; lack of information about technologies, opportunities, costs, and benefits.

In consideration of the above and the experience matured on previous projects, Ukraine needs a pragmatic, sector-wide approach, where the focus is mainly placed on legislation, regulatory framework development and institutional reforms. This is the main objective of the Sector Budget Support Programme *"Support to the implementation of Ukraine's Energy strategy"* financed under the Annual Action Programme 2007 for an amount of 65M€ topped up by the amount of 22M€ allocated under the Governance Facility, and currently at the beginning of its implementation.

## 2.5. Complementary actions

Ukraine has started from 2007 an intensive energy sector rehabilitation and modernisation programme that it intends to finance mainly via borrowings on the domestic or the international market, under the coordination and supervision of the Deputy Prime Minister for Infrastructure. This programme in support of the energy strategy of the Ukraine is complemented by planned EIB/EBRD loan packages (under EC co-ordination) to be followed by further lending operations to modernise the energy sector in relation with the objectives of the Energy MoU. The EBRD is otherwise running a US\$ 100 million fund to finance energy conservation measures in the residential sector.

The proposed measure will add substantial value to the AAP 2007 energy sector budget support programme, which focuses on fundamental energy market restructuring and includes energy savings measures supported under the Governance Facility. These measures put the emphasis on reducing the energy consumption of the energy sector itself, and particularly of the gas transit system. The proposed measures bring essential complementarities to this target by aiming at implementing an energy efficiency and renewable energy sources strategy in line with the overarching objectives of economic and environmental sustainability, security and diversification of energy supplies.

Complementary Tacis projects include a recently started support to prepare Ukraine to integrating the electricity trans-European networks, a forthcoming project in support of coal sector reform and two twinning projects, one ongoing and one presently at design stage, to strengthen NAER’s capacity in policy development and maintenance. The World Bank is also preparing a part on energy sector reform in its forthcoming Second Development Policy Loan to Ukraine.

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<sup>12</sup> From this standpoint, this operation comes rightly after the AAP 2007 energy sector reform measure meant in particular to liberalise the energy market

## **2.6. Donor coordination**

The Government has recently established a Government-led coordination mechanism, which includes an EE/RES sector thematic group. This group first convened on 23 November 2006 (under EBRD co-leadership) and again on 27 February 2007 (under EC co-leadership). In addition, frequent working contacts of the EC Delegation with the World Bank, the EBRD and smaller donors involved in the energy efficiency segment (Denmark, Sweden, the Nordic Environment Finance Corporation) provide guarantees of cohesion and coordination of efforts.

Donor coordination has made less progress in the field of PFM. The PEFA assessment of the PFM system was carried out by the World Bank. The PFM reform strategy and Action Plan are being prepared by the Government with technical assistance of the World Bank, other donors providing assistance to the Ministry of Finance and related institutions not being involved. However, the Commission is defining the PFM related conditions essential for introduction of budgetary support based on the PEFA assessment. This work is carried out in close coordination with the World Bank to ensure that unified criteria are applied.

## **3. DESCRIPTION**

### **3.1. Objectives**

- To contribute to implementing the measures agreed in the Ukraine ENP Action Plan in the areas of Energy efficiency (EE) and Renewable energy sources (RES)<sup>13</sup>.
- To support implementation of the priority measures agreed under the Energy MoU in the areas of energy efficiency and renewable energy.
- To set up an institutional framework appropriate to sustain implementation of such measures in the long run.

### **3.2. Expected results and main activities**

- Ukrainian energy efficiency and RES policies brought in line with best European practice, and substantially improved to aim at an adequate and sustainable energy mix favouring Ukraine's locally available resources (wind, solar, geothermal, hydro); priority measures are jointly approved and implemented; relevant technical norms and standards are harmonised with EU industrial norms and practices
- Increased efficiency of the transit and transportation of energy, including through the reduction of losses and an optimisation of the networks
- Significantly enhanced EU-Ukraine co-operation regarding energy conservation and RES projects, with particular emphasis on research, technology deployment and the promotion of best practice
- Use of renewable energy significantly enhanced, via development and effective implementation of ad-hoc policies, and the active participation of Ukraine in European research projects
- Effective methane recuperation programmes implemented in Ukrainian coal mines, with the related improvement of the safety and efficiency of the coal sector
- Institutions responsible for designing and promoting such policies, including NAER, strengthened adequately to make implementation of the above policies sustainable over time
- Competency of personnel of relevant institutions significantly increased (especially

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<sup>13</sup> Sections 51 and 56 of the EU-Ukraine Action Plan of 21 February 2005.

related to programmes drafting) – more specialists should be involved

- Independence of the institutions responsible for setting the tariffs for competing energy sources has been significantly strengthened
- IFIs investments in the areas of energy efficiency and renewable energy are fostered (priority investment projects to be selected being prepared within the framework of the proposed measure<sup>14</sup>)

As underlined in section 2.5, these results focus on supporting Ukraine in taking last-chance, decisive steps towards energy efficiency and the use of renewable energy sources; by contrast, the previous sector budget support programme focused on supply side improvements and structural reforms to allow for a more transparent and economically sustainable functioning of the energy market.

Activities to implement the measure will consist in setting up and running an appropriate system to monitor progress on the above-listed objectives and more specifically attainment of the agreed disbursement targets. This may imply the use of support technical assistance or specific equipment, budgeted for this purpose (section 4.3).

### **3.3. Stakeholders**

The main partners for implementation will be the Ministry of Fuels and Energy<sup>3</sup>, the National Agency for the Efficient Use of Energy Resources<sup>4</sup>, and the various organisations involved in implementing Ukraine's energy efficiency and renewable energy strategies.

The high degree of congruence of the proposed measure with domestic and donor-sponsored past, on-going or foreseen activities in the energy sector and with the foreseeable lending operations of the main international financial institutions (including the EIB<sup>15</sup>, the EBRD, and the World Bank), makes the proposed measure a good example of beneficiary country's involvement and ownership. NGOs with active participation in Energy Efficiency and Alternative Fuels development have also been involved.

### **3.4. Risks and assumptions**

#### Assumptions

- Ukraine is willing to conduct a policy dialogue with the European Union and other interested donors on the issue of PFM reform.
- Ukraine will keep to all of its commitments under the ENP Action Plan and the Energy MoU, and will continue demonstrating heightened interest in the proposed cooperation in EE/RES.
- Ukraine will not substantially revise the principles underlying its national energy strategy, and its Government will be willing to follow the foreseen reform path, translating it into concrete policies.

#### Risks

- One or several of the ministries, agencies or companies involved in the programme might either be reluctant or not have the capacity to cooperate in an ordered manner.

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<sup>14</sup> Certain projects, such as retrofitting in the power generation sector or the modernisation of the chain of compressor stations on the gas trunk pipeline have already been identified with the MFE.

<sup>15</sup> The EIB's possible contribution to the implementation of EE/RES projects in Ukraine was discussed in October 2007, following a joint review in Kyiv of investment projects under preparation in the energy and environment sectors. The EC and the EBRD are already co-operating closely on energy efficiency measures in the Ukrainian residential sector. Energy efficiency is one of the objectives of the World Bank's upcoming programmatic loans to Ukraine.

This risk can be mitigated via the use of established Energy MoU dialogue mechanisms and the provision of adequate technical assistance.

### 3.5. Crosscutting Issues

The cross-cutting issues of good governance and human rights, as well as environment, are clearly integrated into the proposed programme, through:

- The alignment of EE/RES policies and energy efficiency targets with EU market-based norms, with its three-fold implications: in terms of encouraging wide dissemination of energy savings technologies for the population and small businesses; in terms of mitigating the consequences of the rise in imported energy prices for the population; and in terms of improving access to energy for the population
- The replacement of equipment on the hydrocarbons transit system will go hand in hand with important energy savings and secondary energy recuperation
- Energy efficiency actions will imply active dialogue of the population with the authorities at the local level
- The renewed impetus given to energy-efficiency actions will lead to reduced a environmental impact of the economy as a whole

At this stage, the proposed programme has no identified impact on gender equality.

## 4. IMPLEMENTATION ISSUES

### 4.1. Implementation method

Untargeted budget support under centralised management.

### 4.2. Procurement and grant award procedures

All contracts implementing the action must be awarded and implemented in accordance with the procedures and standard documents laid down and published by the Commission for the implementation of external operations, in force at the time of the launch of the procedure in question.

The essential selection and award criteria for the award of grants are laid down in the Practical Guide to contract procedures for EC external actions. The maximum possible rate of co-financing for grants is 80%. Full financing may only be applied in the cases provided for in Article 253 of the Implementing Rules of the Financial Regulations where financing in full is essential to carry out the action in question.

All programme estimates must respect the procedures and standard documents laid down by the Commission, in force at the time of the adoption of the programme estimates in question.

### 4.3. Budget and calendar

- |                                  |   |            |
|----------------------------------|---|------------|
| – Budget support:                | € | 63 million |
| – Related technical assistance : | € | 7 million  |

Budgetary support is expected to be disbursed in three tranches: a first up-front tranche of €31 million, within 3 months following the signature of the Financing Agreement, and two variable tranches of €16 million maximum each, by the end of the 18<sup>th</sup> and the 36<sup>th</sup> month following such signature, respectively. Provision of technical support to the measure (technical assistance) will also be included in the programme. This will ensure proper follow-up of implementation, and provide for specific advice to facilitate achievement of critical programme benchmarks. The technical assistance component will include an indicative allocation of 0.5M€ for Evaluation, Audit, and Visibility actions.

The programme will in principle be implemented within 36 months starting from the signature of the Financing Agreement.

#### **4.4. Performance monitoring and criteria for disbursement**

Performance monitoring will be exerted by a Joint monitoring group whose basis has been laid down in August 2006 with the establishment of the Energy MoU monitoring group partnering the Ministry of Fuel and Energy and the European Commission. The larger Joint monitoring group will rely on official information provided by Ukraine and verified as appropriate by the ad-hoc Advisory group currently being established at the Ministry of Energy (100% EC funded).

Key indicators measuring progress will focus on policy improvements, number and effective outcomes of approximated legislation / regulation; surveys and market development studies undertaken; number of EE/RES fostering projects generated (with government departments, energy utilities, donors, dedicated funds, lending institutions, business associations, municipalities, cities' networks, accreditation bodies, etc); possibly number and quality of training activities number of buildings concerned by energy conservation measures (public and private, new as well as existing); amount of CO<sub>2</sub> emissions saved.

#### **4.5. Evaluation and audit**

Evaluation of the results achieved will be entrusted to independent consultants, as well as external audits (which will be carried out if necessary). Evaluation and audit will be funded out of the technical assistance component of the programme.

#### **4.6 Communication and visibility**

The programme will follow the orientations of the Manual on Visibility of External Actions (e.g., press release at the signature of the FA, visibility for reports and studies, etc). Given the political importance of EE/RES promotion in Ukraine, a specific communication strategy will be developed, to be funded out of the “technical assistance” budget throughout the measure’s lifetime, in order to inform potential stakeholders of the opportunities that the revamped policies offer, to raise awareness of the potential of EE/RES in the economy, and to generate active support from energy stakeholders and consumers.

## ACTION FICHE UKRAINE – ENPI AAP 2008

### 1. IDENTIFICATION

Title	Promoting mutual trade by removing technical barriers to trade between Ukraine and the European Union		
Total cost	<i>EC contribution – EUR 45.0 million (including EUR 8 million allocated from the Governance Facility)</i>		
Aid method & Management mode	Sector Policy Support Programme: - Sector budget support (EUR 39 million - centralised management) - Project mode for related technical assistance (EUR 6 million - centralised management). <b>CRIS n. 19594</b>		
DAC Code	<b>33120</b>	Sector	<b>Trade facilitation</b>

### 2. RATIONALE AND COUNTRY CONTEXT

#### 2.1. Economic and social situation

##### Basic existing preconditions

The three basic pre-conditions for implementing a sector support programme in the chosen area are currently met:

- there is a Government strategy for the area whose objectives and principles are converging with those of the EU
- there is an active policy dialogue between the Government and the EC on trade related issues and more particularly on the harmonisation of the quality assurance infrastructure (legislation, regulations, institutions)
- a monitoring mechanism of the co-operation outcomes has been put in place.

##### Macro-economic policy and Public finance management

The September 2006 PEFA report assessing Ukraine's PFM system concluded that "Ukraine has in place the fundamental PFM systems for managing macro-fiscal developments and some elements for enabling strategic allocation of resources". A further assessment study confirmed that Ukraine has an effective PFM structure in spite of improvements needed in reporting and controls. To tackle these issues, the Government adopted on 19 October 2007 a PFM Reform strategy that explicitly aims at setting up modernised systems "in compliance with recommendations on governance issued by the European Commission." The World Bank is committed to financing its implementation as from 2008 through a loan estimated at US\$ 65 million.

#### 2.2. Co-operation policy of beneficiary country

Ukraine-EC cooperation in the area of trade policy and in particular the elimination of technical barriers to trade (TBT) is based on the EU-Ukraine Action Plan of 21 February 2005<sup>16</sup> and the joint Action Plan on Conformity Assessment and Acceptance of industrial

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The EU-Ukraine Action Plan of 21 February 2005 defines three priorities, which the proposed measure intends to support: (a) the approximation of Ukrainian legislation, norms and standards with those of the EU; (b) the improvement of conformity assessment procedures; and (c) the development of market surveillance capacities in preparation for the progressive participation of Ukraine in the Internal Market.

products (ACAA) of 19 December 2005. It has gained considerable momentum in 2006, thanks to the support offered by the EU to Ukraine's attempts to accede the WTO.

This framework establishes an institutionalised dialogue between the Government and the Commission on TBT issues, and requires the alignment of the national quality infrastructure with EU requirements in the areas of standardisation, accreditation, metrology, conformity assessment, and market surveillance<sup>17</sup>. Beyond legal approximation in the area of technical regulations, this framework sets also as a priority to reform and strengthen the various institutions making up Ukraine's national quality infrastructure. This objective, targeted for 2011 in the ACAA Action Plan, is seen as a condition for implementing the New Approach and the Global Approach in EU-Ukraine trade relations. In preliminary discussions on the future EU-Ukraine Deep and Comprehensive Free Trade Area agreement (DFTA), both sides have recognised that economic integration can only be achieved by tackling non-tariff barriers, seeking closer regulatory approximation and institutional dialogue.

### 2.3. Government Sector Programme

"The Ukrainian Breakthrough", the new Government programme presented on 16 January 2008, aims to establish by 2010 a system of technical regulation fully adapted to the requirements of the WTO and the EU. This goal has been already pursued, though unevenly, since 1999. New laws on standardisation, on metrology, on conformity assessment, on accreditation of conformity assessment bodies, and on consumer protection have been adopted. The upgrading of the regulatory framework is progressing: 17 EU Directives have been approximated as "technical regulations"; 22 more such regulations are under development; 4248 national standards have been aligned with EU standards, while 870 "old" standards have been repealed.<sup>18</sup>

These figures hide a contrasted picture: depending on the sector considered, the level of harmonisation varies from 6% to 46%. Such disparities stem from the two main practical obstacles to reform:

- Insufficient funding from the State budget: in spite of recent increases (+86% since 2006), they still cover only one third of the estimated funds necessary to achieve the Government's objectives in harmonisation of standards
- Insufficient number of laboratories technically competent to perform internationally recognised tests: limitations exist in terms of equipment, trained personnel, reference materials, availability of national and international comparisons, networking (blind tests), testing procedures, and, as a result, mutual recognition of certificates

Responsibility for this achievement lies both with the Ministry of Economy and the State Committee for Technical Regulation and Consumer Policy (DSSU). To provide direction to these activities, the Government adopted on 11 May 2006 a Concept paper (broad strategy), soon thereafter complemented with a White paper on the reform of the national quality assurance system developed in co-operation with civil society representatives, within the framework of "policy formulation groups".

Based on this strategic framework, the DSSU is now working out a time- and budget-bound Red Paper covering the 2008-2012 period, which will be used as an anchor for the EU-Ukrainian dialogue on quality assurance and quality infrastructure, and as a reference to design benchmarks for disbursing budget support under the proposed measure.

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<sup>17</sup> In implementation of Step 2 of the ACAA Action Plan, the Ukrainian State Committee for Technical Regulations and Consumers Protection (DSSU) has identified four priorities : New Approach directives for immediate harmonisation: Low voltage (LVD, Directive 2006/95/EC); Simple pressure vessels (Directive 87/404/EEC); Electromagnetic compatibility (EMC, Directive 89/336/EEC); Machinery (Directive 98/37/EC).

<sup>18</sup> As of today, about 30 % of the harmonisation work can be deemed done. The current agreements envisage the ACAA to be extended to cover up to 75% of all goods traded, provided both sides agree.

## 2.4. Lessons learnt

Trade-related technical assistance has proven instrumental in supporting Ukraine's WTO accession process. Therefore, a confident working relationship pre-existed in the sector, which has considerably eased talks with the stakeholders of the measure. However, in the Tacis context, these projects could only deal with certain aspects of quality infrastructure (quality management, certification, or accreditation). The political priority placed on the area and the holistic nature of the sector reform emphasise the need for a sector-wide approach. It will have to be reflected in the proper choice of the budget support indicators.

## 2.5. Complementary actions

### *Tacis projects*

The Ukraine NAP 2005 includes a EUR 9 million sector-wide action in the field of "Norms and standards" to be implemented through service contracts, supply contracts, grants and two twinning projects. The latter projects co-operate closely with the Ukrainian-European Policy and Legal Advice Centre (UEPLAC), which is the principal provider of Community assistance on legal approximation.

The TAIEX instrument has also allowed delivering workshops on practical aspects of the New Approach Directives and on Quality Management Systems in public authorities, including those forming the national institutional infrastructure for quality.

### *Other donors' activities in the sector<sup>19</sup>*

The USAID "Trade, Investment and Business Acceleration" project, which focuses on the 'demand-side' of quality assurance services: assistance to WTO accession and post-accession measures; improvement of business environment; and the streamlining of business regulations under the MDC Threshold Programme.

The International Finance Corporation -IFC- "Business Enabling Environment" project consists in surveying the impact of the national quality infrastructure on small and medium enterprises, and promoting reform of the business environment.

## 2.6. Donor coordination

Ukraine has recently established a framework for government-led donor coordination. This mechanism includes a Trade-related assistance group (Thematic group A1), led by the Government with support of the Commission as "lead donor". Frequent working contacts between the EC Delegation and the World Bank and the IFC; USAID; UNDP and smaller donors involved provide a certain degree of cohesion and coordination of efforts.

Donor coordination has made less progress in the field of PFM. The PEFA assessment of the PFM system was carried out by the World Bank. The PFM reform strategy and Action Plan are being prepared by the Government with technical assistance of the World Bank, other donors providing assistance to the Ministry of Finance and related institutions not being involved. However, the Commission is defining the PFM related conditions essential for introduction of budgetary support based on the PEFA assessment. This work is carried out in close coordination with the World Bank to ensure that unified criteria are applied.

## 3. DESCRIPTION

### 3.1. Objectives

The overall objective of the proposed measure is to contribute to economic reform and the gradual integration of Ukraine's economy into the Internal Market<sup>20</sup>.

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<sup>19</sup> An informal survey conducted among EU Member States has shown that the latter are not actively involved in this field of co-operation.

The purpose of the proposed measure is to implement policy measures to remove technical barriers to trade between the EU and Ukraine. Such policy measures include the modernisation of the institutional framework for quality assurance.

### **3.2. Expected results and main activities**

The national sector strategy contemplates the following results, which will be supported by the proposed measure:

- Approximation of the legislative framework in the sphere of technical regulation (to EU and WTO TBT requirements), including the transition from mandatory certification to conformity assessment and the separation of the conformity certification and State surveillance functions
- Set-up of a State market surveillance system
- Upgrading of domestic metrological services
- Introduction of ISO-compatible quality management systems in domestic enterprises
- Improved access by national and foreign interested parties to information on standardisation, metrology and conformity assessment
- Reform of the institutional infrastructure for quality assurance, with a view to enable it to perform and maintain over time the above-listed changes.

Activities to implement the measure will consist in setting up and running an appropriate system to monitor progress on the above-listed objectives and more specifically attainment of the agreed disbursement targets. This may imply the use of support technical assistance or specific equipment, budgeted for this purpose (section 4.3).

### **3.3. Stakeholders**

Primary responsibility for reforming the sector and therefore removing TBTs in EU-Ukraine trade lies with the Ministry of Economy and the State Committee for Technical Regulation and Consumer Policy (DSSU), a central executive body reporting to the Ministry of Economy. The National Accreditation Agency (NAAU) and the future National Standardisation Body to be established in the course of the structural reform will also play a key role in implementing the measure. These institutions generally need strengthening of their institutional capacity to refine, maintain, and monitor reform in their fields of responsibility. External capacity support will be provided in the form of technical expertise, whereas capacity-building twinning projects are already underway with DSSU and NAAU.

The wider target group of recipients includes the sectoral standardisation bodies (Ministry for Agrarian Policy, Ministry of Housing), organisations (conformity assessment bodies; fundamental and industrial metrology bodies; market surveillance authorities; scientific and training institutions) and groups of professionals (industrial and professional associations)<sup>21</sup>.

### **3.4. Risks and assumptions**

#### Assumptions

- Ukraine will keep up to its commitments under the TBT-related chapters of the EU-Ukraine Action Plan and the preliminary ACAA agreement, and will continue demonstrating heightened interest in the proposed measure, as during the formulation phase

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<sup>20</sup> NIP 2007-2010, Priority Area 2 “Support for regulatory reform and administrative capacity building”, Sub-priority 1 “Trade facilitation and improving the investment climate”.

<sup>21</sup> These various groups of potential stakeholders have been consulted during the formulation phase of the proposed measure.

- Ukraine will not substantially revise the objectives of its quality assurance reform strategy, and its government will be willing to pursue the reform path, translating it into concrete policies.

#### Risks

- One or several of the ministries, agencies or companies involved in the project will obstruct cooperation, or will prove unable to cooperate in an ordered manner. This risk can be mitigated via the use of the established dialogue mechanisms under the PCA and its contemplated successor agreements, and the provision of tailored assistance.
- The changes required under the AAP 2007 budget support to the reform of the energy sector to align the Ukrainian public procurement system with EU rules may be delayed for political reasons. To a certain extent, this risk can be reduced through a strict monitoring of the AAP 2007 budget support operation, as well as through a timely implementation of the Tacis NAP 2006 Public finance management reform measures.

### **3.5. Crosscutting Issues**

The cross-cutting issue of good governance is integrated into the proposed programme, through the alignment of market regulation rules and practices with EU rules and best practices.

Besides, a well-conceived quality infrastructure system is an invaluable input to long-run environment conservation and consumer protection. Besides the related economic development, implementation of the proposed measure will result in linking directly environmental factors to business competitiveness and improving access of Ukrainian consumers to goods manufactured to high levels of safety and quality.

The proposed programme has no identified impact on gender equality, although the expected greater involvement of civil society organisations in implementation of the proposed measure should indeed lead to the increased participation of women in decision-making processes related to standardisation and consumer protection.

## **4. IMPLEMENTATION ISSUES**

### **4.1. Implementation method**

Untargeted budget support programme, centrally managed.

### **4.2. Procurement and grant award procedures**

All contracts implementing the action must be awarded and implemented in accordance with the procedures and standard documents laid down and published by the Commission for the implementation of external operations, in force at the time of the launch of the procedure in question.

The essential selection and award criteria for the award of grants are laid down in the Practical Guide to contract procedures for EC external actions. The maximum possible rate of co-financing for grants is 80%. Full financing may only be applied in the cases provided for in Article 253 of the Implementing Rules of the Financial Regulations where financing in full is essential to carry out the action in question.

All programme estimates must respect the procedures and standard documents laid down by the Commission, in force at the time of the adoption of the programme estimates in question.

### **4.3. Budget and calendar**

- |   |   |            |
|---|---|------------|
| – Budget support (maximum):               | € | 39 million |
| – Related technical assistance (maximum): | € | 6 million  |

The budget support will be disbursed as follows: a fixed tranche of €12 million within 3 months following the signature of the Financing Agreement, and three variable tranches of

respectively €10, €9 and €8 million maximum each, by the end of the 18<sup>th</sup>, the 36<sup>th</sup> and the 48<sup>th</sup> month following such signature. Variable tranches are to be released subject to the matching of agreed indicators, to be agreed with the main partners. Implementation will be supervised by a joint Monitoring group, to be supported with ad-hoc technical assistance. The technical assistance component will include an indicative allocation of 0.5M€ for Evaluation, Audit, and Visibility actions.

The programme will be implemented within 48 months after the signature of the Financing Agreement.

#### **4.4. Performance monitoring and criteria for disbursement**

Performance monitoring will be exerted by a Joint monitoring group whose basis has been laid down with the establishment of the ACCA contact group partnering the Ministry of Economy and the European Commission. The larger Joint monitoring group will rely on official information provided by Ukraine and verified as appropriate.

Disbursements of the tranches will be contingent on the continuous implementation by Ukraine of a sound macroeconomic and financial policy and on the adoption and effective implementation of an Action Plan for improving the Public Finance Management system. It will also be related to monitored progress towards achieving a set of benchmarks in quality infrastructure reform. Performance indicators will typically include:

- For the fixed tranche: sound macroeconomic policy; certified and funded PFM reform strategy; established Joint monitoring group based on satisfactory and workable intra-Ukrainian arrangements; proven progress in implementation of the relevant actions of the EU-UA Action Plan and the Action Plan on ACAA.
- For the variable tranches: a maximum of 10 indicators related to PFM and quality infrastructure reform implementation. A combination of follow-up of adopted measures; impact indicators and outcome indicators related to implementation of the quality infrastructure reform will be defined for that purpose.

#### **4.5. Evaluation and audit**

The measure will be subject to regular monitoring by the joint Monitoring group. A specific mid-term evaluation will be organised to check the overall validity of the monitoring system.

Evaluation of the results achieved will be entrusted to independent consultants, as well as external audits (which will be carried out if necessary). Evaluation and audit will be funded out of the technical assistance component of the programme.

#### **4.6. Communication and visibility**

The programme will follow the orientations of the Manual on Visibility of External Actions (e.g., press release at the signature of the FA, visibility for reports and studies, etc).

Proper communication and visibility of the action will be achieved via regular joint communication events on the occasion of the achievement of the disbursement criteria, as well as in connection with the results of technical assistance projects in the energy sector. A reasonable communication budget will be set aside, to be funded out of the “technical assistance” budget, for promotion of the measure throughout its lifetime.

## ACTION FICHE FOR UKRAINE - ENPI AAP 2008

### 1. IDENTIFICATION

Title	<b>Twinning and ENP Support Technical assistance</b>		
Total cost	<i>EC Contribution - EUR 23.6 million (including EUR 2.6 million allocated from the Governance Facility)</i>		
Aid method <i>Management mode</i>	Project approach (twinning and technical assistance) <i>Centralised management</i> <b>CRIS n. 19596</b>		
DAC-code	<b>43010</b>	Sector	<b>Multisector aid</b>

### 2. RATIONALE

#### 2.1. Sector context

On 21 February 2005, the European Union and Ukraine signed a three-year Action Plan foreseeing the achievement of ambitious objectives in a large number of sectors and activities. Both sides entered into negotiations on a New Enhanced Agreement (NEA - the successor to the Partnership and Cooperation Agreement) in March 2007 and in February 2008 they launched negotiations on a future Deep and Comprehensive Free Trade Area agreement as a key element of the NEA, building up on the Action Plan's achievements. Also, at the Cooperation Council in March 2008 it was agreed to keep the Action Plan in place for one more year. It will then be succeeded by a new instrument which will prepare the entry into force of the NEA. In the past three years of Action Plan implementation, insufficient administrative capacity and understanding of Community rules and administrative functioning have come to the fore as significant blocking factors on Ukraine's path towards economic integration into the EU Internal Market, which is the stated major objective of the above-mentioned agreements.

The proposed measure aims therefore at strengthening the capacity of the Ukrainian administration to face the implementation and integration challenge. In areas where, by anticipation, discussions with the Ukrainian Government have underlined the need for sector-wide assistance (such as the reform of the law enforcement system, including the fight against corruption; the reform of the judiciary; environment; and transport), the proposed measure envisages the delivery of preparatory technical assistance. Such assistance will aim at drawing conditions from Ukraine's sectoral reform and development strategies and, where necessary, at helping Ukraine devise such strategies, in line with the Ownership objective of the Paris Declaration, to which Ukraine is a signing party.

The proposed measure should therefore allow for:

- A timely and cost-effective implementation of Ukraine's commitments under the above-mentioned documents, putting an emphasis on priority sectors selected in view of possible future budget support operations or stated priorities of the Ukrainian Government, as reflected in the conclusions of the Twinning Co-ordination Group<sup>22</sup>;
- A timely and efficient preparation of future sector-wide support in jointly identified priority areas for proper EU-Ukraine Action Plan and Deep and Comprehensive Free Trade Area agreement implementation;

<sup>22</sup>

This group, established in February 2006, comprises the Twinning PAO, the Ministry of Economy (overall coordinator of external assistance to Ukraine) and the Commission, represented by its local Delegation. The Group's main purpose is to weigh requests for twinning against the priorities of the Action Plan. A priori, and non exhaustively, priority sectors should include: public finance management system; judiciary reform; law enforcement reform; trade-facilitating sectors (quality assurance infrastructure; customs; statistics; intellectual property rights...); environment; transport; and energy.

- An eased political dialogue for further enhancement of neighbourhood relations, based on the successful realisation of joint objectives defined in bilateral agreements.

Worth is noting, at this stage, that nearly all other donors and IFIs have already agreed to use the commitments and objectives set forth in the EU-Ukraine bilateral agreements as a basis for designing their own aid conditionalities or projects in the relevant sectors. Ownership by Ukraine of these same objectives, which are designed together in the context of a political dialogue, is not questionable.

## **2.2. Lessons learnt**

The measure focuses on raising Ukraine's chances of achieving the key objectives without which its political dialogue with the EU will likely lose momentum, as a consequence of insufficient implementing capacities. The project draws on past experience and on-going projects, be they funded by the Community or other donors. The delivery methods have been chosen based on recent positive experience with twinning projects (more than 30 twinning projects are now on-going or under preparation, starting from zero less than two years ago, and new requests for twinning projects flow in at an accelerated pace), and the successful use of preparatory assistance for designing sector-wide support (for instance in the agricultural, transport, financial services or energy sectors). The results expected from sector-wide studies foreseen under previous Action programmes for Ukraine have been given due consideration, as well as the need to further past or on-going assistance, where appropriate.

## **2.3. Complementary actions**

As experience has shown for the last two years, there is a clear correlation between the areas identified as priority ones in the unofficial Action Plan Implementation Tool and the sectors whose responsible Ministries and Agencies have been the most active in requesting twinning and other interventions. In this context, twinning projects are usually defined as a component of a larger sector-wide support programme (where activities are sometimes implemented in a coordinated manner with other actors such as the World Bank) or as a precursor project for further definition of a sector-wide programme. Each of them can therefore be seen as complementary to other actions, past or future, in the same sectors, including technical assistance to be designed within the framework of the proposed measure.

## **2.4. Donor coordination**

Other donors and IFIs have generally agreed to use Ukraine's commitments set forth in the EU-Ukraine Action Plan as a basis for designing their own aid conditionalities in the relevant sectors, thus ensuring consistency of external assistance. In addition, all Donors and IFIs (including USAID) are co-ordinated via the Donor-Government Working Group recently established and run by the Ministry of Economy of Ukraine.

## **3. DESCRIPTION**

### **3.1. Objectives**

#### Overall objective:

To meet the objectives of the EU-Ukraine Action Plan and prepare for future implementation of the NEA and the Deep and Comprehensive Free Trade Area agreement.

#### Specific objectives:

- To build the capacity of the Ukrainian ministries and agencies to comply effectively with the commitments set forth in the EU-Ukraine Action Plan, the NEA and the Deep and Comprehensive Free Trade Area agreement, as well as in their national reform and development programmes (respecting the priorities referred to in Footnote 1)
- To prepare Ukraine to, and support implementation of, the Deep and Comprehensive Free Trade Area agreement in sectors identified as key for its success (like WTO SPS, Quality assurance, Market infrastructure)

- To prepare the introduction of sector-wide support, in whichever form, in the sectors recognised as priorities (see Footnote 1 for a list of priorities as at the beginning of 2008).

### **3.2. Expected results and main activities**

The last available OECD/SIGMA analysis of Ukraine's public service (June 2006) identifies the lack of administrative capacity as the main weakness behind the country's difficulties in streamlining its reforms and abiding by its international commitments (including those undertaken within the framework of bilateral relations with the EU). The proposed measure will address this weakness using, as appropriate, the advantages offered by the twinning modality or by technical assistance. Improved administrative capacity will be achieved by improving the ability of the Ukrainian civil servants to understand and make use of EU concepts, and adapting the institutional structure to the requirements stemming from the bilateral agreements (e.g. participative dialogue with EU and international partners, elimination of functional conflicts of interest, modernisation of the scopes of responsibilities and decision-making procedures, involving changes in sector supervision and management practices).

As a result, the proposed measure will yield EU-compatible sector-wide strategies in the areas critical to achieve the objectives of the bilateral agreements (and where Ukraine is currently seeking to achieve substantial reform), and provide the tools for their implementation, possibly with the help of sector-based donor assistance. It will also, in particular, allow using a systemic approach towards legal approximation, departing from the textbook approach, helping to achieve in due time the critical mass of approximated legislation required by the bilateral agreements.

### **3.3. Stakeholders**

The key stakeholders will be the concerned industries and society groups, policy-setting and implementing ministries and agencies and also, though indirectly, the community of donors. The proposed measure will impact first and foremost on the policy-setting and implementing agencies; however enforcement of EU-compliant procedures should rapidly lead to involving the civil society and businesses. Ukraine is characterised by a rich, though under-developed, civil society and business infrastructure, whose development the projects should foster. As for twinning, all Ukrainian government entities, including regional ones, are potential stakeholders.

### **3.4. Risks and assumptions**

#### Assumptions:

- The European Union pursues its ENP policy and enhanced cooperation with Ukraine in priority sectors (see Footnote 1)
- Ukraine pursues its objective of improved relations and economic integration with the EU, maintains its trend of increased co-financing of cooperation projects with the EU, and pursue its efforts to modernise its administration
- The Government continues its donor coordination effort and supports improvement of decision-making processes in line with European practice
- Ukraine will go on with its administrative reform, thus creating the pre-conditions for retaining civil servants in public administration after implementation of the measure.
- It is also assumed that the Ukrainian beneficiaries will contribute to the logistical arrangements in order to ensure the successful implementation of this programme

#### Risks:

- The Ukrainian Government repeals its July 2006 decision to cancel the Administrative provisions limiting the presence and access to premises and information of foreign

advisers in ministries and Government agencies

- The Ukrainian Government does not improve the material conditions for the preparation and implementation of twinning projects, with particular reference to language training, the stability of persons in charge on behalf of Beneficiary administrations, the adequacy of premises, or the timely earmarking of funds for co-financing
- The Government does not provide sufficient political support to the reform processes supported by the twinning or technical assistance projects designed under this measure
- The Government does not complete the necessary steps to receive budget support under AAP 2007 and 2008.

### **3.5. Crosscutting Issues**

Coherence with the cross-cutting issues can be characterised as follows:

- Good governance and human rights: Improved administrative capacity and rendering it aware of EU policies and systems will raise the democratic standards of governance; preparing a budget support for law enforcement system, implying improved wider and systematic consultation of the civil society and businesses, will take Ukraine a major step forward to democracy at central government level; the monitoring by civil society organisations will be a guarantee of setting up an efficient and stable surveillance of the law enforcement system.
- Gender balance: The proposed measure has no direct impact per se on gender balance. However, certain activities funded by the measure may be designed to tackle gender inequality, or may have otherwise an impact on this issue. To be noted is the current gender imbalance in the Ukrainian Government, where about two thirds of the employees are female. At decision-making level, however, this imbalance does not exist: in the central Government, as at the end of 2006, 1643 heads of departments (and higher ranks) were male, whereas 1663 were female, for the same level of remuneration.
- Environment: The measure will specifically prepare future sector-wide support in the environment sector, as one of the identified priorities for EU-Ukraine Action Plan implementation. In addition, promoting gradual convergence with EU *acquis* on the occasion of regulatory reform (via twinning projects) will impose the ex-ante evaluation of the impact on the environment of decisions likely to bear on it.

## **4. IMPLEMENTATION ISSUES**

### **4.1. Implementation method**

The implementation method for this project for all components will be centralised management by means of service contracts, supply contracts, grant contracts and twinning contracts.

### **4.2. Procurement and grant award procedures**

All contracts implementing the action must be awarded and implemented in accordance with the procedures and standard documents laid down and published by the Commission for the implementation of external operations, in force at the time of the launch of the procedure in question.

### **4.3. Budget and calendar**

Each project component will include its own provision for evaluation, audit and visibility. The indicative breakdown of the budget would include : component 1 – twinning projects 16.8M€ component 2 – sectoral technical assistance 6.6M€ including an indicative provision for evaluation and visibility of 0.2M€

It is foreseen that all the operational duration of the project will be of 48 months after the signature of the Financing Agreement.

#### **4.4. Performance monitoring**

The monitoring of the measure will follow standard procedures, based on benchmarks to be agreed during the preparation of each of the sub-projects to be defined under the measure, in co-operation with the Ukrainian government and civil society representatives and, in the case of twinning, based on the mandatory results agreed during the project preparation phase.

There is no standard indicator applicable to the DAC sector code of the proposed measure. It is proposed to use a modification of Standard indicator 407 “Scope of capacity-building actions”, considered at central government level, to assess global project performance, given the measure’s general focus on improving government administration. The performance of the proposed indicators (see annex) will be monitored based on a periodic assessment of progress and delivery of specified project results and towards achievement of project objectives. Harmonisation of monitoring frameworks of other Donors is expected to be one of the outcomes of the government-led coordination process referred to in section 2.4.

#### **4.5. Evaluation and audit**

In addition to regular ROM, a mid-term evaluation of the entire measure will be organised. Each of the sub-projects to be defined under the measure will undergo financial audit, as foreseen by the standard procedures, which foresee that such audit be properly budgeted under each of such sub-projects.

#### **4.6. Communication and visibility**

Proper communication and visibility of the measure will be achieved via widespread dissemination of project achievements and results (to be budgeted under each of the activities), as well as international visibility of twinning projects, for which a specific budget will be allocated (section 4.3).