

ANNEX 1 - ACTION FICHE UKRAINE AAP 2011

1. IDENTIFICATION

Title/Number	Support to Ukraine's Regional Development Policy CRIS: ENPI/2011/022-825		
Total cost	EU contribution: EUR 20 million		
Aid method / Method of implementation	Direct centralised management		
DAC-code	15110	Sector	Economic and development policy/Planning

2. RATIONALE

2.1. Sector context

It is of major importance for the European Union and its Member States to work in the area of Regional and Local Development with its partners of the Eastern partnership and, more particularly, with Ukraine, in order to support, as underlined by the recent Joint Communication "*A new response to a changing Neighbourhood*", an inclusive economic development, reducing social and regional inequalities and creating higher standards of living for its people. This is particularly true in the case of Ukraine, an extremely rich and diversified partner country in economic, social, cultural and political terms, a diversity that needs to be acknowledged in order to promote its development in a sustainable way and to guarantee, at the same time, that this diversity is compatible with the necessary social and regional cohesion that any country legitimately requires and demands.

The deepening of EU-Ukraine relations in the context of the Eastern Partnership will include significant economic integration of Ukraine with the EU. In order for Ukraine's economy to fully benefit from the opportunities of a future Association Agreement with a Deep and Comprehensive Free Trade Area as an integral part, efforts of modernisation will continue to be undertaken. This is likely to involve certain restructuring, which will affect the regional level and regional development efforts. In this context, the European Union adopted very recently its Guidelines on Pilot Regional Development Programmes (PRDP), shared with its Eastern European Partners, where a comprehensive number of general principles are drawn up in order to implement actions in the area of regional development. This action is a first response to the PRDP principle under the Eastern Partnership.

During the last ten years before the break out of the international financial crisis, Ukraine has experienced an important phase of economic growth. Nevertheless, the living conditions of the population have not equally improved. According to the Ukrainian Ministry of Social Policy and Labour, in January-September 2010 26.4% of Ukrainians (or 12.5 million people) were living under the poverty line. In addition, 9.5 million people lived on income below the living wage. Ukraine is ranked 69th out of 169 countries in the 2010 UN Human Development Report.

Increasing social and regional disparities create risks of social discontentment in a country with notorious cultural and political regional and local cleavages. Worth noting is that not only interregional disparities are growing, but also disparities between urban and rural areas and, within urban areas, between the wealthy and prosperous districts (generally located in the centres of big cities) and the outskirts (sleeping towns, etc.). These developments will have important political effects in the short and medium term.

Despite growing socio-economic intra- and inter-territorial disparities, Ukraine has not implemented successfully, until now, any substantial regional development policy in order to address those important challenges. The Ukrainian Regional Development system can be characterized as rather fragmented and ineffective, and mainly based on the efforts of the international cooperation.

The process of decentralisation of powers and competences is rather limited, *de jure* and *de facto*. Regional decentralised authorities (Regional Councils) have almost no significant competences, while, at the level of regions (Oblasts), Governors (nominated by the President) and its Oblast Administration play a major role in establishing the regional development economic plans and in the choice of major investments (like infrastructures). The Oblast Administration is almost unavoidable for any kind of ambitious development plan for the region. On the other hand, City Administrations and Municipal Authorities enjoy a limited but effective level of decentralisation, even if their budgets are insufficient to cope with all challenges local authorities are deemed to address. Nevertheless, despite the limited level of decentralisation, for identical levels of formal powers and competences, the situation in Ukraine is not uniform, and some municipal authorities are able to push the limits of their self-government to unexpected levels, mainly based on the possibilities offered by the international cooperation or their own institutional efforts. The situation, in this regards, differs a lot from region to region (especially between the East and the West of the country, with a special situation for the Autonomous republic of Crimea), due to historical and cultural reasons, but also due to current political developments (a more cooperative dialogue between Governors and Majors of big cities can have very positive effects, for example).

With few exceptions, regional and local authorities lack the institutional (and sometimes even technical) capabilities and budgets to implement their own policies and are heavily dependant on decisions and transfers from the central level (from Governmental departments). Consequently, there are on all levels low capacities for the management of regional and local development. A major challenge is not only the design of new policies and of a financial instrument, but especially the identification and implementation of projects. In this regard, the necessity for capacity building in project management and needs assessment is especially evident at the level of municipalities which is closest to the citizens and their problems, and at the level of regions (especially oblasts), where most of the planning processes are originated and where national resources are collected.

At the national level, Government changes and administrative reforms in the last years have led to institutional instabilities and changing distributions of competences among different Ministries. In December 2010, a new reshuffle has been taking place and, for the time being (May 2011), it has not been officially decided which governmental body will take the responsibility for regional development in the future (either the Ministry of Regional Development or the Ministry of Economy). On 1.06.2011 the President of Ukraine dismissed Viktor Tykhonov as Ukraine's Deputy Prime Minister and Minister of Regional Development, Construction, Housing and Municipal Economy who was appointed in December 2010.

The Ukrainian side has repeatedly stressed the wish to align its Regional Development System with EU best practices. In a recent meeting with the Council of Regions, President Yanukovich expressed the intention to create a state fund for regional development and to adopt a new law on State Regional Policy. This political declaration explicitly mentioned the need to reform the "management of regional development" and stressed that the fund should follow EU best practices. The Ministry of Regional Development, Construction and Municipal Economy has been requested to elaborate a concept for the fund and suggested that the EU model of IPA (Instrument for Pre-Accession Assistance) may be followed.

At the institutional level, important actors and stakeholders agree on the importance of regional development for the country. Nevertheless, there are consistent disagreements about the institutional responsibilities and the operational implementation of a regional development policy. This lack of coordination and interaction between different regional development stakeholders prevents a consensus on the issues and has been a major obstacle to reforms in the past. Therefore, future commitments with the EU should help to achieve a sustainable consensus among key stakeholders. In this sense, the Government has repeatedly expressed a strong interest for the budget support instrument to regional development.

EU's contribution will take into account economic areas and regions where there will be restructuring processes linked to Ukraine's economic integration with the EU, and the challenges and opportunities that this will entail. Regional and local development plans financed by the EU should, therefore, support some of the following areas of intervention directly linked to the communal and regional competences:

- The housing sector (essentially the renovation of multi-apartment buildings), in order to ameliorate the living conditions of citizens.
- The social services connected to the health care system, today in a dramatic situation in most of the country.
- The solid waste treatment, a major environmental problem at communal level.
- The social services of proximity, some primary social care services delivered at local level.
- The protection of local and regional cultural heritage.
- The promotion of sustainable and inclusive regional and local economic plans.
- The enforcement of programmes to ameliorate local governance and the relations with citizens at communal and regional level.

2.2. Lessons learnt

The project draws on past experience, on-going projects and, on the feedback provided by the beneficiaries. None of three dimensions of regional policy (social, economic, territorial) have been totally absent from our cooperation with Ukraine. Nevertheless, until very recently, those issues have never been a priority (the recent Global Evaluation of our assistance underlines this aspect) and not been addressed in a comprehensive way. The reasons for that situation are various and complex: the so-called "historical" legacy of soviet times that promoted the opinion that social and regional issues would not be a priority in times of "liberalisation" and economic reform, the priorities fixed by the EU Assistance, the lack of priority given by successive Governments of the country, etc. But 20 years after the Declaration of Independence and the collapse of the Soviet Union, those issues have become major challenges. Further, those problems have proved to be persistent and affect the economic and political development of the country, the successive governments having reacted mainly in a fragmented way.

Specific regional and local development projects financed in the past, have had, by nature, only a limited capacity to disseminate experiences and best practices to all regions and municipalities of the country. There is, therefore, a need to implement a systematic step-by-step approach related to deepening the capacities in all regions and for all local authorities, and to balance the efforts by favouring, in a second phase, those who have never had the possibility of being confronted to the proper management of their own development.

Capacity building measures have mostly concentrated on short-term trainings and were offered to institutions and organisations instead of offering them to individuals to help their personal career development to ensure a long-term build up of knowledge, expertise and skills. Giving the high level of staff turnover in the Ukrainian administration (especially the local and regional) the prevailing approach to training prevents a sustainable capacity building for regional development.

The prevailing regional development planning methodology in Ukraine does not establish a link between limited resources and development needs. Very often Regional Development strategies and regional programs are elaborated based on academic expertise "ex cathedra", but without involvement of stakeholders and concrete implementation plans and budgets. The promotion of a dialogue, in order to promote realistic development strategies will be a key element of the new project. Further, the new project will support implementation and monitoring of strategies, based on a learning by doing method.

In spite of the general observation that institutional and absorption capacities in the regions are generally very low, there are on the local level good practices and experiences in understanding main mechanisms for development of specific areas. These lessons have to be taken into account.

A lack of coordination and interaction between different regional development stakeholders has been a major obstacle to reforms in the past. Therefore, future project should promote cooperation, networking and exchange between all major stakeholders and increase horizontal and vertical linkages. The final goal is to achieve consensus.

Projects combining "soft" (capacity building/ technical assistance) with "hard activities (funding of projects) have proved be effective, since they gave the possibility to implement what was "learnt" and/or supported "learning-by doing".

2.3. Complementary actions

The EU has supported Ukrainian authorities in the past five years through different types of projects.

The EU has already financed a long term Technical Assistance Project to support Regional Development Policy in order to develop an EU-compatible approach and a financial instrument for regional development. This project initially focused on the provision of TA support at central level. Later, it was very active in supporting, for example, the elaboration of the Support Programme of the Joint Cooperation Initiative for Crimea (JCIC), our first comprehensive approach to regional development in the country. In addition, almost all the other regions of the country have already benefited from this TA support in order to ameliorate their institutional capacities in planning, but few have already drafted and approved a regional development plan. This proposed new programme should therefore be a continuation of the above mentioned TA project, and should base its work on the activities already implemented. In addition, this new programme should also help in enforcing the operational concept "learning by doing", as established in the above mentioned Guidelines for PRDP.

The EU also supports and finances development programmes in the area of local rural development, based on a participatory/community based approach. It owns a large experience in the so-called decentralised cooperation, in which several projects are financed through relevant programmes like CIUDAD, Cross Border Cooperation or the Non State Actors and Local Authorities programmes. Generally speaking, those EU Programmes follow bottom-up approaches and promote the concept and principles of self-government or autonomy of local authorities.

Some of the main complementary actions are summarized below:

- *A Memorandum of Understanding for the Establishment of a Dialogue on Regional Policy and Development of Regional Cooperation* has been signed between the Ministry of Regional Development and Construction of Ukraine and the Directorate Regional Policy of the European Commission. The Memorandum is (theoretically) implemented by an annual work plan.
- The *Community Based Approach project* mobilises local communities around their development priorities. A second phase of CBA II (AAP 2011, EUR 17 million) has been signed on the 31/05/2011.
- 5 CIUDAD projects with Ukrainian partners have been selected. The aim of CIUDAD Programme is to modernise and strengthen local and regional governments in order to enhance democratic governance and sustainable development through partnerships between local authorities in the EU and in the ENPI region.
- *Neighbourhood investment facility: Technical Assistance Support for Ukrainian municipalities (ENPI 2008, contribution agreement of EUR 5 million):* The project provides technical assistance for EBRD investment in selected municipalities in the water, district heating, and urban transport sub-sectors.

- *Support to Sustainable Regional Development (SSRD)* (2006 National Action Programme starting in July 2008) adopting a comprehensive approach at strategy, instrumental and implementation levels.
- The *Joint Cooperation Initiative in Crimea* consists of a core package of technical assistance focusing on capacity/institutional building for regional development funded by the European Commission, plus sector-based support/investment projects by EU Member States. The European Commission and a group of interested Member States are working together in Crimea on a wide range of issues in a co-ordinated and harmonised way.
- *ENPI Cross-Boarder-Cooperation programme 2007-2013*: Ukrainian regions are eligible for three CBC programmes (Black Sea Basin, Poland-Belarus-Ukraine, Romania-Ukraine-Republic of Moldova)

The overwhelming majority of donors active in Regional Development finances projects targeted at the local level (e.g. USAID, CIDA, SIDA, the Swiss Agency for Development and Cooperation, GIZ Ukraine Office).

2.4. Donor coordination

During the period 2006-2010, with the support of the EU, an active working group for donor coordination on Regional Development was established. The Government of Ukraine is now finalising the mechanism of donor coordination, in particular by defining political and technical levels of such coordination. If this process is finalised, donor coordination activities will be re-launched under the auspices of the relevant Minister. Otherwise, the EU Delegation will activate this process in cooperation with other donors interested in this policy in order to ensure a good coordination between donors.

The previous EU Support to Sustainable Regional Development project carried out a thorough donor mapping study. The study clearly shows that no other donor undertakes a systematic sector-wide approach to regional development in Ukraine. This makes the role and the leadership of the EU in this field even more important.

The proposed action is fully compliant with key principles of the Paris and Accra Declaration on Aid Effectiveness and EU commitments on development. Consultations with all main donors have been held in the formulation stage of the project.

3. DESCRIPTION

3.1. Objectives

Overall objective:

To contribute to the social, economic and territorial cohesion of the country.

Specific objective:

To strengthen the capacity of Ukrainian authorities and other stakeholders to develop and implement effective regional development policies.

3.2. Expected results and main activities

This project has to be understood in the framework of a long term strategy to support Regional Development. It is the second project of a series of actions that will assist Ukraine to develop and finance a comprehensive regional policy. It will take into account the context of its economic integration with the EU.

The action will be divided into two components. The first component will be carried out by a technical assistance project which will provide institutional support and capacity building. This project will work nationwide. The second component provides a budget to support the financing of regional policy of Ukraine and, most specifically, regional and local development programmes in the country, in regions and municipalities duly identified in accordance with relevant criteria pertaining to the best standards of a regional development policy. Both components will be closely linked to facilitate a learning-by-doing approach. The technical assistance project (first component) will also support the implementation of the regional development programmes and the disbursement of funds.

Therefore, this new programme is building on the results of work already done in regard to regional policy recommendations for Ukraine; however it will carry the EU support in this field further towards implementation of concrete regional development projects. For that purpose, the foreseen budget of EUR 20 million provides both: a technical assistance component (EUR 6 million) and a financial support component (EUR 14 million), which will be used as direct co-financing for a new financing mechanism for regional development projects in Ukraine. Technical Assistance will be provided to support coordination, participation and consensus building at the national and regional levels in regard to regional development policies, measures and managements structures as well as to help introduce a new inclusive and more effective approach for capacity building in this area.

Expected results

- i) A National Policy on Regional Development elaborated by the Government, including the legal and administrative instruments necessary to operate it (Regional Development Fund or other options).
- ii) An Action Plan on Regional Development elaborated and approved.
- iii) Pilot Regional Development projects implemented.

Indicative list of main activities

Component 1: Institutional support and capacity/Technical Assistance (EUR 6 million)

- § Mobilization of task forces (with participation of Ukrainian decision makers, local and international experts and donor representatives) to help build consensus among key stakeholders in the area of regional and local development and facilitate "consultancy tailored upon demand";
- § Support to the updating and implementation of well coordinated national and regional development strategies (operational plans, budgeting), enabling identification/formulation, implementation/financing, monitoring/evaluation of projects;
- § Support to local and regional promoters of projects along the whole cycle;
- § Support to the management and disbursement of funds, including the national, regional and local level, with special attention to the EU rules, regulations and systems;
- § Improving the capacity building system for stakeholders using networking and following a long-term and personalized approach (coaching, training, updating curricula, training of trainers, certification of trainers, development of a compulsory training module for staff of regional and local administrations in Ukraine, project cycle management, etc.
- § Support the systematization and institutionalization of trainings.
- § Communication activities regarding funding activities (component 2).

Component 2: Financial support (EUR 14 million):

- § The second component supports through Calls for proposals the financing of regional and local development plans, unless the conditions allowing the setting-up of a budget support are fulfilled by the Ukrainian authorities. (see below)
- § The principle of co-financing by Ukrainian national or local authorities of regional plans or specific local and regional actions will be promoted.

3.3. Risks and assumptions

Assumptions:

Ukrainian authorities (at national and local level) will remain committed for delivering improved regional development policies. Promotion of regional and local development and of an administrative-territorial reform will remain a national priority and the Government ensures a stable institutional environment for its implementation.

National/Regional/Local stakeholders are open for full cooperation within the programme. Local and regional authorities will be granted with greater financial autonomy, as well as greater financial visibility and capacity in the mid-term.

Risks:

Uncertainties about entities and personnel in charge of Regional Development, at the national level, have hampered the formulation of the project (medium). Nevertheless, at regional and municipal level, several consulted authorities are active and ready to implement regional development plans and activities **Risk Mitigation:** If the government shows commitment and the regional fund is created as promised, the financial support could be provided in the form of a budget support to a sector wide approach. Ways of channelling the funds to the local and regional authorities, from the national budget, do exist and are normally used by national authorities. However, in case the main pre-conditions of a budget support are not fulfilled, the EU would then finance pilot regional development projects in several regions and cities, through calls for proposals. Pilot regions would be selected according to defined criteria, using a competitive approach.

The Government or Parliament will not approve any major reform on the Regional Development until the program will start (Medium). **Risk Mitigation:** In case the regional development system will not change, the project will have to concentrate on capacity building and implementation activities at the local and regional level. Regional and local authorities can achieve the implementation of self development programmes without legislative changes.

Political instability may continue in the country leading to less than full cooperation from the elected/government authorities on national, regional, local level (Medium). **Risk mitigation:** The objective of the programme is to have a wide impact at all levels of development. A step-by-step strategy approach, using a mix of cooperation and competition, has proved to be successful in previous projects to convince stakeholders to cooperate.

The continuation of the economic crisis provokes weaknesses in providing a transparent and comprehensive financial framework for the regions and the municipalities in the short and medium term (medium). **Risk mitigation:** Continuous dialogue with the authorities and strengthening of coordination processes should lead to a better assumption of financial responsibilities within state authorities toward regions and cities.

3.4. Crosscutting Issues

Putting in place policies and framework for Regional Development will per se tackle the issue of good governance. The project's activities should lead to an increased involvement of civil society into the

regional and local planning process. Cooperation, coordination and networking will be promoted by the project. Participation of local and regional actors (bottom-up) into policy making on the national level will be strengthened. Participatory platforms and capacity building networks will be explored and supported within the scope of the project as well as other direct modalities of participation when possible.

The stakeholders are not only administrative authorities, but the civil society as well. The civil society organisations will be invited to participate in coordination and consensus building measures, as well in capacity building networks. Through the financing of regional and local development projects, various crosscutting issues are likely to be tackled (e.g. environment/climate change through energy efficiency projects, gender issues in the framework of the amelioration of living conditions of the citizens, etc...).

3.5. Stakeholders

Regional and local development is a multi-dimensional issue covering a number of policy areas. Stakeholders included are:

§ *Central government:* Ministry of Economic Development and Trade, Ministry of Regional Development, Construction Housing and Municipal Economy, Cabinet of Ministers, Ministry of Finances, Presidential Administration, etc.

§ *Local authorities* at Oblast, rayon and municipal level.

§ *Other national & local stakeholders:* Institutes, business and other associations, NGOs, education institutions, etc.

§ *Donors and international organisations:* USAID, GIZ, WB, UNDP, CIDA, Swiss cooperation, EU, EBRD, etc.

4. IMPLEMENTATION ISSUES

4.1. Method of implementation

Component 1: Direct centralised management for the technical assistance component.

Component 2: The EU should, for this second component of the programme, enforce a financial mechanism allowing the financing of actions and development plans in the regions and municipalities, to be managed by the relevant local authorities. Taking into account the principles underlined in the *Guidelines for the preparation of Pilot regional Development programmes under the Eastern Partnership*, the first option for implementing this component will be the direct financing of projects through Calls for Proposals and the signature of Grant Contracts. Although the EU Delegation is responsible for the financial support (Component 2), the Technical Assistance (Component 1) and the Ukrainian Ministry in charge of Regional Development will need to assist in every aspect of the management of the fund, including the preparation for call for proposals, evaluation and selection. As a budget support is foreseen for AAP 2012, the project should pave the way towards its smooth implementation.

Nevertheless, it could be also an option to expedite the start of the budget support in case the negotiations will progress fast and be backed by a solid policy dialogue with the relevant Ukrainian Ministerial Department¹. In that case, general conditions for sector budget support will apply and the following minimum specific conditions: i) the adoption, by Law, of the National Regional Development Fund; ii) the adoption, by secondary or administrative legislation, of the rules governing the financial and operational management of that Fund (incomes and expenditures); iii) the adoption of a Comprehensive Policy on Regional Development by Ukraine, aligned to EU standards (with criteria

¹ The Ukrainian side has indicated that the Ministry of Economic Development and Trade will be the leading entity for the budget support on Regional Development. The negotiations on budget support including the elaboration of conditions and indicators will start in September 2011.

for selection of beneficiary regions, definition of types of Institutional Beneficiaries, etc...); iv) the adoption of an Operational Plan to be implemented the first years of the policy (years covered by the EU support programmes); v) the adoption of basic Regulations or pieces of Legislation in order to promote the level of decentralisation, or the implementation of existing ones, in line with the efforts made by other donors (i.e., the Swedish Cooperation).

4.2. Procurement and grant award procedures

1) Contracts

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.

Participation in the award of contracts for the present action shall be open to all natural and legal persons covered by the ENPI Regulation. Further extensions of this participation to other natural or legal persons by the concerned authorising officer shall be subject to the conditions provided for in article 21(7) of the ENPI Regulation.

2) Specific rules for grants

The essential selection and award criteria for the award of grants are laid down in the Practical Guide to contract procedures for European Union external actions. They are established in accordance with the principles set out in Title VI 'Grants' of the Financial Regulation applicable to the general budget. When derogations to these principles are applied, they shall be justified, in particular in the following cases:

- Financing in full (derogation to the principle of co-financing): 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 Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of the Financial Regulation applicable to the general budget.
- Derogation to the principle of non-retroactivity: a grant may be awarded for an action which has already begun only if the applicant can demonstrate the need to start the action before the grant is awarded, in accordance with Article 112 of the Financial Regulation applicable to the general budget.

4.3. Budget and calendar

The overall amount is set at EUR 20 million. The indicative breakdown of the budget would include: a Technical Assistance Component of EUR 6 million and a financial support of EUR 14 million (in principle, through Calls for proposals, unless the conditions allowing the setting-up of a budget support are fulfilled by the Ukrainian authorities).

In several selected regions calls for proposal will be published. Projects selected and financed should respond to national and regional development priorities as defined in the national and regional development strategies. Regions will be encouraged to implement regional strategies with regional operational programmes according to EU common practice. The individual grants awarded to the beneficiaries through Calls for proposals imply co-financing. The modalities of the co-financing will be defined once the financial schemes will be fixed. Nevertheless, the expected sources of co-financing are the municipal or regional budgets.

If the alternative option of a sector budget support is implemented, the Ukrainian National Budget, as well as local budgets, will co-finance the programme.

It is foreseen that the indicative operational duration of the technical assistance component will be 36 months, following the signature of the contracts. The indicative operational duration of the second component of the programme will be 48 months following the signature of the grant contracts (if the second component is implemented through calls for proposals) or will be 36 months following the

signature of the Financing Agreement (if the second component is implemented through sector budget support).

The overall duration of the operational phase of this programme will not exceed 60 months from the date of signature of the Financing Agreement.

4.4. Performance monitoring

Objectively verifiable indicators (OVI), both qualitative and quantitative, will have to be part of the methodologies included in the technical proposals for each project component. Given the demand-driven character of the project, the OVIs must be designed properly and should be further revised at regular stages of operations to make sure that they are ambitious and realistic. The monitoring of the day to day implementation will be carried out by the European Commission under its standard procedures, based on benchmarks to be agreed with the project beneficiaries. It includes periodic assessment of progress and delivery of specified project results towards achievement of project objectives.

4.5. Evaluation and audit

The project may be subject to evaluation/audit following European Commission's standard procedures. Evaluation of the results achieved may be entrusted to independent consultants as well as external audits. Mid-term and final evaluation of the project implementation may be commissioned by the European Commission to assess project performance, achievements and impact.

Evaluation and audit will be funded from the present budget or from another Financing Decision.

4.6. Communication and visibility

Communication activities may include initiatives such as media coverage, press conferences, press releases and website. The communication activities should follow the visibility guidelines of the Communication and Visibility Manual for European Union External Actions. They cover the written and visual identity of the EU and are to be used in briefings, newsletters, publications, press conferences, presentations, invitations, signs, commemorative plaque and all other items used to highlight EU participation. The communication and visibility manual is available at: http://ec.europa.eu/europeaid/work/visibility/index_en.htm.

ANNEX 2 - ACTION FICHE UKRAINE AAP 2011

1. IDENTIFICATION

Title/Number	Second EU Contribution to the Eastern Europe Energy Efficiency and Environment Partnership Fund (E5P, also known as "the Swedish Initiative") / ENPI/2011/ 268-938		
Total cost	EU contribution to be committed under this Decision: €15 million (2nd contribution, the 1st EU contribution amounted to €10 million in 2010). Total EU pledged contribution (2010-2013): €40 million [Other pledged contributions: see table in Section 2 below]		
Aid method / Method of implementation	Joint management with the European Bank for Reconstruction and Development (EBRD)		
DAC-code	23010	Sector	Energy policy & Administrative Management

2. RATIONALE

The second EU contribution to the E5P Fund will come after positive development on the operational launch of the E5P Fund demonstrated by the first Steering Group Meeting that took place in Kiev on April 21, 2011. €19.6 million of contributions have been paid in so far out of €1.8 foreseen. The Government of Ukraine's contribution agreement has been signed on February 24, 2011 and a first disbursement is expected during Q3 2011. Other pledged contributions are:

Contributors	Pledged (€)
Denmark	5,000,000.00
Estonia	160,000.00
Finland	2,000,000.00
Latvia	50,000.00
Iceland	56,413.00
USA	5,325,000.00
Norway	5,000,000.00
Sweden	24,000,000.00
EU	40,000,000.00
Poland	191,814.00
Ukraine	10,000,000.00
Total	91,783,227.00

A pipeline of promising projects has been identified and presented by the Fund Manager at the first Steering Group Meeting.

Project proposals presented for approval to the Steering Group:

- EBRD: Zhytomyr district heating rehabilitation and two technical assistance programmes to promote energy efficiency in the residential and public buildings ;
- European Investment Bank (EIB): development of the water supply and wastewater system in the city of Mykolayiv;

- Nordic Environment Finance Corporation (NEFCO): DemoUkraina district heating (10 district heating pilot projects) and Rivne-Soshenko/Makarovo district heating rehabilitation.

Project proposals for information to the Steering Group:

- EBRD: rehabilitation of Lviv, Ternopil, Zaporizhzhya and Donetsk oblast district heating;
- Nordic Investment Bank (NIB): Lviv Vodokanal Sludge Digester

The cumulative budget of these projects is worth €175 million, out of which the Fund Manager expects approximately €50 million grant. Based on this, the Fund Manager has called the contributors for additional contributions.

2.1. Sector context

Ukraine has inherited a very inefficient energy system from the USSR, which was still affordable when energy (mostly imported from Russia) was relatively cheap. This is no longer the case today with rising energy prices. The authorities are therefore committed to improving energy efficiency in all spheres (industries, housing) in order to decrease energy consumption.

By joining the Energy Community on February 1, 2011, Ukraine has now the obligation to implement the *acquis communautaire* related to energy efficiency, e.g. implementation of the directive 2010/30/EU on the indication by labelling and standard product information of the consumption of energy and other resources by energy-related products, the directive 2010/31/EU on the energy performance of buildings, and the directive 2006/32/EC on energy end-use efficiency and energy services. Implementation of the *acquis communautaire* requires the preparation of a National Energy Efficiency Action Plan that will give to Ukraine a framework to foster the development of its energy efficiency potential.

The Ukrainian Energy Strategy till 2030, adopted in 2006 and currently under revision, calls for substantial energy-saving measures in all industries, as well as for a noticeable increase in the use of renewable energies, from current 0.1 billion kWh up to 2.0 billion kWh by 2030. The Government has launched a number of measures to promote investments in renewable energies, starting with the introduction of green tariffs and tax incentives, and has set ambitious targets to replace or upgrade obsolete equipment in the industrial and residential sectors, in order to significantly decrease energy consumption and CO₂ emissions.

These efforts can lead to concrete results only if they are supported by private investment and significant public funding. In this perspective, the Swedish Presidency of the EU had in the context of the Eastern Partnership proposed in mid-2009 the creation of a Donors Fund that would help countries in the region to finance, through a combination of loans and grants, projects aimed at improving energy efficiency and promoting the use of renewable energies. The initial geographical focus is Ukraine but the Initiative is likely to expand, as appropriate, to the other countries of the Eastern Partnership (Armenia, Azerbaijan, Belarus, Georgia and Moldova).

The Fund was officially launched at a Pledging Donors Conference in Stockholm on November 26th, 2009, co-chaired by Commissioner Ferrero-Waldner. The EU has pledged a contribution of €40 million over the period 2010-2013

2.2. Lessons learnt

The EU has already contributed to ERBD-led Funds in Ukraine (e.g.: Chernobyl Shelter Fund) and cooperation with the Bank is good. EBRD also implements a number of investment projects in Ukraine under the Neighbourhood Investment Facility.

For what concerns operations in Ukraine, however, special attention will have to be paid to the complex regulatory framework around renewable energies, energy efficiency and environment. This framework is expected to evolve positively with Ukraine having joined the Energy Community. Technical and financial cooperation provided by several donors (including a large EU budget support, EU funded technical assistance including upcoming twinning) will strongly contribute to this improvement.

2.3. Complementary actions

The launch of the E5P initiative coincided with the Copenhagen conference on climate change. Environment/energy issues are still high on the global agenda, as well as in the EU and in Ukraine.

All major donors have been supporting reforms towards the improvement of energy efficiency in Ukraine for many years. Of particular relevance are the following ongoing initiatives and projects:

- The **€3 million on going EU Budget Support** on Energy Efficiency. The Budget Support focuses on five areas: policy framework (review of the national energy strategy, implementation of state programmes), legislative framework, public finance management (performance analysis of the EE programmes); EE measures (energy balance, public awareness, access to financing); policy outcomes (reduction of energy intensity; reduction of losses). This Budget Support is accompanied by a €3.2 million technical assistance component and a call for proposals targeting energy efficiency measures in small Ukrainian municipalities. Approximately 10 small grant projects will be financed for a total budget of €1.5 million.

- The **EU's INOGATE** energy programme has been assisting Ukraine (and other countries in the region) to pave the way for investments in the field of renewable energy and energy efficiency through assistance to legislative and policy reforms. In the frame of INOGATE, the regional Energy Saving Initiative in the Building Sector (ESIB) project was launched in January 2010 for four years; furthermore, the project 'Support to Market Integration and Sustainable Energy' (SEMISE) provides support to the creation of a positive environment for sustainable energy investments including in cooperation with IFIs.

- Under the **EU Covenant of Mayors** initiative, 16 large cities of Ukraine have now taken the commitment to go beyond the target of 20% CO₂ reduction by 2020 through the implementation of Sustainable Energy Action Plans, to be supported by the EU. Implementation of those Sustainable Energy Actions Plans could be supported by the Fund created under the E5P initiative. A specific technical assistance project in support of the Covenant of Mayors in the region is foreseen.

- The EU financed **Community Base Approach (CBA)** running until 2011 (€13 million) has been supporting the creation of an enabling environment for long-term self-sustaining social-economic and community development at the local level by promoting local self-governance and community-based initiatives. 60% of the projects implementing under CBA have targeted energy efficiency. The 2nd phase of the project, which was signed on the 31/05/2011, targets energy efficiency as well.

- The EU **Support to the Joint Cooperation Initiative in Crimea**, signed on the 13/05/2011, has identified support to social and municipal infrastructures as a priority, including heating. Synergies can be developed with this Fund.
- The **Neighbourhood Investment Facility (NIF)**, now available to Ukraine, can be used to further support and leverage IFI lending in support of the initiative;
- The **EBRD**, through its Sustainable Energy Initiative (SEI), has been providing large scale loans to private and governmental/municipal facilities to support the introduction of environmentally clean and sustainable equipment. Energy consumption has decreased by up to 40% in facilities supported by this initiative.
- The **World Bank** has been supporting since the mid-1990s large projects aiming at improving energy efficiency, with a focus on large public buildings in Kiev. A new programme to support energy efficiency has been signed in April 2011 with the government of Ukraine; it aims through sub-lending to finance energy efficiency projects in the private sector and at municipal level. For the latter, the World Bank is considering the use of E5P Fund.
- **GIZ** has been supporting the Ministry of Regional Development and Construction of Ukraine since October 2007 (till mid-2013) to improve energy efficiency in commercial and private buildings. The main focus of the project is to introduce energy management at local level and implement pilot projects in four Ukrainian cities.
- **USAID** has been supporting large projects (amounting to a total of \$13 million) since early 2009 in district heating in no less than 36 Ukrainian cities. For each city, energy audits are being carried out. These audits will serve as a good basis for the identification of future technical projects to be financed by the Fund. Coordination of interventions will be ensured by the fact that the US count amongst the main contributors to the Fund.

2.4. Donor coordination

Donor coordination is formally ensured in Ukraine by the Government, via thematic working groups, but meetings have however not been regular. The present donor coordination is led by the World Bank thanks to regular coordination meeting where donors and IFIs participate.

Relations between donors in the frame of the proposed intervention are regulated by the "Rules of the Eastern Europe Energy Efficiency and Environment Partnership Fund" developed by the EBRD as Fund manager. Donors joining the Initiative will have to comply with those rules.

Those rules state that the governing body of the Fund will be the Assembly of Contributors (one representative per donor), which shall be responsible for the overall policy of the Fund and supervise its implementation. The EBRD, the European Investment Bank (EIB), the Nordic Investment Bank (NIB), the Nordic Environment Finance Corporation (NEFCO) and the World Bank Group shall act as implementing agencies of the Fund. A steering group proposes projects and subsequent grant requests to the Assembly of Contributors which decides if the projects shall be supported with the resources of the Fund. Agreement of the beneficiary country will always be sought. Grants will be sized in proportion to environmental benefits and/or gains in terms of energy efficiency, quantified in monetary terms. This will allow measuring the efficiency of the action.

3. DESCRIPTION

3.1. Objectives

The purpose of the Fund is to allow a harmonised and effective delivery of international financial support over several years by pooling contributions from a group of donors and beneficiaries, to be used primarily for supporting energy efficiency and environmental projects, resulting in a significant reduction of carbon dioxide (CO₂) and other greenhouse gases (GHG) emissions.

3.2. Expected results and main activities

The main expected results of the proposed action are:

- A reduced energy consumption in Ukraine and in the countries of the region, thanks to a more efficient use of available energies. This will be achieved through the implementation of projects contributing decisively to this objective. Implementation of those projects will be supported by the Fund resources, on a proportional basis;
- A decrease in CO₂ and other greenhouse gases emissions in the region, thanks to decreased energy consumption;

The proposed initial thematic focus of the Fund's activities is housing and district heating. Both sectors consume together more than half of the energy used in Ukraine. It is however envisaged that the Fund will also support other investments for energy efficiency or environmental projects.

3.3. Risks and assumptions

1. It is assumed that the Government of Ukraine pays its first € million contribution to the E5P Fund, which is a necessary condition for the Fund to start to operate.
2. It is assumed that the suitable amendments to the budget code are passed in order to overcome current legislative obstacles making difficult municipal debt financing needed for investment at local level.
3. Use of grants shall be carefully monitored in order not to over subsidise investments that were already planned by IFIs or public sector utilities; more generally the use of grants should be necessary for the feasibility and affordability of the project financed.
4. Synergies with other EU initiatives such as the Covenant of Mayors shall be emphasised by the Fund Manager, who will be made aware of specific opportunities in this regard;
5. The Fund is in its nature similar to the Neighbourhood Investment Facility (NIF). Attention will be paid on avoiding overlap between the two financing instruments and underlining their specificities;
6. A particular attention will have to be paid to the questions of procurement and follow-up of costs during the implementation of the Fund.

3.4. Crosscutting Issues

Environmental sustainability and climate change are the main cross-cutting issues raised by this project. The project will directly contribute to climate change mitigation and to reducing pollution due to power generation from fossil fuel.

3.5. Stakeholders

The stakeholders of the proposed intervention will be, for what concerns Ukraine: the central Government, the cabinet of Ministers, the Ministry of Fuel and Energy, regional and local authorities, municipalities, companies, NGOs, home owners, etc.

4. IMPLEMENTATION ISSUES

4.1. Method of implementation

The method of implementation will be joint management, through the signature of a new contribution agreement with the EBRD in accordance with Article 53d of the Financial Regulation. This new agreement will be based on the model of the first contribution agreement including the corresponding derogations. As for the first intervention no separate Financing Agreement will be signed with the Government of Ukraine.

EBRD is currently subject to an external review in relation to Article 53d of the Financial Regulation. In anticipation of the results of this review the authorising officer deems that, based on the long-standing and problem free cooperation with this organisation, joint management can be proposed and the standard contribution agreement with an International Organisation can be signed in accordance with the provisions laid down in Article 43 of the Implementing Rules to the Financial Regulation.

The Manager of the Fund and contact person on the EBRD side is based in London at EBRD headquarters during a first phase of the Fund's operation, and its Deputy has been appointed in EBRD's office in Kiev. The EU Delegation in Ukraine will follow-up and ensure coordination with the local EBRD offices as appropriate.

The Delegation coordinates relations with the Bank and other donors involved in the Initiative, with support from Commission services in Brussels.

The largest donor, i.e. the EU (represented by the Commission), will chair the Assembly of Contributors to the Fund, unless otherwise decided by the Assembly. The Chair will convey, together with the Fund Manager, meetings of the Assembly and might invite, as relevant, representatives of governments, other institutions and entities to attend specific agenda items. The Chair can as well call special meetings of the Assembly, when deemed necessary.

4.2. Procurement and grant award procedures

All contracts implementing the action are awarded and implemented in accordance with the procedures and standard documents laid down and published by the EBRD and Rules of the Fund.

4.3. Budget and calendar

The Fund is foreseen to remain active until 31 December 2019 unless otherwise decided by the Assembly of Contributors to the Fund. The proposed second EU contribution to the Fund is €15 million. The implementation period of this Action will start from the date of signature of the Contribution Agreement with EBRD. In order to ease the monitoring of the EU contribution, it is proposed that the implementation duration of this action coincides with the period of activity of the Fund, i.e. until at least 31 December 2019.

4.4. Performance monitoring

The monitoring of the day to day implementation of the proposed action will be carried out by EBRD under its standard procedures based on benchmarks to be agreed with the donors contributing to the Fund. The effectiveness of the action will be evaluated using key indicators like:

1. Number of requests made to the Fund over a certain reporting period;
2. Number of grants considered, selected and approved during this period;
3. Share of the Funds disbursed;
4. Fund's effectiveness ratio, comparing the environmental benefits and/or gains in terms of energy efficiency converted in monetary terms with the amount given from the Fund.

Energy efficiency will be measured for example by the saving of energy (kWh p/a), reduced use of natural gas (cubic meters p/a), electricity efficiency (MWh p/a) and its equivalent in monetary terms (UAH, € p/a) and environmental benefits by the decrease of CO₂/NO_x emissions (tonne p/a), decrease in water use (cubic meters p/a) and the consumption of treated water (cubic meters p/a).

4.5. Evaluation and audit

No funds from this €15 million contribution should be put aside for financing evaluation(s) or audit. Evaluation and audit will be under the responsibility of EBRD. Should the need arise, the EU would finance additional evaluation(s) and/or audit(s) from other budgetary resources.

4.6. Communication and visibility

Communication and visibility activities should follow the Communication and Visibility Manual for EU External Actions (http://ec.europa.eu/europeaid/work/visibility/index_en.htm). The projects will aim for a widespread dissemination of its achievements and results as well as awareness-raising and image building through inter alia, project websites, electronic newsletters, outreach to the media, etc. Once the activities have started, communication and visibility plans should be prepared and submitted to the EU Delegation for approval, as per the Communication and Visibility Manual for EU External Actions. Any events organised as part of or related to the project should include the participation of the contracting authority.

1. IDENTIFICATION

Title/Number	Reform of the Administrative Legal Framework and Civil Service in Ukraine CRIS: ENPI/2011/022-826		
Total cost	EU contribution: EUR 70 million		
Aid method / Method of implementation	Sector Policy Support Programme: - Sector budget support (EUR 63 million, centralised management); - Project mode for complementary measures (technical assistance – EUR 7 million, centralised management).		
DAC-code	15110	Sector	Public Sector Policy and Administrative Management

2. Rationale and country context

2.1. Country context and rationale for SPS

2.1.1. *Economic and social situation and poverty analysis*

From 2000 to 2007, Ukraine's economic performance was strong and poverty decreased substantially but the world crisis hit Ukraine hard in late 2008. After experiencing one of the sharpest downturns in the region in 2009, real GDP growth in 2010 was 4.2 percent y-o-y, helped by export-oriented industries, particularly steel. More recently, domestic demand has gained momentum on the back of improving consumer and business confidence and robust wage growth². According to the IMF assessment, growth is expected to increase to 4.5 percent in 2011 helped by stronger domestic consumption and investment (including for the Euro 2012 football tournament). The authorities' major concern in 2011 is to keep inflation below the 10% threshold, which becomes increasingly unlikely as the effects of growing global food and oil prices are becoming more and more pronounced. In early June 2011, National Bank of Ukraine (NBU) indicated that it is ready to tighten the monetary policy to curb inflation but warned that economic growth would slow as a result.

While central bank reserves are at a historical high and the government is boasting a rather strong liquidity position, the continuation of the ongoing Stand-by Agreement with the IMF requires additional reform by the government. While the law on the pension reform passed the first reading in Parliament and may be adopted in 2011, the gas price increase, the second key conditionality of the IMF's programme yet to be fulfilled, is less certain. In June 2011 the IMF stressed again the importance of strong policies and reforms in Ukraine to achieve the programme objectives; reduce vulnerabilities and lay the foundation for sustainable growth. Both parties agreed to continue their close cooperation in the coming months.

2.1.2. *National development policy*

The deepening of relations between EU and Ukraine in the context of the Eastern Partnership through an Association Agreement with a Deep and Comprehensive Free Trade Area (AA/DCFTA) as an integral part involves unprecedented regulatory approximation. To prepare for and facilitate the entry into force of the AA/DCFTA, EU and Ukraine have jointly agreed on an implementation tool, the Association Agenda, which covers key reforms in all areas of the future agreement. The parties agree on priority reforms on an annual basis.

² <http://www.imf.org/external/pubs/ft/scr/2011/cr1152.pdf>

The national development framework is broadly defined by the Economic Reform Programme for 2010-2014³ (ERP), adopted on 2 June 2010 at the meeting of the President's Committee for Economic Reform. The ERP covers important policy goals related to sustainable economic development, improving social services, improving the business climate, attracting more investment and modernising the infrastructure. The ERP is linked to the main priorities of the EU-Ukraine Association Agenda, including the measures related to the establishment of a Deep and Comprehensive Free Trade Area (DCFTA), visa liberalisation, cooperation in energy and other sectors.

By decision No. 1724 of 23 June 2010, the Government of Ukraine committed itself to implement the ERP. Ownership of the ERP by the Government is supposed to be ensured through allotting personal responsibility of Ministers for relevant reforms areas in line with the presidential decree No. 1154 of 21 December 2010.

2.2. Sector context: policies and challenges

2.2.1. Sector Policy

There is a clear understanding in Ukraine that there is a link between the performance of the civil service and the public sector as a whole and economic development. Public Administration Reform (PAR) has therefore been launched mainly with a view to improving the business environment and furthering economic reforms.

Ukraine has recognised public administration reform (PAR) as a pre-condition for the successful implementation of ongoing and planned economic reforms as well as a way to improve the public administration's performance, the quality of public service delivery to citizens and business, as well as the general integrity of the public sector.

Several PAR initiatives have been launched and are being implemented since 2010:

2.2.1.1. The Economic Reform Programme (ERP)

The announced overall objective of the ERP is to boost economic recovery and to modernise the country's economy. While the draft ERP covers five main reform areas, two have a specific impact on the organisation of public administration: a) improving business climate by reducing government intervention into the economy and by alleviating administrative burden for its development; and b) raising public administration efficiency by reforming the civil service and the system of executive power.

However, the description of measures aimed at raising the efficiency of Ukraine's public administration drafted in February 2010 was not included in the final text of the ERP published in June 2010. The only reference to this priority is a footnote announcing that the block of reforms towards modernization of the public administration system will be presented in autumn 2010.

On 13 October 2010 a restructuring of the central administration was launched by presidential decree, which tasks the President's Committee Economic Reform and the Government to prepare proposals for the improvement of the central executive system and to draft amendments to the current legislation. These proposals were introduced by presidential decree on 9 December 2010 (see next section).

2.2.1.2. Re-organisation of the central administration launched by the President's decree No. 1085 of 9 December 2010

The decree established a new typology of executive bodies and a new approach to redistribution of functions and responsibilities. Six types of central executive agencies were defined: ministries (in charge of policy making), services (in charge of policy implementation and service delivery), inspections (in charge of control and auditing), agencies (in charge of programme implementation),

³ Unofficial translation in English is available at http://www.usubc.org/site/files/Ukraine_Program_of_Economic_Reforms_2010-2014.pdf

independent regulators and agencies with special status. The number of central executive agencies was reduced from 112 to 63: 16 ministries, 28 services, 12 agencies and 7 inspections.

In the course of the re-organisation (liquidation) of central executive bodies, the Government is expected to reduce the number of civil servants by 30% in central administration and by 50% in the secretariat of the Government of Ukraine. This process is on-going, although no clear timetable or criteria of dismissal have been communicated so far.

2.2.1.3. Adoption of a new legal framework for central executive bodies and revision of the law on the Cabinet of Ministers

In the follow-up to the restructuring process launched in December 2010, a new law on central executive bodies (No. 3166) and amendments to the law No. 2591 on the Cabinet of Ministers of 7 October 2010 (No. 3165) were adopted by Parliament on 17 March 2011.

The above-mentioned laws confirm a new institutional set-up and redistribution of functions between the main political actors: Ministers, the Cabinet of Ministers and the President, including his Administration.

However, according to a number of experts, the new institutional framework leads to an excessive control by the President and his Administration over the Government. The prerogative to appoint all deputy ministers, heads of agencies and senior and middle level public officials could entail a weakening of the system of checks and balances, decrease transparency in decision making and indicate a return to the previous "Ukaz (presidential decree) system". It does not provide adequately for a clear differentiation between political appointees and professional civil servants, as required in a number of recommendations (e.g. OECD Anti-Corruption Network for Eastern Europe and Central Asia, Istanbul Anti-Corruption Action Plan Monitoring), and is incompatible with the principle of a merit-based civil service.

2.2.1.4 National Action Plan for the ERP's implementation in 2011

The National Action Plan (NAP) for the ERP implementation in 2011 was adopted by the President in April 2011 by decree No 504. It covers all reform priorities targeted by the ERP and includes action plans on the reform of civil service (section 20 of the NAP), administrative legal framework, including public service delivery (section 9 of the NAP) and executive bodies (section 19 of the NAP). The following priority measures are foreseen to be implemented in 2011:

Administrative legal framework:

- development and adoption of the law on administrative services (establishing a typology and modality of the provision of services to citizens) and the Code of administrative procedures (laying down basic principles of administrative procedures);
- development and adoption of the secondary legislation aimed at simplification of the administrative procedures;

Civil service:

- adoption of a new law on civil service;
- adoption of a new regulation on the Main Department of the Civil Service (MDCS);
- development and adoption of the secondary legislation on civil service management;
- reform of the National Academy of Public Administration;
- reform of the civil service training system.

The above-mentioned measures of the National Action Plan for the ERP's implementation in 2011 represent orientations for an administrative and civil service reform. However, it should be mentioned that they focus on adoption of the legislation rather than on its effective implementation and make no reference to financial or other resources needed.

Therefore, after the adoption of the laws necessary to advance the above-mentioned reforms, it would be crucial to elaborate and put in operation comprehensive implementation plans for each reform, including activities, resources, timeline, output indicators and entity in charge. The disbursement of the variable tranches of this budget support will be linked to the implementation of these plans and the achievement of measurable results.

2.2.1.5. New law on civil service

A new law on civil service has been adopted in first reading in April 2011 and there is an intensive policy discussion in Parliament with involvement of political decision makers (Presidential Administration, Ministry of Justice, Main Department of the Civil Service) concerning its final wording. While the draft law contains some improvements, there are serious deficiencies remaining, related, *inter alia*, to the division of political and administrative posts.

2.2.1.6. Conclusion on sector policy

Ukraine has no formal strategic document on Public Administration Reform. In addition, the annual character of the National Action Plan for the ERP implementation does not provide a medium-term perspective, which would be needed in order to ensure continuity, coherence and sustainability, and also for budgeting in order to finance the foreseen activities. Moreover, the approach so far has been to implement reforms *ad hoc* and top-down, without an inclusive public debate involving stakeholders or a proper communication strategy.

However, given that the performance of public administration is a crucial element of Ukraine's economic and social development and a pre-condition for deeper cooperation with the EU, it would be advisable to take advantage of the current dynamics in this area and support the on-going efforts of the Government to improve efficiency of public administration and to ensure that best practices are used.

In the absence of a formal sector strategy, the EU support will focus on clearly defined components in areas where some preparatory work has been conducted, including by SIGMA and EU-funded projects and a reform commitment can therefore be assumed. Benchmarks for reform are therefore being formulated in the following 3 fields: administrative legal framework, administrative justice, and civil service reform. These 3 fields represent the sector for this intervention.

The implementation of this SPSP in line with the proposed approach will allow further synergy and strong complementarity with the Comprehensive Institution Building (CIB) programme under the Eastern Partnership. While the CIB programme focuses on strengthening capacity of the key institutions related to the future Association Agreement between the EU and Ukraine, the SPSP will support improvements of the key elements of Ukraine's governance system, which can have a sustainable impact on the overall performance of the public administration and thus improve Ukraine's capacity to implement the Association Agenda. Therefore, combining these two programmes could have a catalytic effect, promoting reform efforts in other related areas such as fight against corruption, judiciary reform, as well as improvement of the economic competitiveness and the investment climate.

This SPSP together with the CIB programme could improve the framework for EU assistance to Ukraine with an aim to preparing ground and ensuring further effective implementation of the future Association Agreement between the EU and Ukraine.

2.2.2. Sector Context and MTEF

There is neither an overall Medium Term Fiscal Framework (MTFF) nor a Medium Term Expenditure Framework (MTEF) for the whole public administration. The effective allocation of funds is subject to specific parameters of the annual state budget.

The absence of a formal sector strategy makes it difficult to estimate financial and other resources needed for future reforms in the target areas mentioned above. The ERP implementation plans have no measurable impact indicators to guide the implementation process. An *ex ante* legal and regulatory impact assessment of the laws drafted and/or endorsed is missing, which will favour *ad hoc* allocations which are difficult to track, monitor and audit. For instance, the impact of the dismissal of civil servants on social budgets such as pension and unemployment funds has not been calculated yet. Upon request by the Government the European Commission is ready to offer its support to address these weaknesses through technical assistance.

Following the adoption of a new Budget Code and Tax Code, the Government has stated its commitment to gradually progress towards a MTFF/MTEF, which will be encouraged and monitored under this and ongoing SPSP and within the overall EU-Ukraine cooperation. The on-going 2011 PEFA⁴ exercise by the World Bank and the Commission has already confirmed for the first time the introduction of a medium term dimension into budget planning for the 2012 Budget.

2.2.3. Coordination with beneficiary country and other donors

At political level, reforms of the administration are decided on by a working group "Legal and Institutional Changes for Reforms" within the President's Committee for Economic Reforms (CER). This group is led by the Minister of Justice and includes two sub-groups: civil service reform (Deputy Head of the President's Administration and the Main Department of the Civil Service/MDCS) and executive power reform (Ministry of Justice/MoJ). The work related to the administrative legal framework is carried out by a working group "Deregulation and entrepreneurship development" led by the First Vice Prime Minister – Minister of Economic Development and Trade with support of the Minister of Justice and other relevant public bodies.

Furthermore, an Economic Reforms Coordination Centre has been established within the CER. It has a special mandate from the President of Ukraine for coordinating PAR implementation.

On a technical level, the process is mainly being promoted by the MoJ, the MDCS, the Ministry of Economic Development and Trade and the Presidential Administration, High Administrative Court as well as other relevant institutions in the areas targeted by this SPSP.

However, recent experience shows that this complex coordination structure – where so far no clear mandates were assigned to all the individual bodies involved - leads to confusion of roles and increases the policy functions of the Presidential Administration to the detriment of the line ministries. This can potentially lead to an opaque policy making with unpredictable outputs.

The coordination with donors is supposed to be ensured by a specially created donor-government sub-group for PAR led by the MDCS. However, this sub-group is still not functioning as no meeting has been convened by the MDCS since the launching meeting of the sub-group held in September 2010.

2.2.4. Assessment of institutional capacity

The PAR will require strong political support. The involvement of the Presidential Administration, the Cabinet of Ministers and the Parliament (including relevant committees), the coordination between these individual institutions and the assignment and monitoring of clear mandates to each of them will be of crucial importance for its successful implementation.

A number of factors that limit the institutional capacity of Ukrainian public bodies should be pointed out:

⁴ Public Expenditure and Financial Accountability

- A highly centralised policy making system that is exposed to weak coordination;
- A prevailing conviction that with the adoption of the legislation, the implementation process starts automatically. Therefore, there is limited practice of detailed implementation plans, including budget forecast for implementation of the legislation, drafting and approval of the secondary legislation, internal and external communication, obligatory training on implementation of new legislation;
- A politicised civil service, which is not guided by an integrity framework and a code of ethics. Pay and motivation are generally low, while staff turnover is high, which makes it difficult to create and maintain teams that could work in a sustainable manner in designing and implementing reforms over longer periods of time.

Finally, the current Ukrainian approach to the initiation of a PAR lacks transparency and inclusiveness. The main political actors need to be convinced that the effective incorporation of European principles of governance envisage involvement of stakeholders outside the inner circles of decision- and lawmaking such as independent experts, NGOs, business associations and that modern policy making tools are both efficient and compliant with a participatory democracy.

2.2.5. Performance Monitoring

There is no formal sector-wide performance monitoring system in place to date.

An output-based monitoring of the reform of civil service and legal administrative framework is only partly possible based on the targets established by the annual National Action Plan (NAP) for the ERP' implementation. The NAP does not include any indicators and sources of verification in terms of implementation and impact of the legal acts that are planned to be adopted in 2011.

It is therefore proposed to design with SIGMA programme support a performance monitoring system connected to three areas targeted by this SPSP (the administrative legal framework, administrative justice and the civil service), as well as to the horizontal dimensions of the public administration (integrity, public finance, policy making, etc).

2.2.6. Macroeconomic framework

The global economic crisis seriously affected Ukraine in late 2008 and 2009. The real GDP declined by 15.1% in 2009 and recovered by timid 4.2% y-o-y in 2010, with the general government public deficit reaching 9% of GDP in 2009 and 5.9% in 2010 (not including bank recapitalisation costs). Public debt rose rapidly, to 40% GDP in 2010, with both external and domestic debt surging.

To cope with the consequences of the crisis, the Government has implemented a number of measures envisaged by the ERP, which are also supported by the IMF stand-by agreement. After a 14.8 percent GDP decline in 2009, the economy grew 4.2 percent in 2010, and posted 5.2 percent grow in the first quarter of 2011. The current account deficit widened in 2011, but remains financeable. The fiscal stance remains fragile and could be further undermined by delays in pension and utility tariff reforms and new spending initiatives⁵.

The IMF and the Government of Ukraine continue their close cooperation in order to reach the objectives of their programme.

2.2.7. Public Financial Management:

The legal and institutional responsibilities in the field of public finance management (PFM) in Ukraine are, in general, clearly defined and assigned. In addition to key legislation, the government has approved a resolution on the PFM modernisation strategy in October 2007, which is, however, of a general nature, and has not yet been implemented. A more practical approach to the elaboration of

⁵ World Bank economic update June 21, 2011

PFM sector development was introduced as a chapter in the recently approved Economic Reform Programme, which however requires further refining and precision.

Overall, budgeting performs relatively well in Ukraine, with an orderly budget process and the fundamental legislative framework largely in place. The most significant weakness in this area is the continued absence of a publicly verifiable multi-year perspective in fiscal planning. This absence poses a significant risk to overall fiscal discipline as well as to a more strategic use of limited resources and to improved efficiency. While the budget execution system does assure some degree of predictability in the flow of funds, uneven performances and fragmentation of responsibilities negatively impact the quality and transparency of budget execution. No system of internal audit is yet in place.

However, with the adoption in July 2010 of a new Budget Code (which came into effect on 1 January 2011) some improvements compared to the existing framework are made: the Code introduces some elements conducive to the setup of a sound PFM framework, in particular a clear distinction between public control and public audit. It is expected that a comprehensive multi-year budgeting system would include a medium-term fiscal framework (MTFF) in the draft Budget Policy Guidelines, providing medium-term aggregate fiscal objectives, to which the MTEF would be a complement. A major drawback is that the Code still does not improve transparency and accountability in the public finance sector.

The system of public procurement in Ukraine is going through systematic revisions aimed at achieving better transparency, efficiency, competitiveness and, last but not least, compliancy with the EU directives. The public procurement law adopted in June 2010 was assessed by the international community as a firm step towards alignment of the Ukrainian legislation with international standards of public procurement and, particularly, with the EU Directive 2004/18. However, Parliament, in the first half of 2011, has adopted some amendments to the law, which are not in line with international best practices. On 14 June 2011 the President vetoed the proposed amendments and sent it back to Parliament reiterating the necessity to adjust it to the EU Directive 18, 2004 and therefore, to keep the amendments in line with the recommendations provided by the EU and World Bank. According to the established procedure, the Parliament must accept or overrule the Presidential veto within a month.

The final Law on Public Procurement has been adopted by the RADA and signed by the President. The law 3681 (former 7532) constitutes an important step towards approximation of the Ukraine public procurement law with the EU Directives, which is foreseen as an obligation in the currently negotiated Deep and Comprehensive Free Trade Area. Nonetheless, further steps to ensure full approximation of the public procurement law with the EU Directives shall have to be taken by the Government. Further steps in the development of a transparent and efficient public procurement system in Ukraine will include the definition of contracting authorities, the preparation of a medium-term public procurement strategy, and the rationalisation of the utilities' procurement.

2.3. Eligibility for budget support

An analysis of the three eligibility criteria for sector budget support is presented below.

- (1) Although there is no formal sector strategy, there is a commitment at the highest level as well as some draft legislation and orientations contained in the National Action Plan for the Economic Reform Programme (ERP) implementation in 2011.

It can be considered that the administrative legal framework and civil service are the centrepiece of any Public Administration Reform. It is therefore proposed to consider the relevant measures of the National Action Plan for the ERP implementation in 2011 and the two draft laws in these fields as constitutive of a sector strategy, and to include the review of these laws in the light of European principles, as advised by SIGMA, and their adoption into the general disbursement conditions. This would mean that an assessment of the laws

demonstrating that they are generally in line with European principles would be a precondition for any disbursement.

- (2) The macroeconomic stability criterion is met (for detailed assessment see section 2.1.1 and 2.2). The progress in cooperation with the IMF should be subject to continuous monitoring from the EU side in order to allow necessary corrective measures.
- (3) The assessment in section 2.2 also confirms that the eligibility criterion related to Public Financial management is met, with basic elements being in place. However, the PFM system still requires significant improvement, particularly, needed for effective implementation of the new Budget Code and Tax Code, and progress will be needed over the medium-term, in particular on the preparation of a credible MTEF/MTEF. Furthermore, as mentioned in the section 2.2(8) Ukraine's public procurement system requires further alignment with the European principles, as well as development and implementation of the medium-term public procurement strategy. This also requires a close monitoring of proposed amendments to the relevant legislation. The 2011 PEFA exercise with the World Bank will support the Government in defining the reforms still needed to improve Ukraine's PFM system further.

2.4. Lessons learnt

A multi-project Result Oriented Monitoring (ROM) in the field of public sector reform in Ukraine has been prepared in December 2010 to draw summary conclusions and recommendations on the project's sector logic and strategy, in line with the lessons learned from the past.

The analysis of support areas (administrative law, civil service, anti-corruption) covered by the ROM has shown their high relevance, solid ownership throughout the projects on behalf of direct stakeholders and beneficiaries and a positive assessment of outputs produced in quantity and quality, although the assistance in the sector was strongly affected by the volatile political situation during the period under review.

2.5. Complementary actions

The main donors involved in the sector are the European Commission, Canada, Denmark and USAID (main focus on regional governance, legal reforms, and anti-corruption). Current EU-funded projects include a Twinning with the National Academy of Public Administration and a Twinning with the High Administrative Court. A Twinning with the MDCS is envisaged to start in 2012.

2.6. Donor coordination

The Government has recently restructured its donor-coordination system and created a special sub-group for PAR led by the MDCS. However, this sub-group is still not functioning as no meeting has been convened by the MDCS since September 2010. Therefore, the system remains weak since government activities and donor interventions are not aligned both content- and time-wise. In this context, coordination among the donors themselves helps to compensate for a lacking capacity/commitment on the side of the government.

3. Description

3.1. Objectives

The general purpose of the SPSP, which builds on the ERP and the 2011 National Action Plan for its implementation, and the EU-Ukraine Association Agenda is to support Public Administration Reform with a view to rendering government more accountable, effective and efficient, and thus allowing for an improved sector policy planning and implementation, which will enhance Ukraine's capacity to successfully implement the substantive reform agenda linked to the association process, including the AA/DCFTA.

The main objective of this SPSP is to create the necessary conditions for general, fair and effective administrative procedures to be implemented by public service bodies using qualified and professional

civil servants that are recruited and managed exclusively according to their merit, perform their jobs following principles such as legality, impartiality and integrity and in which decisions can be challenged before independent courts that will solve disputes fairly and timely.

The specific objectives of the SPSP are as follows (3 components):

- To contribute to the implementation of a coherent administrative legal framework, including a law on general administrative procedures (or Code of Administrative Procedures) and other relevant legislation in line with acceptable European standards and good practices for improving the quality of public services delivery;
- To support the implementation of a law on civil service in line with European standards and good practices, conducive to creating a professional, politically neutral and merit-based civil service system;
- To improve the overall quality and effectiveness of the administrative justice system, including administrative courts, following European and world good practices.

3.2. Expected results and main activities

The proposed SPSP will therefore encompass the following results:

3.2.1 Budget support:

Component 1 "Reform of administrative legal framework":

- improved administrative legal framework (Code of administrative procedures and relevant internal administrative procedures) fully implemented and applied by public authorities;
- Law on Administrative Disputes reviewed and adapted following the adoption of the Code of Administrative Procedures;
- capacity of the public authorities to enforce the new administrative legal framework, including through training, is improved;
- public services for citizens and business delivered in a more transparent and efficient manner, including regular independent monitoring of service quality;
- general access to and provision of information on the administrative procedures related to public service delivery is improved.

Component 2 "Reform of civil service":

- relevant secondary legislation to the law on civil service and internal administrative procedures is adopted;
- implementation plan for the Law on civil service is adopted and its follow-up is ensured;
- capacity of the public authorities to enforce the law on civil service is improved;
- corruption is significantly reduced and the integrity framework for the public service is enhanced, including through the adoption of the law on Integrity of the civil service, a law on conflict of interest and the implementation of appropriate measures to fulfil international conventions, recommendations (e.g. OECD, ACN);
- efficient human resources management policy, including integrated HRM information systems, developed and implemented;

- co-operation with civil society in addressing various matters of PAR and civil service reform to promote good governance enhanced.

Component 3 "Strengthening capacity of the administrative justice":

- capacity and effectiveness of the administrative justice system is enhanced, including the review of public complaints mechanisms and modernisation of the relevant infrastructure;
- the legal framework related to the functioning of the administrative justice is improved according to European principles;
- general access to and provision of information on administrative justice, including on the relevant administrative procedures, is ensured.
- the capacity of the administrative court system, including the High Administrative Court, to apply the administrative legislation in a timely, fair and independent manner is ensured;
- a monitoring system to measure process and results of the reform processes (e.g. regular surveys on public trust of public institutions and other relevant tools) is developed, applied and disseminated in line ministries.

3.2.2 Complementary measures (technical assistance):

The technical assistance component will focus on improving the capacity of relevant Ukrainian authorities to steer and implement the above-mentioned reform areas targeted by this SPSP. The technical assistance will support and facilitate the Ukrainian authorities in ensuring the effective and transparent implementation of this SPSP by ensuring high quality and coherence of the implementation measures and maintaining an efficient programming, management, control and evaluation system for the three reforms areas targeted by the SPSP.

The exact components of the technical assistance are to be defined once the above mentioned draft laws have been passed. They are likely to include several Twinning measures with key institutions, including the Ministry of Justice.

3.3. Risks and assumptions

The key risks are the following:

- lack of consensus among main stakeholders resulting in constitutional uncertainty and unclear (or insufficient) division of powers between the branches of government;
- lack of political consensus between the legislative and executive branches after the parliamentary elections in 2012;
- Parliament does not adopt the legislation defined as opening benchmarks or adopted legislation does not meet minimum European requirements, which would lead to non-fulfilment of the general conditions;
- Government and public authorities do not adopt internal administrative procedures in line with the Code of administrative procedures (only partial implementation of legislation);
- persistent corruption in the civil service and in the administrative courts system hampers the implementation of reforms areas targeted by this SPSP;
- lack of support or outright opposition to the changes from inside the civil service.

The SBS hinges upon a number of assumptions:

- the Government is committed to implement the reform of public administration and civil service reform in line with best European practices, thus not merely focusing on the re-structuring of central executive bodies;
- consensus among main political and administrative stakeholders regarding the vision of the public administration and key policy directions and instruments for its reform reached and maintained over its implementation period;
- basic legal framework necessary for the effective implementation of the proposed reform approved by the Parliament;
- real commitment to address corruption.

3.4. Stakeholders

The main stakeholders for this SPSP are the Ministry of Justice (MoJ), the Main Department of the Civil Service (MDCS), the Presidential Administration (Main department in charge of staff policy) and the Ministry of Economic Development and Trade. As far as the administrative justice is concerned, the main player is the High Administrative Court.

The MoJ is playing a crucial role in designing the PAR process and in drafting the necessary legal framework. The MDCS is in charge of the civil service management, it is one of the authors of a new draft law on civil service currently under the consideration of the Parliament.

At political level, the main stakeholders are the Presidential Administration and the Parliament.

Recipients of public and administrative services are important stakeholders. This includes citizens and business frequently facing red-tape and cumbersome, slow and low-quality public services.

As far as non-state actors are concerned, there are a number of analytical centres specialised in the reform of public administration. Furthermore, a range of civil society organisations are engaged in the monitoring of public activities, most prominently in the area of access to information, public procurement and anti-corruption. They will be consulted and involved to the highest possible extent in the course of the implementation of this SPSP.

3.5. Crosscutting Issues

Good governance and human rights: increased knowledge of EU standards and practices will raise democratic standards; involvement of civil society organisations will be a guarantee for an efficient and stable surveillance of the reform progress in main area covered by this SPSP.

Integrity of public administration: actions envisaged under this SPSP shall include measures aimed at improving transparency of the administration and at eliminating or minimising opportunities for corruption and the misuse of public funds.

Other issues: in implementation of this Programme attention will be paid to ensure equal opportunities, sustainable environment as appropriate.

4. Implementation issues

4.1. Method of implementation

Direct centralised management: budget support (EUR 63 million)

Direct centralised management: complementary measures (technical assistance – EUR 7 million)

4.2. Procurement and grant award procedures

1) Contracts

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.

Participation in the award of contracts for the present action shall be open to all natural and legal persons covered by the ENPI Regulation. Further extensions of this participation to other natural or legal persons by the concerned authorising officer shall be subject to the conditions provided for in article 21(7) ENPI.

2) Specific rules for grants

The essential selection and award criteria for the award of grants are laid down in the Practical Guide to contract procedures for EU 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 Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of the Financial Regulation applicable to the General Budget of the European Communities.

- Financing in full (derogation to the principle of co-financing): 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 Commission Regulation (EC, Euratom) No 2342/2002 of 23 December 2002 laying down detailed rules for the implementation of the Financial Regulation applicable to the General Budget.
- Derogation to the principle of non-retroactivity: a grant may be awarded for an action which has already begun only if the applicant can demonstrate the need to start the action before the grant is awarded, in accordance with Article 112 of the Financial Regulation applicable to the General Budget.

4.3. Budget and calendar

Budget support (indicative):	EUR 63 million
Related technical assistance (indicative):	EUR 7 million

The budget support will be disbursed in fixed and variable tranches. 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 EUR 0.5 million for Evaluation, Audit, and Visibility actions.

The exact amount of the fixed and variable tranches, as well as an indicative calendar and tentative breakdown of payments shall be specified in the Technical and Administrative Provisions of the Financing Agreement, based on the consultation process between the European Commission and the Government of Ukraine with support of SIGMA programme.

In case the amount of EUR 7 million foreseen for complimentary measures is not fully contracted, the remaining amount may be allocated to the budget support component.

The indicative operational implementation period is 48 months from the entry into force of the Financing Agreement for the budget support and 48 months after the signature of the contracts for the complementary measures component.

Specific conditionalities for the SPSP shall be included in the Technical and Administrative Provisions of the Financing Agreement. These specific conditionalities will be established and agreed between the EU and Ukraine with support of the SIGMA programme at an appropriate level. This will include a detailed working plan (actions, priorities, outputs, quality control, monitoring mechanism), quality control of the expected pieces of legislation and their implementation plans.

4.4. Performance monitoring and criteria for disbursement

Performance monitoring will be exerted by a Joint Monitoring Group to be led by the Ukrainian authority designated by the Government of Ukraine and the European Commission. The Joint Monitoring Group will rely on official information provided by Ukraine and verified as appropriate.

Disbursements of all tranches (fixed and variable) will be contingent to general conditions related to a stable macroeconomic environment, progress in PFM reforms and progress in the implementation of administrative reforms targeted by this SPSP, including adoption and continuous implementation of the key pieces of legislation (Code of administrative procedures and law on civil service). Disbursements of variable tranches will, in addition, be contingent to the adoption and progress in the implementation plans related to the above-mentioned laws and results achieved.

The number, amount and disbursement calendar of fixed and variable tranches shall be specified in the Technical and Administrative Provisions of the Financing Agreement, based on the consultation process between the European Commission and the Government of Ukraine with support of SIGMA programme.

4.5. Evaluation and audit

The programme will be subject to the regular monitoring by the Joint Monitoring group. A specific mid-term evaluation will be organised to, inter alia, review the validity of the monitoring system.

Evaluation of the results achieved will be reviewed and decided by the European Commission. In carrying out such review, the EC will, as appropriate, use the technical advice of external consultants recruited by the EC to verify technical reports and data transmitted by the government of Ukraine. Programme evaluations and audits, whenever necessary, will also be decided and funded by the EU out of the technical assistance component of the programme. Part of the technical assistance component may be used to enhance the local capacities for auditing the programme.

The complementary measures (technical assistance) component may be subject to evaluation/audit following European Commission's standard procedures. Evaluation of the results achieved may be entrusted to independent consultants as well as external audits. Mid-term and final evaluation of the project implementation may be commissioned by the European Commission to assess project performance, achievements and impact.

4.6. Communication and visibility

The programme will follow the orientations of the "Communication and Visibility Manual for EU External Actions" (e.g. press release at the signature of the FA, visibility for reports and studies, etc) available at this address http://ec.europa.eu/europeaid/work/visibility/index_en.htm.

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 areas targeted by the SPSP. The complementary measures (technical assistance) may be used for funding activity(ies) aiming at promoting the programme.