Ex-post evaluation of Macro-Financial Assistance operation to Ukraine over the period 2015-2017

Final Report - Annexes

Written by Juliette Mathis, Oskar Andruszkiewicz, Ana Cordon, Majda Santi (all ICF); Graham Hay, Michael Lee, Jack Spencer (CE); Vitaliy Kravchuk, Kateryna Furmanets (IER)

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Final Report - Annexes

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Annex 1 List of completed interviews

Stakeholder group / category	Entity	Institution	Contact person	Role
EU	European Commission (EC)	DG ECFIN	Joern Griesse	Deputy Head of the Neighbourhood Countries –Macro-financial Assistance Unit
		DG ECFIN	Radostin Neykov	Former Desk officer for Ukraine (MFA I, II, III)
		Former DG ECFIN (now SecGen)	Roxanne Rua	Former Desk officer for Ukraine (MFA III)
		DG TAXUD	Kaido Sirel	In charge of customs issues
		SGUA	Torsten Woellert	Energy expert
		EC	Nicolas Lilienthal	Legal service – non-disbursement decision
		EC	Julio Baquero Cruz	Legal service - non-disbursement decision
		SGUA	Katja Lenzing	Team Justice and Home Affairs / Anti-Corruption
		DG Trade	Nicholas Burge	Former head of trade section in EUDEL in Kyiv
		DG Trade	Jocelyn Guitton	Former trade affairs manager in EUDEL in Kyiv
		DG ECHO	Cristina Martinez-Galligo	Desk Ukraine, ECHO/B.4.

Stakeholder group / category	Entity	Institution	Contact person	Role
	European Union External Action (EEAS) / EU DEL	EEAS	Ulla Hakanen	Team Leader for Ukraine, Eastern Partnership Bilateral Relations
		EEAS	Adriano Martins	Human rights division, Former Deputy Head of Eastern Partnership Bilateral Relations Division
		EU DEL in Kyiv	Stefan Schleuning	Head of Cooperation (EU DEL), Former Head of Financial Cooperation (SGUA)
		EU DEL in Kyiv	Oksana Popruga	Economist at the EU Delegation in Ukraine
		EU DEL Cabo Verde	Jose Roman Leon-Lora	Former head of the section for Economic Cooperation, Regional and Social Development of the EU Delegation to Ukraine. Former team member of SGUA – worked mainly on IDPs issue
		EU DEL in Kyiv	Johannes Baur	Former SGUA member (2014-16) – worked on energy (spec. on SSN) and on SOEs. Now at the EUD in Kyiv
		EU DEL in Kyiv	Manfredas Limantas	JHA team / anti-corruption
		EU DEL in Kyiv	Martin Klaucke	Head of section – PAR reforms
		EU DEL in Kyiv	Fabio Della Piazza	Head of political section 2015-19
		EESC	Katarina Albrechtova	Administrator, External relations

Stakeholder group / category	Entity	Institution	Contact person	Role
		DG CLIMA	Niels Boelling	International Relations Officer - International Forest Policy - EU Timber Regulation
	Member State	Permanent Representation of Poland to EU	Maria Janzcak	Head of Budget and Finance Section
	Businesses and their representatives	Business Europe	Sofia Bournou	Responsible for EU-Russia relations and relations between the EU and neighbouring countries (Eastern Partnership, South-Mediterranean and accession countries)
Ukraine	Ministry of Finance	Ministry of Finance	Yuriy Butsa	Deputy Minister monitoring the reforms implementation in 2016 and 2017 / Debt management department
		Ministry of Finance	Olga Fedorenko Oleksii Kosharnyi	European integration department
	National Anti Corruption Bureau	National Anti Corruption Bureau	Gizo Ugvala	First deputy director
	National Bank of Ukraine	National Bank of Ukraine	Volodymyr Kuchyn Vitalii Vavryshchuk Volodymyr Lepushynskyi Serhii Ponomarenko	- Head, Office for European Integration and International Programs; - Director, Financial Stability Department; - Director, Monetary Policy and Economic Analysis Department; - Director, Open Market Operations

Stakeholder group / category	Entity	Institution	Contact person	Role
				Department.
	Ministry of Social Policy	Ministry of Social Policy	Team dedicated to social programmes	Social assistance programmes
	Civil Society Organisations	Ukrainian Center for Independent Political Research	Svitlana Kononchuk	Political analyst
		NGO"The European Truth" ("Evropeiskaia Pravda") - European Pravda	Yuriy Panchenko	Economic Editor
		Commission on Ethical Journalism / Media Detector	Svitlana Ostapa	Member of the Commission on Ethical Journalism / Media expert / Deputy Editor-in-Chief
		Center of policy and legal reform	Ihor Koliushko	Head of the board (PAR reform)
		Center of policy and legal reform	Mykola Khavronyuk	Expert on anti corruption measures
Wider donors community		IMF	Thanos Arvanitis	On Ukraine fine from 2015 until the end of 2018.
	Other IFIs and multilateral / bilateral donors	EBRD	Ana Kresic	Associate Economist, Eastern Europe and Caucasus
		EBRD	Guiseppe Grimaldi	Energy expert

Stakeholder group / category	Entity	Institution	Contact person	Role
		World Bank	Anastasia Golovach	Economist for Ukraine
		OECD	Klas Klaas	Senior Adviser / Policy Analyst SIGMA programme – PAR reforms
		GIZ	GORDIENKO Olena - Nadiia Rozhko - MARKHAI Sergii	Public Finance Management projects
		Swiss Embassy (SDC and SECO)	Viktor Shutkevych	SMEs and Competitiveness Domain Coordinator

Note that in addition, a roadmap has been launched by the Commission with an aim to inform citizens and stakeholders about the present MFA Ukraine III evaluation and provide them with an opportunity to share their views. The roadmap feedback period was 6 March 2020 – 3 April 2020. Only one response was received during this period. Full details can be found at: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12118-Ex-post-evaluation-of-macro-financial-assistance-to-Ukraine-

Annex 2 Key takeaways from interviews

<u>EU side</u>:

Relevance:

The MFA III operation was the largest operation ever implemented by the EC. This was commensurate with Ukraine's financing needs and a sign of EU solidarity.

Without this financial assistance in particular in 2015, the country would have been on the edge of the bankruptcy.

The size of the financial assistance was not a threat to UA's debt sustainability given the concessional nature of the loan.

The number of conditions was in a way proportionate to the financial envelope and also reflected the extensive coordination which was undertaken.

Every condition was achievable, with some interviewees expressing doubts regarding the one on ultimate beneficiary.

With the benefit of hindsight, a lower number of conditions would have helped to help sustain motivation over time.

Coherence:

The Association Agenda and the DCFTA were used as a reference for the design of the conditions.

The VLAP was also a powerful tool of EU leverage

Technical assistance and budget support provided through other EU programmes were key elements for the implementation of the reforms

Effectiveness:

In macro-economic terms, the situation in 2017 was much different than in 2015. The non disbursement of the third tranche was quite an exceptional occurrence but did not have significant macroeconomic impact in this instance.

UA has made significant progress across many reform areas (public procurement, energy sector), including in anti-corruption.

Lack of progress on conditions blocking the disbursement was attributable to lack of ownership beyond core institutions (NBU, MoF), difficulties in case inter-ministerial coordination or involvement of Parliament, vested interest.

Efficiency:

There are some capacity issues in Ukraine but that is not the main explanatory factor with lack of progress with reforms.

The reform impetus slow downed in 2016 with the change of government.

The communication and coordination among the various institutions on the EU / international side was unanimously regarded as very well done, with significant improvements noted compared to the MFA I and II operation.

EU added value:

The MFA III programme has included non-conventional conditions as IDPs and justice sector reform. That was seen as ambitious and positive.

From the perspective of EU business associations, the MFA III operation and more widely the Association Agreement and the DCFTA was a conveyor of confidence for the private sector. The impacts in terms trade volume, improvements to the business environment have not yet materialised in a significant manner but expectations are high.

Ukrainian side:

Relevance:

The exceptional size of the MFA was welcome.

There were too many conditions including some on aspects of lower importance. Less conditions but more targeted would have been more helpful.

Some conditions, such as the anti-corruption conditions, were too ambitious for the envisaged timeframe.

MFAIV conditions are better designed (less numerous and more precise)

Coherence

Conditions in areas where the EU has technical expertise (e.g. in relation to EU directives) or conditions fully aligned with those of IMF / WB (in areas in which IMF/WB have technical expertise) are most helpful.

Effectiveness:

From a macro perspective the support was really key in 2015. The unconditional disbursement of the first tranche in 2015 was very helpful (even if its shorter maturity was a disadvantage).

In 2017 the situation was better but alternative financing options still limited. It was costly to replace the non-disbursement of third tranche. More advance notice would have been helpful.

Even when conditions are aligned with the country's priorities, having the MFA / EU / international backing helps reformers pushing reforms more quickly (e.g. at the Parliament)

Efficiency:

[For UA authorities]: Lack of sufficient resources (skilled civil servants, IT equipment and budget) were explaining the lack of progress on reforms around electronic asset disclosures system and beneficiary ownership disclosure.

[For UA CSOs]: Lack of pollical will, vested interests are the main impediments to reform.

The lack of flexibility (compared to the IMF) on the formulation of MFA conditions (set in stone ex-ante in the MoU) is not helpful.

EU-added value:

It matters for UA that the support comes from the EU itself.

***IMF and the donor community*:**

Relevance:

Size of EU support smaller than IMF but recognition that the EU was trying to max out its support to UA and importance of the wider package

Relevant conditions but too high number sometimes mentioned as an issue

Coherence:

Concerted efforts, reinforcing programmes and conditions

In a few instances and at the granular level of details, some discrepancies as to which approach to recommend to achieve particular results (e.g. asset declaration)

Effectiveness:

There were very clearly different macro economic conditions in 2015 versus 2017.

Many key reforms were completed in a relatively short time

Non disbursement decision was logical given the lack of progress on key reforms at the time.

Efficiency:

Need to fine-tune the wording of conditions notably: leaving no room for interpretation, focusing on key aspects achievable within the timeframe of the operation. Recognition that conditions implying a vote of the Rada may be difficult to implement.

EU added value:

EC political role brings added value in the joint efforts of the international donor community.

Annex 3 Focus Group Discussion – Summary Note

A3.1 List of participants

Invitees

- Yaroslav Zhalilo, Deputy director, head of center for economic studies, NISS – National Institute for Strategic Studies
- Maria Rapko, Deputy executive director Centre for Economic Strategy
- Olexii Chugaiev, Associate Professor Institute of International Relations
- Ilona Sologoub, CEO, Ukraine VoxUkraine
- Olexii Dorogan, CEO, Better Regulation Delivery Office (BRDO)
- Andrii Borovyk, Executive Director Transparency International Ukraine
- Kateryna Laba, Ukraine Project Manager, Institute for War and Peace Reporting

Study Team

Facilitator

- Charu Wilkinson, ICF associate

Presenters

- Juliette Mathis, ICF
- Katerina Furmanets, Institute for Economic Research and Policy Consulting
- Oskar Andruszkiewicz, ICF

Study team

- Majda Santi, ICF
- Vitaliy Kravchuk, Institute for Economic Research and Policy Consulting
- Ana Cordon, ICF

A3.2 The presentation

The study team presented some slides on each aspect covered during the Focus Group to kick off the discussion. To see the presentation, please access the attached file:

20200528_MFA UA III_ online FG presenta

A3.3 PART 1 – High level discussion on design and implementation issues

A3.3.1 Added value of the MFA

A3.3.2 Visibility / awareness

The overall message on the visibility / awareness of the MFA is that it remains patchy depending on the audience and the reform area. Often, the knowledge, even among experts, is limited to some key facts (amount, number of tranches, link to the IMF programme). Knowledge of the specific conditionality is negligible.

The main channels of information on the MFA include mostly the newspapers, online media and sometimes debates on TV. The specialised economics press provides more in-depth reviews of the MFA programme.

Contributory factors behind the low awareness include:

- Public finance and macroeconomic issues may be quite complicated for the general public (NB: although the public can show interest for technical discussions on Eurobond issuance so it cannot be the sole explanation);
- The information on MFA conditionalities and financial aspects of the support (e.g. the interest rate) was not publicised enough. Publicity on the impacts of the reforms promoted by the MFA is also lacking;
- MFA programmes are conducted in parallel with other EU programmes, programmes from other IFIs, making it harder to distinguish the source of the funding.

One exception to the otherwise low awareness is the focus of the MFA on anti-corruption, with specific MFA conditions being widely discussed in the media, also thanks to the communication leveraged by some Civil Society Organisations (CSOs).

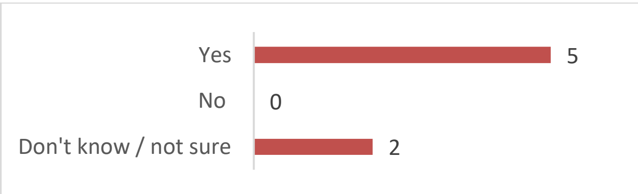
A3.3.3 Attitudes towards the EU among the general public

Opinion polls conducted by the Pew Research Center[1] showed that the share of people who had favourable opinion about the European Union (EU) in Ukraine (UA) raised from 72% to 79% between 2015 and 2019. In parallel, the share of people who had an unfavourable opinion on the EU decreased from 19% to 11%. MFA III was part of the overall EU package to Ukraine which altogether may have contributed to the positive image of the EU.

Despite this otherwise positive image, one participant pointed out that some Russian inspired narratives emerged on the negative impact of foreign assistance in Ukraine[2]. More generally, the MFA requirement to lift the wood export ban was negatively perceived among the focus group audience. It was reported that it was the case of the general public as well, which reportedly sometimes wrongly attributed linked the lifting of the wood export ban to the IMF programme. It was seen as non-relevant for the general reform shift in Ukraine and reflecting the lobbying activities of EU businesses.

A3.3.4 Non-disbursement of the third tranche

Figure 1. Given the unmet conditions, was the decision of the EU not to disburse justified?



Source: Online Focus Group 29 May 2020, sli.do. n = 7

Welcoming the disciplinary effect, the majority of the participants thought that it was justified to cancel the disbursement of the third tranche given the non-fulfilment of some of the conditions. The EU credibility was at stake and turning a blind eye on major shortcomings in reform progress by Ukrainian authorities would have sent the wrong signal that the EU is ready to compromise on its reform requirements in the area (anti-corruption) where its role has been well recognised over the recent years. In addition, the EU had already shown some

[1] https://www.pewresearch.org/global/database/indicator/28

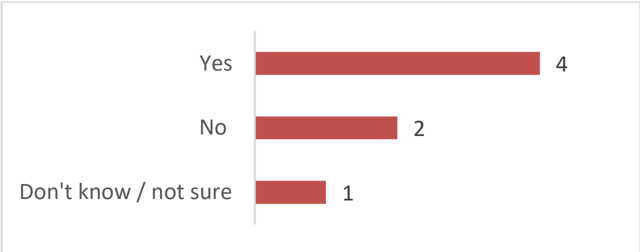
[2] Note that this was also captured by the social media analysis conducted as part of the evaluation of the MFA I and II to Ukraine

flexibility when disbursing the second tranche, with delays, thanks to the use of waivers.

In that context, participants do not support a pure "check list approach" and if the wood export ban had been the only blocking condition, they would not have found the decision justified (as this issue is not central on Ukraine's path to reform).

Besides, some participants noted that the non-disbursement should remain exceptional, otherwise it may undermine the EU-UA relationship. The following trade-off was mentioned: by being too strict in an attempt to enforce the reforms without considering some contextual factors, one may risk to push Ukraine towards Russia, similarly to what happened to Moldova now benefiting from financing from Russia.

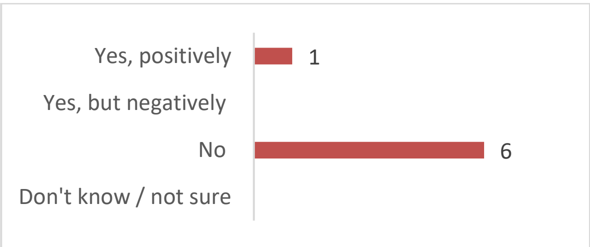
Figure 2. Has the non-disbursement of the third tranche been publicized in the media in Ukraine?



Source: Online Focus Group 29 May 2020, sli.do. n = 7

Participants added that, when covering the EU non-disbursement decision, the media was mostly neutral towards the EU but negative towards the Ukrainian president (Petro Poroshenko) at the time. Higher coverage would have helped the general public to put an increasing pressure on the government to implement the required reform in the future.

Figure 3. Did the non-disbursement of the third tranche affect your perceptions towards the EU?



Source: Online Focus Group 29 May 2020, sli.do. n = 7

Participants' perceptions towards the EU have generally not been affected by the non-disbursement decision (or if at all only positively, reinforcing EU credibility).

Participants had no comments on whether the impact of the non-disbursement would have been different if the economic context had been more difficult or if MFA IV had not been proposed quickly after.

A3.3.5 EU and Macro-Financial Assistance III contribution to Ukraine reform efforts

From the discussion it emerged that there are two types of reforms in UA:

- those responding to the '*sandwich principle'*: at the top there are international institutions (EU, IMF, US), at the bottom the CSOs and in between the Ukrainian government.
- those where the '*sandwich principle'* is not needed (given the sufficient ownership / other drivers of a reform) but where the international support can still play a role to support the ongoing efforts. According to opinion polls, western countries are always mentioned at least in the top 5 when prompting about the main reform engine in the country.

Overall, conditions were assessed as quite technical, but there was a balance between UA and EU originating conditions. The general idea is that in some areas, without the MFA, reforms would still have been implemented but the reform process would have been slower / there would have been gaps in implementation. In other areas, i.e. strategic reform areas (such as anticorruption and judiciary sector, PAR), the EU showed the necessary direction of travel. In such cases where the EU push had to be stronger, participants consider that the progress made is at times limited (e.g. PAR). However, without the EU support, there would have been no reform attempt at all.

A3.4 PART 2 – Deep-dive into selected reform areas

A3.4.1 Anti-corruption & justice reform

Overall, it should be noted that anti-corruption reforms happened for two reasons: first, a strong demand from the public and secondly, a strong push from international partners of UA.

One participant used the analogy of traffic lights to illustrate the EU role (and importance) in the fight against the corruption in Ukraine. If the EU gives a green light for the disbursement on account of the progress in the anti-corruption conditionality, this is seen as a general sign of progress in this area in the country. By analogy, non-disbursement – red light, is seen as overall regress in this area.

Regarding the electronic asset declarations system, there was indeed some divergence in the requirements from the international players: the IMF requested declarations for fairly narrowed cohort of top officials while the EU, supported by CSOs, preferred a much wider typology of public officials. In view of one participant, with the benefit of hindsight, it seems that the IMF position was more feasible given the resource needs to do the checks. Now, the fact that the system was designed to have a wide coverage does not per se explain the non-disbursement. The lack of progress was, to a significant extent, linked to the fact that it was not prioritised by the authorities. The lack of good will of the government can also be read from its willingness to apply the system to activists and to public sector job applicants (excess of zeal). Moreover, any progress made in this area thanks to the asset declaration system was undermined by the fact that judicial procedures of anti-corruption cases were stopped in the courts.

Regarding the beneficial ownership condition, one participant clarified that the rationale behind the condition was clear to the UA authorities, but there was no willingness to implement the system. That said, the ambition level of this condition was found by some participants as too high. Regarding the verification mechanisms which needed to be put in place, there was no international template for it. Participants believed that it was not fair to ask UA authorities to implement a system that does not exist yet in the EU (as some EU countries do not even have the necessary registries in place). In the end, Ukraine had to go faster than other EU countries and became the first country in the world to commit to integrating with the Open Ownership Register.

Some participants reckoned it would be hard for MFA to go beyond the promotion of the "technical" aspects of the reforms. Given the fears about external interference already present in Ukraine, more political moves could be negatively perceived, especially in case not all goes according to plan.

A3.4.2 Business Environment

Business environment / deregulation was painted as an area already quite high on the agenda of UA policy makers. The focus of the CSOs/ business associations in that context was on the nuanced negotiation of the priorities / sequencing rather than needing to indicate direction of travel. The availability of local resources - financed by donors – remained one key facilitating factor in that conducive context: very hands-on technical assistance was provided, going beyond advising policy makers in the general sense and also helping with drafting many acts.

Some obstacles to reforms and challenges when implementing reforms were mentioned. Those included: the need to avoid creating tax gaps while easing the tax burden, the need to tackle corruption issues and tax evasion from entrepreneurs and the need to increase the performance of the authorities at the local level. There is also an issue with *institutional memory* (better handover is needed when transitioning from one technical assistance project to another, and more should be done to paint a precise overview of progress made and next immediate priorities).

Overall, the general opinion among focus group participants was that there were progresses in the business environment reforms despite the remaining limitations (e.g. the influx of Foreign Direct Investment is still low as compared to GDP). Further steps are however needed (regarding the simplification of procedures for starting business, the insurance of properties rights, the rule of law, the stability of currency change, the quality of the products).

The inclusion of the wood export ban condition was widely regarded as unfortunate, and political from day 1. As one participant explained, over the lifetime of MFA III, the pre-requisites were simply not there for the export ban to be lifted. As such, the MFA condition gave the impression that the EU wanted to undermine UA environmental efforts, while the MFA could have instead introduced conditions directly related to the reform of the forestry sector (to ensure transparency, accountability, tracking, etc). This alternative approach would have been perceived more positively.

A3.4.3 Public Administration Reform

Overall, the views on progress made are mixed. In any case, despite the tangible progresses which may or may not have been made, there is consensus that positive outcomes were not reached. The public administration still does not work efficiently. Some participants were more positive and flagged that some aspects of the PAR reforms were quite successful (e.g. PAR directorates) despite the slow pace of the implementation which is understandable given (i) the nature of the reforms, taking time (3/4 iterations and some reversals are typically to be foreseen)and (ii) the top down approach for the PAR reform (the government was not in the main driving seat here).

The PAR reform is, however, incomplete. The following ideas were put forward:

- the possibility to better use the leverage of internationally trained experts;
- the need to support the civil servant salary reform (for now, those working outside the directorates but still performing important duties are receiving a lower salary);
- the need to focus on the local level as well.

Annex 4 Analysis of the Delphi Survey on the Ex-post evaluation of the third Macro-Financial Assistance (MFA III) operation in Ukraine over the period 2015 - 2017

A4.1 Introduction

Out of 54 invitations sent, 21 experts from different organisations participated in the survey (39% response rate). The survey was launched on 19 March 2020 and remained open for almost 4 weeks. Initially, the closure date was due on 27 March 2020, but this deadline had to be extended until 14 April 2020 due to a number of received answers lower than expected and the outbreak of Covid-19. Three reminders were sent and additional follow-up on the phone has been undertaken by IER.

The structure of the survey questionnaire is divided in four sections: Section A: General Information; Section B: Macroeconomic situation in Ukraine over the period 2015-17; Section C: Impact of conditionality attached to the MFA III; and Section D: Social impacts of the MFA III operation. Section A relates to respondents' familiarity with MFA III. Conversely, Section B explores the macroeconomic situation in the country during the period of study and covers questions on real GDP/economic growth, external sustainability and alternatives available to Ukrainian authorities. The impact of conditionalities tied to MFA III is assessed under Section C, while Section D focuses on the social impacts derived from it.

A4.2 Objective

The Delphi survey sought to establish views on the role and contribution of the MFA III in achieving macroeconomic stability, easing external financing constraints and alleviating Ukraine's balance of payments and budgetary needs; and promoting structural reforms over the period 2015-17.

The recruitment to the panel was carried out with the support of the local research team at IER and with advice from DG ECFIN and the EU Delegation in Kyiv. We included 54 representatives of the following groups / institutions in the Delphi panel:

- Business representatives and financial / macroeconomic analysts from the private sector (e.g. research departments of commercial banks); and
- Researchers from think tanks, experienced commentators of Ukrainian economic policies (i.e. specialized press), independent fiscal policy experts, and academic experts.

Twenty-one respondents provided complete answers which resulted in a 38.89 per cent response rate in the first round of the Delphi survey. Respondents included representatives from think tanks, academia, banks, credit rating agencies, investment funds, media and consulting.

Table 1 provides the details of the background of respondents by type of organisation.

Table 1. Details of the Delphi Panel that were invited and responded

Type of organisation	Number of invitees	Number of respondents 1st round
Bank – research department	9	2
Businesses and their representatives	4	0
Civil society organisations	6	4
Credit Rating Agency	5	2

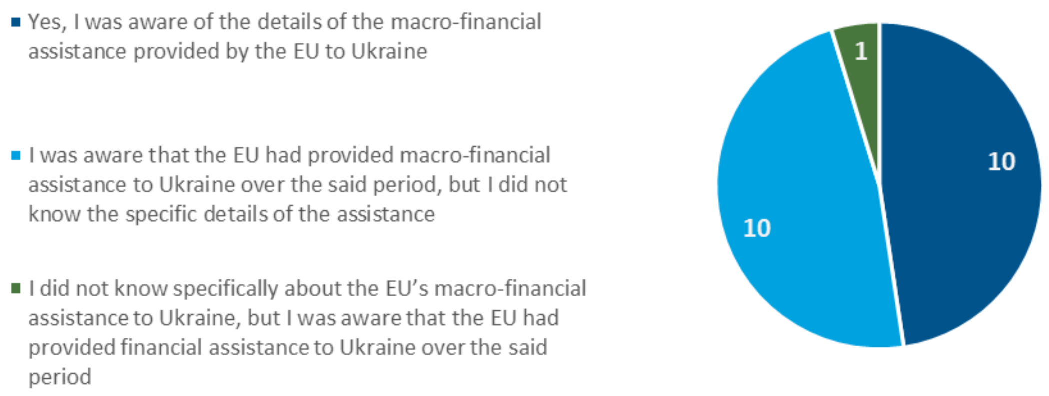
Type of organisation	Number of invitees	Number of respondents 1st round
Media / Think tanks / academics	20	8
Media / Think tanks / academics/ civil society organisations (EU side)	3	2
Research Consultancy	5	1
Investment Bank	1	1
Other	1	1
Grand Total	**54**	**21**

A4.3 Section A: General Information

Figure 4 reveals that the vast majority of respondents (20) were aware of the fact that the EU had provided Macro-Financial Assistance III to Ukraine over the period 2015-17. However, only 10 of them were aware of the specific details of the macro-financial assistance provided to Ukraine. Only one person affirmed not to know specifically about the EU's MFA III, but was instead aware that the EU had provided assistance to Ukraine over the said period.

Figure 4. Familiarity of respondents with EU's MFA III to Ukraine

Question A2. Before receiving an invitation to this Delphi questionnaire, were you aware of the fact that the EU had provided Macro-Financial Assistance III to Ukraine over the period 2015-17?



Base: all (n=21)

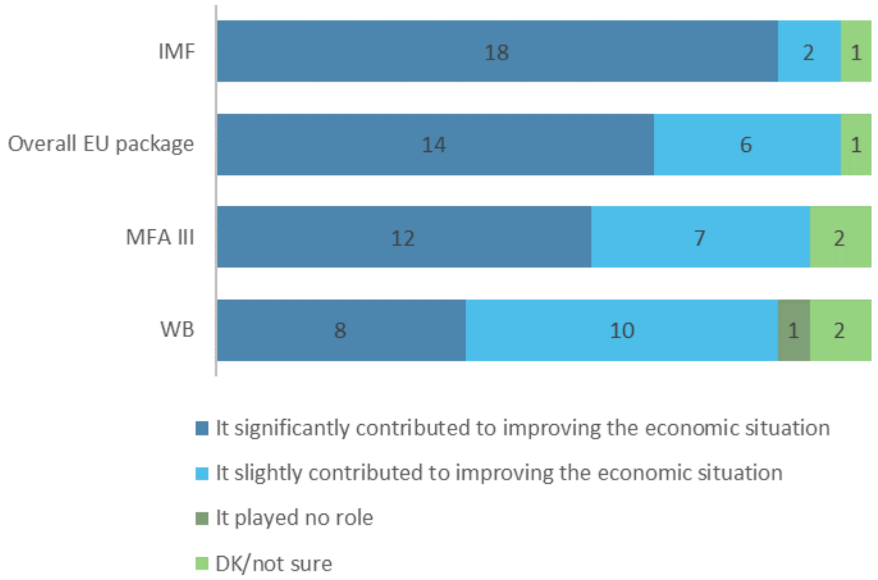
A4.4 Section B: Macroeconomic situation in Ukraine over the period 2015-17

A4.4.1 Real GDP / Economic growth

Participants were asked about the impact different foreign donors had in improving the economy of Ukraine over 2015-17 (see Figure 5). In respondents' views, the overall EU package and IMF seem to be the most contributing financial assistance programmes. Regarding IMF, the large majority of respondents considered this assistance "*significantly contributed to improving the economic situation*" (18). The overall EU package is given the same appreciation by 14 respondents; whereas 6 of them believed it "*slightly contributed to improving the economic situation".* When it comes to MFA III, more than half said this operation *"significantly contributed to improving the economic situation"* (12) and one third thought it "*slightly contributed to improving the economic situation"* (7). In the opinion of 8 participants, the World Bank (WB) contributed significantly to improving the economic situation – whilst almost half of them believe it slightly contributed (10). One person considered that the WB played no role in the improvement of the Ukrainian economy.

Figure 5. Contribution of foreign financial assistance to improving Ukrainian economy

Question B3. What role did foreign financial assistance play in improving the economic situation of Ukraine over 2015-17?



Base: all (n=21)

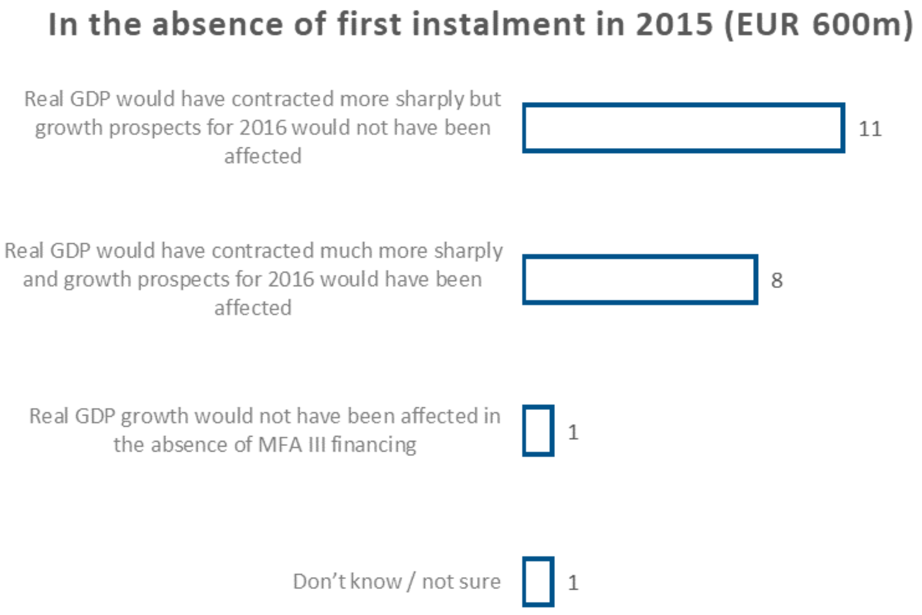
Question 4 explores possible counterfactual scenarios in the absence of MFA III support (Figure 6). First, respondents are asked about the economic consequences had the first instalment of the MFA III (EUR 600m) not been made available to Ukraine in 2015.In this sense, the majority of participants (11) believed that the "*real GDP would have contracted more sharply but growth prospects for 2016 would not have been affected*". Here, one person argued that "*In 2015, MFA was critical to support macro financial stability".* By contrast, 8 out of 21 respondents considered that the "*Real GDP would have contracted much more sharply and growth prospects for 2016 would have been affected"* had the first tranche not been made available. Reasons given for this are the active was that was ongoing in 2015 in the Donbas region and the economic crisis. This was followed by one person arguing that "*real GDP growth would not have been affected in the absence of MFA III financing"* on the basis that *"In 2015, the international rescue package led by the IMF (of which MFA from the EU was effectively part) did NOT contribute to economic growth in Ukraine, since it had a conditionality of fiscal austerity which suppressed growth in Ukraine. By 2017, fiscal policy was already relaxed considerably."*

When it comes to the scenario in the absence of the second tranche in 2017, the large majority (17) agreed that the most plausible hypothesis is that the *"real GDP growth would have been lower*" as, in words of one respondent, "*the MFA-III provided the government with money needed to finance its obligations, including the increase in investment projects*.". In the same vein, another said that "*MFA III volume less compared to IMF package. Yet it provided necessary pressure for reforms to continue, especially in 2017*". By contrast, 3 out of 21 people believed that the "*real GDP growth would not have been affected"* had the second tranche of MFA III not been disbursed since "*In 2015, MFA was critical to support macro financial stability. In 2017, Ukraine was much more stable and issued USD 3 bln Eurobonds on the external market to ensure public debt refinancing"*

In the opinion of one expert, the situation was much better in 2017, so the impact would be higher if 2015 loan was more sizable, covering more significant amount of budget deficit so that the NBU would not have to monetize it thus pushing inflation higher. In 2015 the hidden deficit was close to 10% of GPD (banks, Naftogaz, general government deficit), while in 2017 it was much lower.

Figure 6. Counterfactual scenarios in the absence of the first and second instalment in 2015 and 2017

Question B4. Hypothetically speaking, had the MFA III loan not been made available to Ukraine, how would it have affected economic / real GDP growth over the said period? Please indicate what you think would have been the most plausible outcome in the absence of the MFA III loan, separately for 2015 and 2017.



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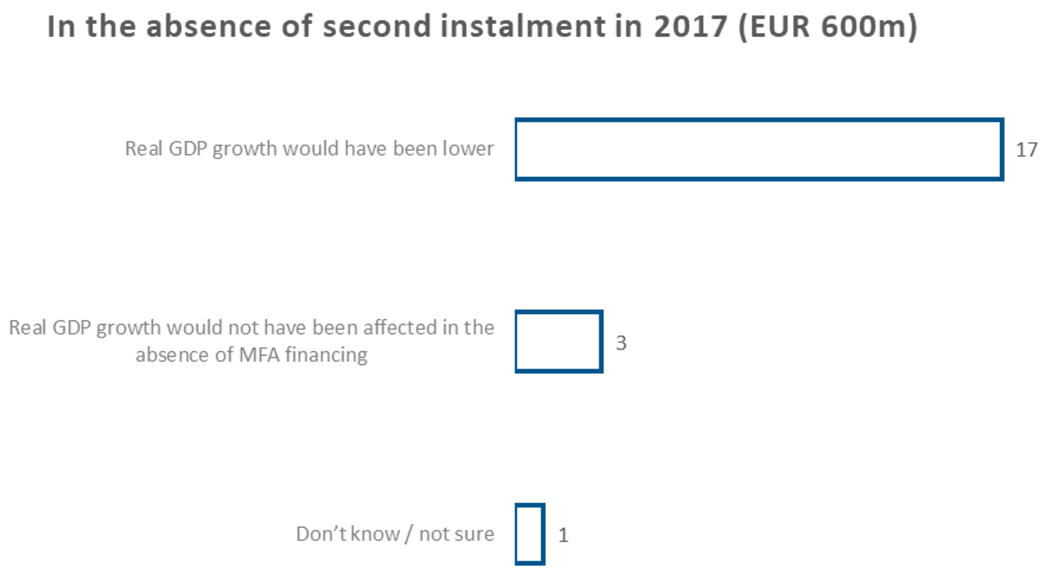

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A4.4.2 External sustainability

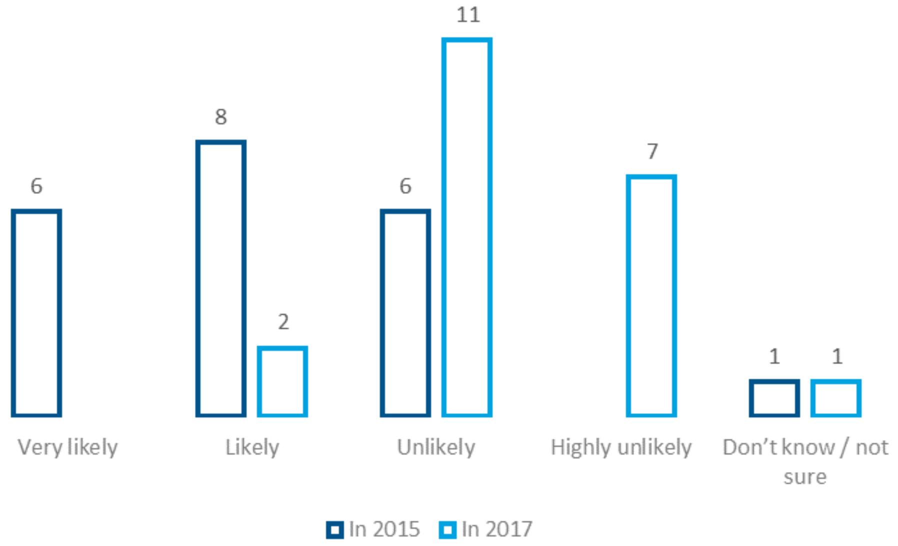
Respondents' views on the likelihood of sovereign default over the period 2015-17 differ when considering different scenarios: i) without MFA III; ii) without MFA III nor other international assistance.

When it comes to the first scenario (without MFA III), Figure 7 reveals that some respondents (6) said a sovereign default would have been "*Very likely*" and some others (8) stated that it would have been "*Likely*" in the absence of the first tranche in 2015. On the contrary, up to 6 respondents believed this would have been "*Unlikely*" to happen. Different answers are observed when asked about the likelihood of a sovereign default had the second instalment not been disbursed in 2017. In this case, the majority (11) think a sovereign default would have been "*Unlikely*" to occur; whereas a third of respondents (7) say this possibility is "*Highly Unlikely*". Only 2 out of 21 respondents considered it would have been "*likely*" to have a sovereign default in 2017 without MFA III.

Figure 7. Likelihood of a sovereign default in the absence of MFA III to Ukraine

Question B6. What, in your view, would have been the likelihood of a sovereign default occurring…

a …had the MFA III financing not been available to Ukraine? [provided that the other international assistance remained available]



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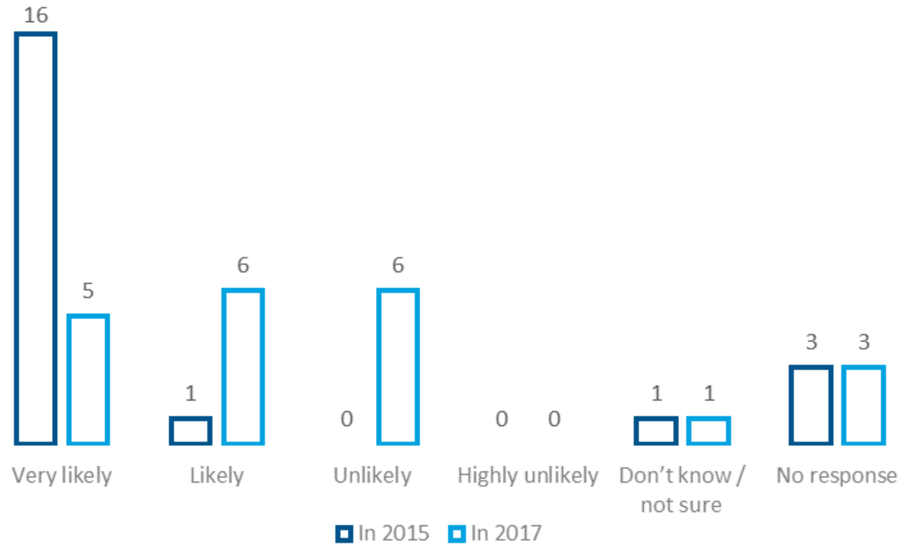
The second scenario (Figure 8) shows greater degree of agreement among respondents when considering what would have happened in the absence of MFA III and other international assistance. In the opinion of 3 in 4 respondents (16), a sovereign default would have been "*Very likely*" without external assistance in 2015. Whereas for 2017, a number of 5 respondents considered that risk of sovereign default would have been "*Very likely*". Likewise, 6 out of 21 participants stated that the probability of a sovereign default in the absence of MFA III nor other international assistance would have been "*Likely*". By contrast, the same number of respondents (6) considered this would have been "*Unlikely*" to happen.

Differences between both scenarios are explained by some respondents. One expert argued that default would have been more likely if IMF program was not in place since it acted as an anchor for other financing. It is generally agreed that Ukraine was much more stable in 2017 from a macro-financial perspective than in 2015. Therefore, another respondent added, "*sovereign default was more likely in 2015, and MFAIII formed a part of 'reanimation package' of macro-financial support*". In other expert's view, Ukrainian credibility was better in 2017 than in 2015.

Figure 8. Likelihood of a sovereign default in the absence of MFA III nor other international assistance to Ukraine

Question B6. What, in your view, would have been the likelihood of a sovereign default occurring…

b …had neither MFA III financing nor the other international assistance been available to Ukraine?



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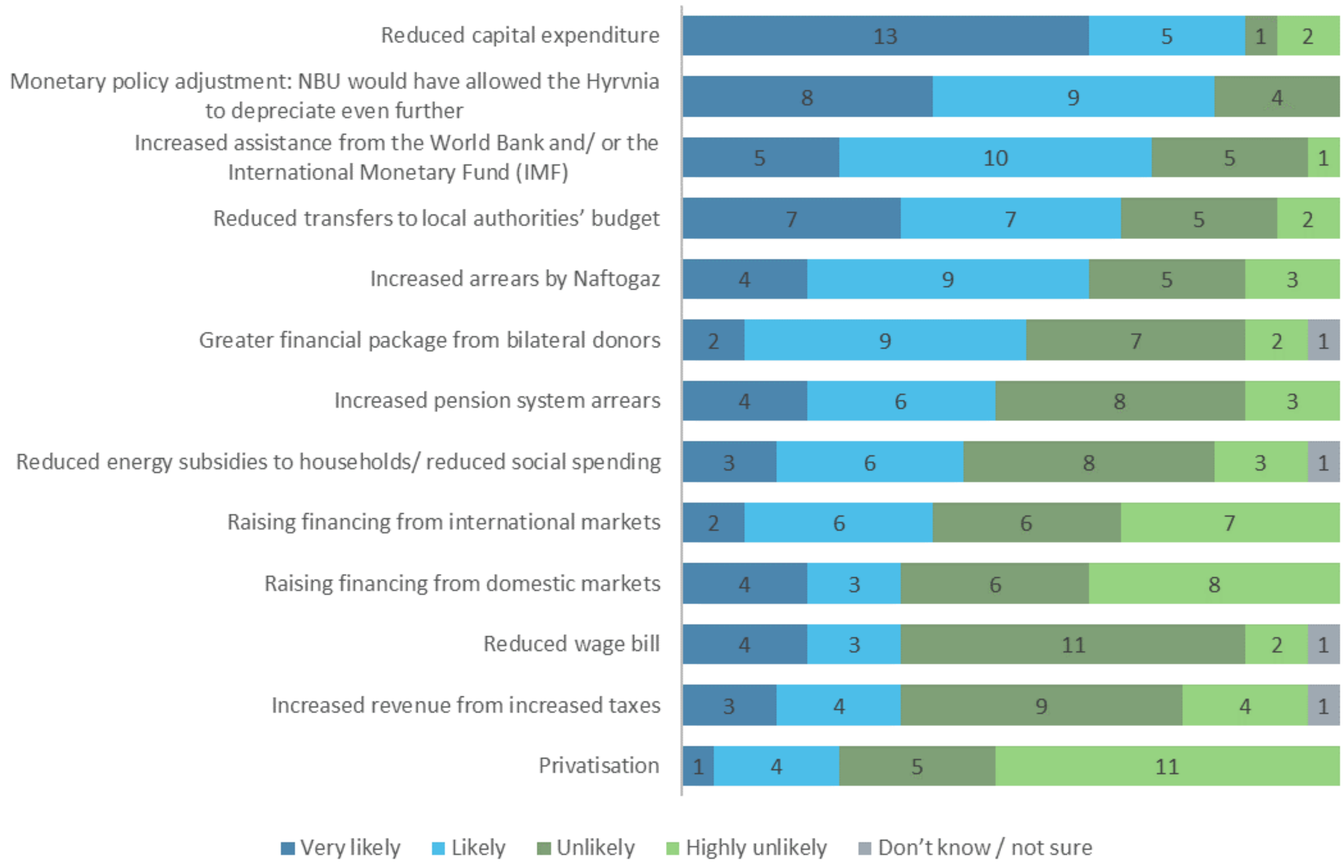
A4.4.3 Alternatives available to Ukrainian authorities

Following with the counterfactual exercise, Question 8 studies possible alternatives the Ukrainian authorities would have had to pursue in the absence of MFA III. Had the first tranche of MFA III not been disbursed in 2015, Figure 9 shows what respondents think that the Ukrainian authorities would have opted for: Reduced capital expenditure (18); Monetary policy adjustment: NBU would have allowed the Hyrvnia to depreciate even further (17); Increased assistance from the World Bank and/ or the International Monetary Fund (IMF) (15); Reduced transfers to local authorities' budget (14); Increased arrears by Naftogaz (13); Greater financial package from bilateral donors (11); Increased pension system arrears (10).

Figure 9. Alternatives Ukraine would have taken in the absence of the first instalment of MFA III in 2015 (EUR 600m)

Question B8. In the absence of the MFA III loan, the Ukrainian authorities would have had to pursue alternatives. What action(s) would have been taken by the Ukrainian authorities had the MFA III loans not been available?

In the absence of the first instalment in 2015 (EUR 600m)



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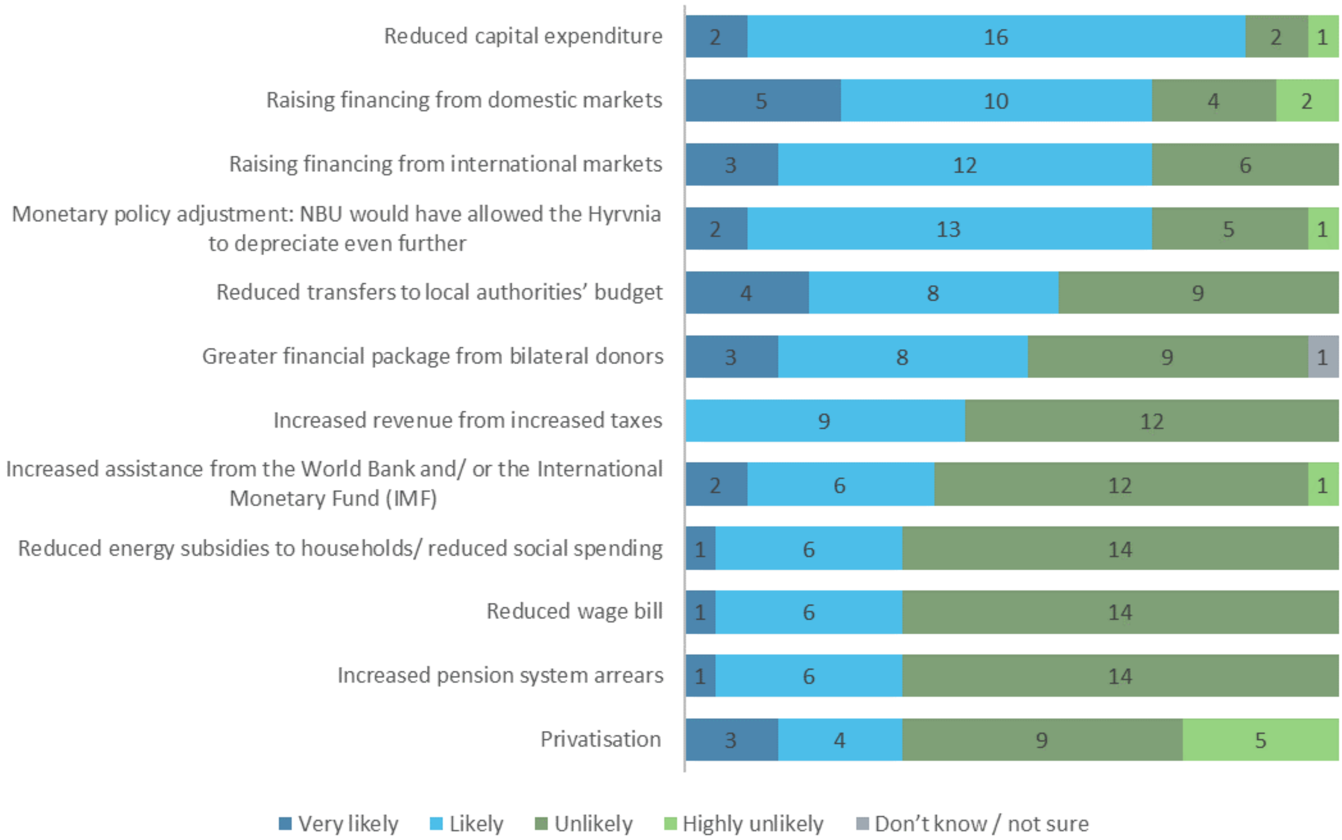
When it comes to the 2017 scenario in the absence of the second tranche, respondents consider that the most plausible alternatives would have been: Reduced capital expenditure (18); Raising financing from domestic markets (15); Raising financing from international markets (15); Monetary policy adjustment: NBU would have allowed the Hyrvnia to depreciate even further (15); Reduced transfers to local authorities' budget (12); Greater financial package from bilateral donors (11).

Figure 10. Alternatives Ukraine would have taken in the absence of the second instalment of MFA III in 2017 (EUR 600m)

Question B8. In the absence of the MFA III loan, the Ukrainian authorities would have had to pursue alternatives. What action(s) would have been taken by the Ukrainian authorities had the MFA III loans not been available

In the absence of the second instalment in 2017 (EUR 600m)



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Question 9 continues with the speculation exercise and proposes respondents to indicate, for those alternatives selected under question 8, the most likely amount of funding that each alternative would have brought to cover for the missing loan (EUR 600m in 2015 and EUR 600m in 2017). The results of this question are not reported here as these are really hard to interpret at an aggregated level. One learning which becomes evident from the ventilation exercise is that respondents tend to see the alternative to an MFA loan as a combination of several different alternatives: they have typically spread the EUR 600 mln across four or six different alternatives and have not used this question to flag their one or two most plausible alternatives.

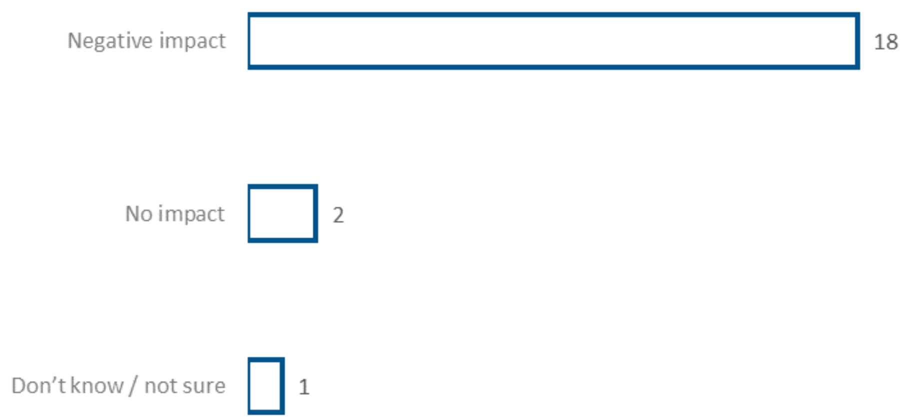
The third and last tranche of MFA III was due to be disbursed in Autumn 2017. However, this third instalment (EUR 600m) was never been disbursed due to Ukraine's failure to meet a number of significant conditions related to anti-corruption, trade and financial sector reforms. Therefore, Question 10 proposes now a positive counterfactual exercise and Figure 11 reveals what, in the opinion of respondents, has been the likely economic and political impact derived from the non-disbursement of the third tranche. Regarding the economic impact resulting, the vast majority of experts asked (18) indicated that the non-disbursement of the third tranche had a negative impact. One respondent argued that "*The non-disbursement and delay with IMF program further constrained government's capacity to reduce refinancing risks and enter the 2019 electoral year with the economy in a better position."* Additionally, another respondent noted that "*Negative impact was caused by non-implementation of conditions rather than by not receiving the tranche per se*". Whereas only 2 out of 21 respondents believed that it did not have an impact in the Ukrainian economy, on the basis that "*by that time MFA assistance was no longer crucial*".

When it comes to the political impact, answers received seem to be more balanced. Up to 9 people agreed that the non-disbursement had a negative political impact; whereas 8 of respondents said that there was no political impact resulting from the non-disbursement of the third tranche. Interestingly, 1 participant specified that the non-disbursement generated a positive political impact, as this gave a "*strong signal of the importance of the continuing reforms in the anti-corruption area, rule of law, etc.*" and created *"leverage of EU towards Ukrainian authorities - nudge to reforms".*

Figure 11. Non-disbursement of the third tranche of MFA III: economic and political impact

Question B10. The third tranche of EUR 600 mln under MFA III has not been eventually disbursed given a number of important commitments not being fulfilled, including with respect to the fight against corruption, international trade obligations and financial sector reform.

Could you please specify what has been the likely economic impact of non-disbursement of the third tranche:



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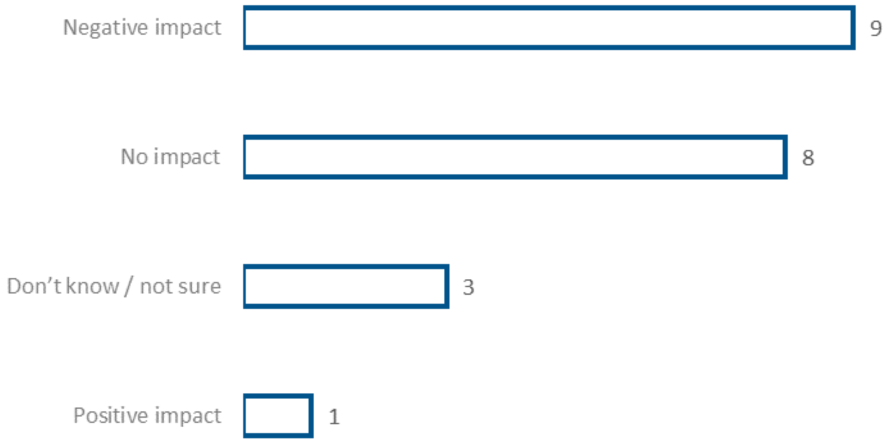
Could you please specify what has been the likely political impact of non-disbursement of the third tranche in Autumn 2017:



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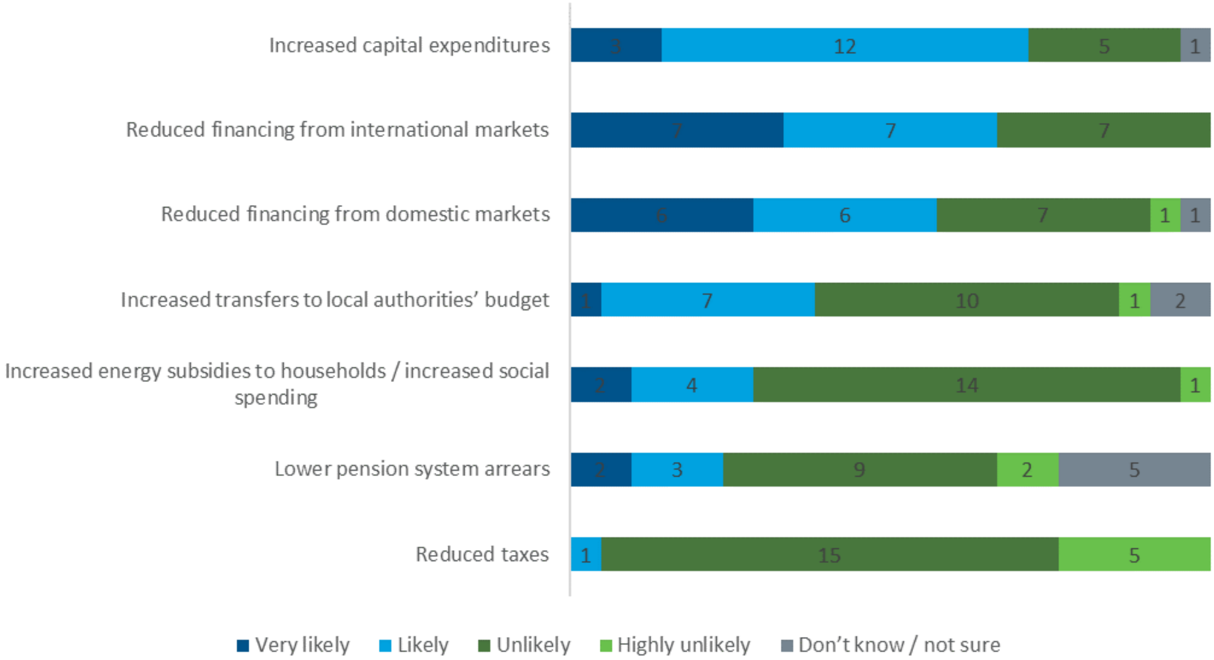
Then, respondents are asked what actions the Ukrainian authorities would have been taken had the third tranche of MFA III been made available in Autumn 2017 (EUR 600m) (Figure 12). According to respondents, the most plausible actions that Ukraine would have taken are: Increased capital expenditures (15); Reduced financing from international markets (14); Reduced financing from domestic markets (12); Increased transfers to local authorities' budget (8)

Figure 12. Alternatives Ukraine would have taken in the presence of the third instalment of MFA III in Autumn 2017 (EUR 600m)

Question B11. What action(s) would have been taken by the Ukrainian authorities had the third tranche of the MFA III loan be available (in addition to the first two)?

Had the third instalment been made in Autumn 2017 (EUR 600m)



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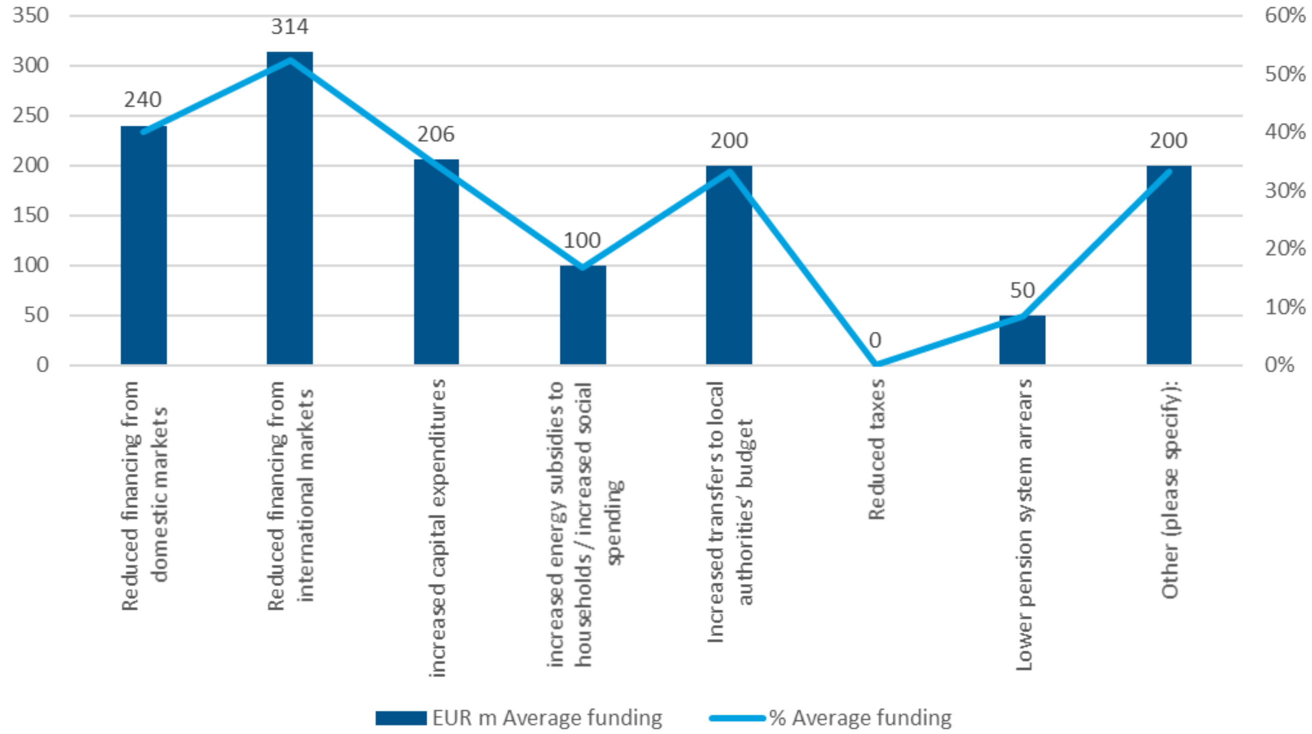
Following with the counterfactual scenario in the presence of the third tranche of MFAIII, respondents are now asked to estimate what would have been the most likely use of the EUR 600m, among those responses selected under question 11 (Figure 13). On average, respondents indicated that more than half the funding (52%) would have gone to reduced financing from international markets and 40% of it to reduced financing from domestic markets. Likewise, on average participants believed that 34% of the third tranche would have been used to address increased capital expenditures and 33% of the loan to address Increased transfers to local authorities' budget.

Figure 13. Possible uses of the third tranche (EUR 600m) had it been disbursed in Autumn 2017.

Question B12. You think that there were several possible alternative course of events in case of the disbursement of the third tranche in Autumn 2017 (in addition to the first two). Could you please indicate what would have been the most likely use of the €600 m? Note that the total needs to add up to €600 million



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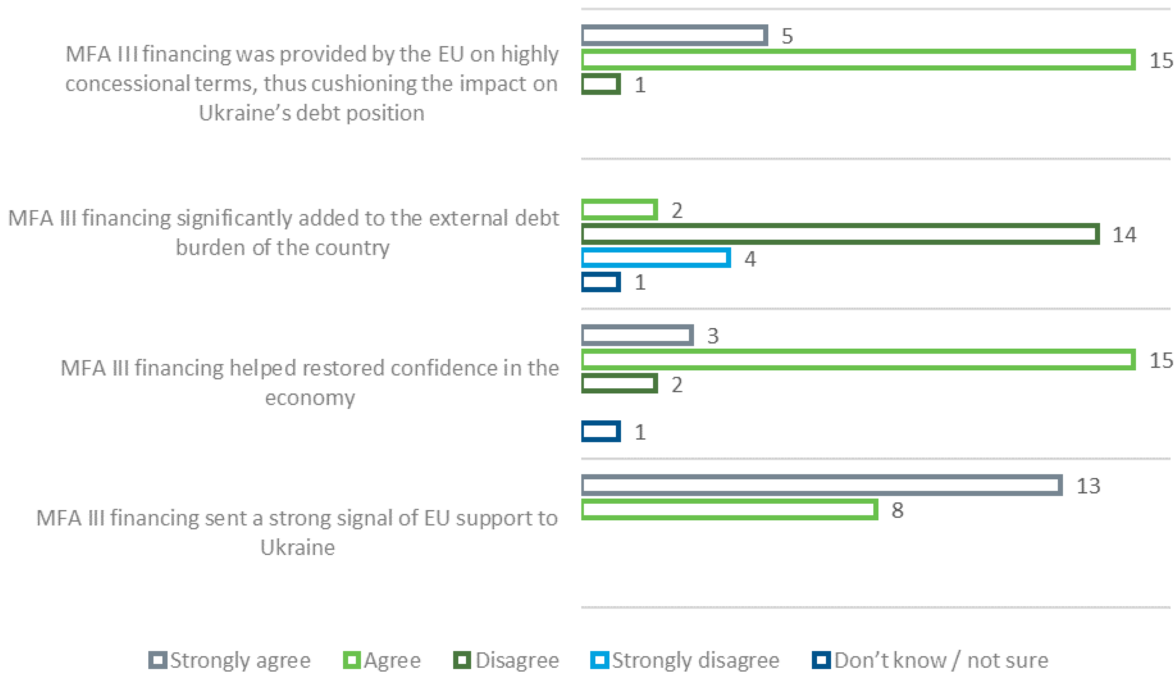
Afterwards, the relevance of the MFA III financing is assessed in respondents' eyes (Figure 14). The vast majority of participants (20) agreed or strongly agreed with the statement that "*MFA III financing was provided by the EU on highly concessional terms, thus cushioning the impact on Ukraine's debt position*". Likewise, most of respondents (18) agreed or strongly agreed that "*MFA III financing helped restored confidence in the economy".* Additionally, the totality of participants (21) agreed or strongly agreed that "*MFA III financing sent a strong signal of EU support to Ukraine*". Conversely, 18 out of 21 respondents disagreed or strongly disagreed with the statement that "*MFA III financing significantly added to the external debt burden of the country*"

Figure 14. Relevance of the MFA III operation to Ukraine

Question B13. Please indicate the extent to which you agree or disagree with the following statements



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A4.5 Section C: Impact of conditionality attached to the MFA III

The aim of this section is to analyse the influence of the conditions tied to MFA III financing in Ukraine and the different reform areas. The counterfactual exercise undertaken in Question 14 (Figure 15) looks to identify what progress Ukrainian authorities would have made in the reform areas without the assistance of the MFA III operation.

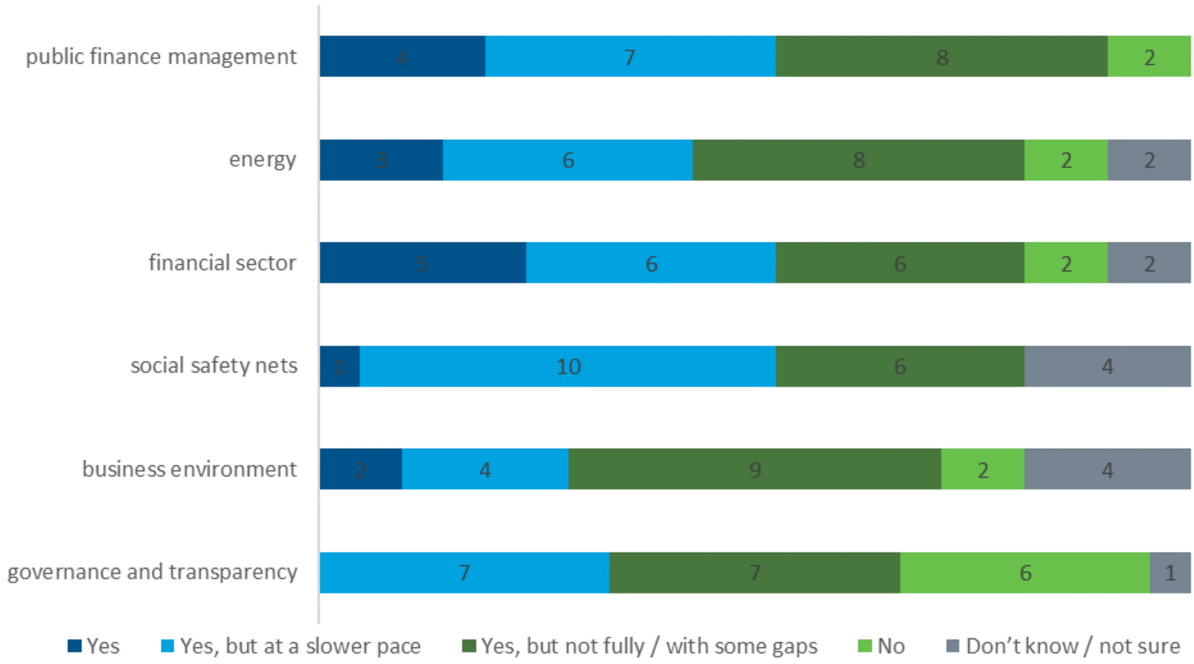
Regarding the public finance management reform area, the wide majority of respondents (19) are positive that Ukrainian authorities would have made progress in this area without MFA III anyways. Specifically, one third of respondents (7) answered "*Yes, but at a slower pace*" and 8 of them said "*Yes, but not fully / with some gaps*". As for the energy area, 17 out of 21 participants agreed that Ukraine would have pushed forward in the energy reform area. However, 8 respondents noted that this progress would not have been fully but with some gaps; and 6 of them believed that progress would have gone at a slower pace.

When it comes to social safety nets, 17 out of 21 participants indicated that Ukraine would have continued with its reforms in this area. Nevertheless, 10 of them believed that progress in social safety nets would have been made at a slower pace without MFA III. According to 17 respondents, progress in reforming the financial sector would have continued in the absence of MFA III anyways. This can be explained, in words of one respondent, as "*quite strong conditionality in areas of finance from other donors/partners/lenders of Ukraine*". Likewise, up to 15 experts said that Ukrainian authorities would have pushed through progress in the business environment reform area anyways. However, 9 of them specified that progress in this area would not have been fully but with gaps without MFA III.

Conversely, up to 6 of respondents considered that in the absence of MFA III the Ukrainian authorities would not have made any progress in the governance and transparency area. One of the answers received argued that "*Government had macro and fiscal situation under control but institutional building and addressing the weaknesses in business environment were lagging areas due to complicated politics*". Whereas 7 out of 21 respondents said that there would have been progress in the area without MFA III, but a slower pace; and 8 participants noted that the progress made would have been only partial and with gaps.

Figure 15. Progress in reform areas in the absence of MFA III

Question C14. We would want to assess whether the reform areas targeted by MFA III and derived from the Association Agreement were known to be high on the authorities' agenda. Could you speculate whether, in the absence of the EU MFA III, progress under these key reform areas would have been pushed through by the Ukrainian authorities anyways?



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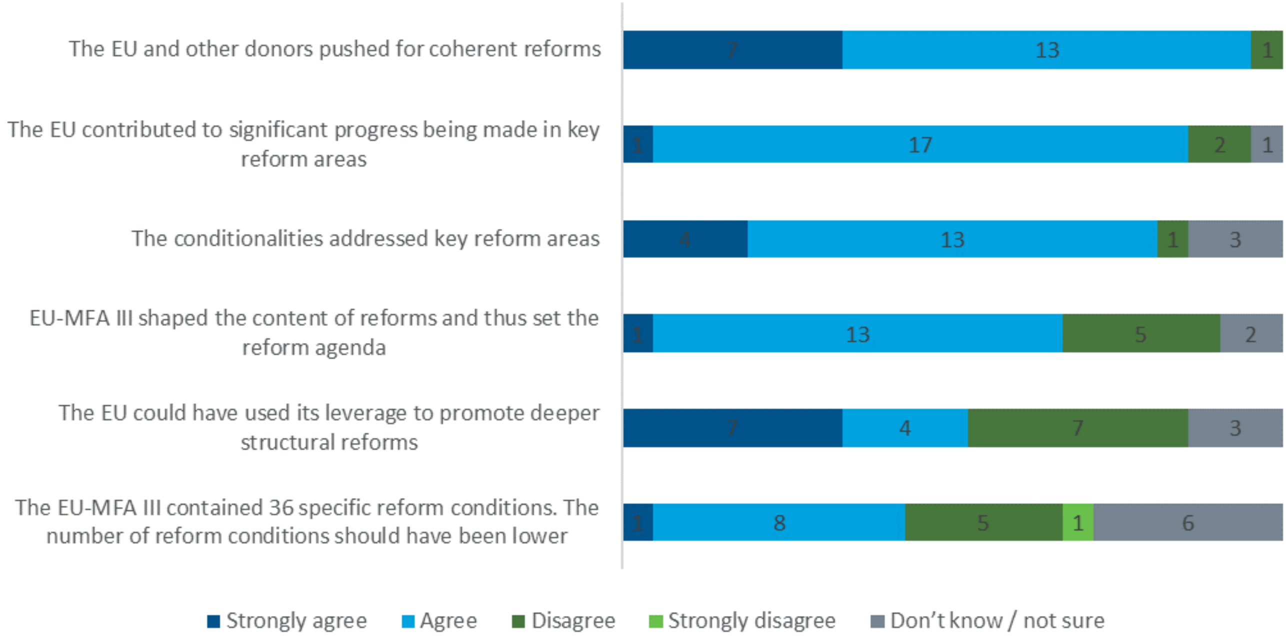
Last question under this section explores the influence of MFA III conditionalities in supporting Ukraine's key reform areas (Figure 16). The large majority of respondents (17) agreed or strongly agreed that "*the conditionalities addressed key reform areas*". Likewise, up to a number of 18 people said to agree or strongly agree that "*the EU contributed to significant progress being made in key reform areas*". Conversely, more than half of participants (11) agreed or strongly agreed with the statement that "*the EU could have used its leverage to promote deeper structural reforms",* whereas 7 of them disagreed with that same statement.

Additionally, 14 out of 21 experts asked said to agree or strongly agree that "EU-MFA III shaped the content of reforms and thus set the reform agenda", in contrast to 5 of them who disagreed with that statement. Moreover, most of respondents (20) agreed or strongly agreed that "*the EU and other donors pushed for coherent reforms".* Last, the statement that *"The EU-MFA III contained 36 specific reform conditions. The number of reform conditions should have been lower"* seems to be supported by 9 respondents against 6 respondents who disagreed or strongly disagreed.

Figure 16. Realised impact(s) of MFA III

Question C16. Please indicate the extent to which you agree or disagree with the following statements. When answering this question, please bear in mind that we are only referring to reforms promoted by the EU-MFA III.



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A4.6 Section D: Social impacts of the MFA III operation

This section covers the social consequences that resulted from the fulfilment of conditionality linked to MFA III financing. In this sense, respondents were asked whether MFA III conditionality was successful in different social areas in Ukraine (Figure 17). The majority of participants (14) considered that MFA III conditionality was successful in making sure social assistance is better targeted.

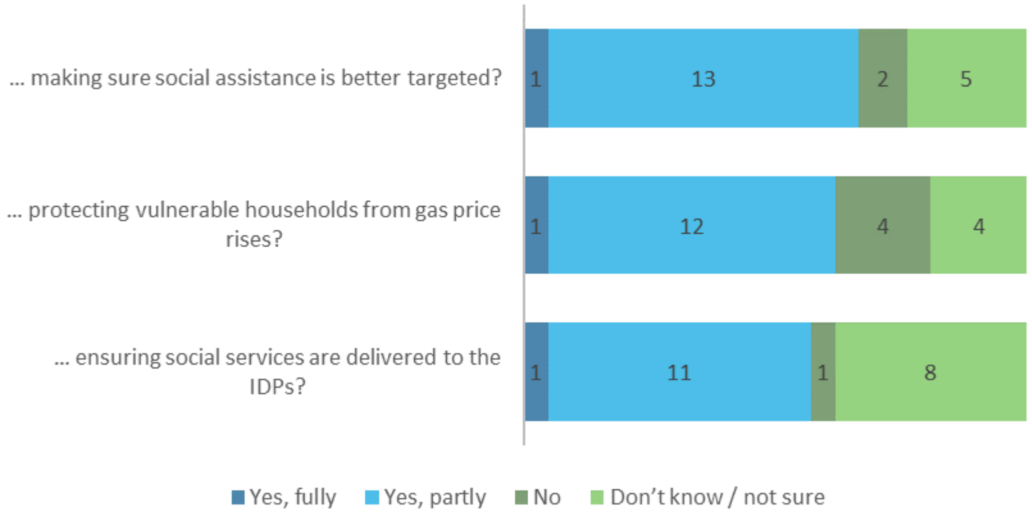
Likewise, according to 13 out of 21 people MFA III conditionality was successful in protecting vulnerable households from gas price rises. This is contrary to the opinion of 4 respondents who thought that MFA III conditionality was unsuccessful in this area. Last, more than half of participants (12) agreed that MFA III conditionality was successful in ensuring social services are delivered to the IDPs.

Responses received include, among others, the following comments:

- *"Adopting the necessary legislation and creating the programs are significant steps. Further progress in implementation, delivery and targeting is possible."*
- *"I see distortions in the system of state and municipal financing. Ukraine's economy is vulnerable to shocks. The state monopoly (oil and gas) did not establish communication with social cases. The public procurement system has significant problems in purchasing high-value goods. Monopolies are withdrawn from public procurement. Any economic shock will return state control to "hand mode" asap."*

Figure 17. Effectiveness of MFA III conditionality in the social area

Question D18. Was the MFA III conditionality successful in…?



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Annex 5 Relevance and effectiveness of MFA conditionality, condition by condition tables

A5.1 PFM

Table 2. Conditionality #1, 2nd tranche – Public Finance Management, External audit

Conditionality number 1 – Strengthen the external audit function by publishing the audit reports of the Accounting Chamber of Ukraine in full, as well as information notes about the follow-up to the audit reports.	
Relevance and importance	Publication of audit reports reinforce transparency, accountability and value for money in the use of public money[3].
Implementation	The new law "On the Accounting Chamber of Ukraine", and more precisely its articles 30 and 36, introduced the requirement to publish audit reports of the ACU in full, together with follow-up notes[4]. After being approved in July 2015, the law entered into force on 9 August 2015. The first report and accompanying note were published on the ACU website[5] on 31 August 2015.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	Publication of ACU's reports have continued since August 2015 and this is now an established practice. To this day, a total of 337 audit reports and accompanying notes have been published on ACU's website[6], strengthening Ukraine's Good Governance. Further to audit reports, the ACU also publishes information about its activities including annual reports and open data such information, work plans, and decisions of the ACU on its website[7]. However, the ACU's mandate is limited compared to other SAIs. The

[3] GIZ "Good Governance in Public Administration" (2017) International conference "Role and Challenges of the Accounting Chamber in Ukraine". Available at http://gogov.org.ua/en/news/mizhnarodna-konferentsiya-rol-rahunkovoyi-palaty-v-ukrayini-ta-vyklyky-shho-stoyat-pered-neyu-2/

[4] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

[5] www.ac-rada.gov.ua

[6] https://rp.gov.ua/FinControl/FinReports/?pid=111

[7] https://www.pefa.org/node/3676

	Accounting Chamber is not responsible for auditing local government budgets as its mandate does not include local finances[89]. Even though its scope does cover State budget funds and transfers from the State budget to local government. Therefore, an annual opinion report on financial statements of local government budgets is not published by ACU[10].

Table 3. Conditionality #1, 3rd tranche – Public Finance Management, External audit

Conditionality number 1 – Making use of the extended mandate of the Accounting Chamber of Ukraine under its new law, the ACU will carry out audits of at least five of the largest state-owned enterprises and publish the reports.	
Relevance and importance	Prior to the new law in 2015, ACU's powers and independence had some limitations, notably in relation to objects of audit[11]. The new law promoted under MFA I and II adopted in 2015 reinforced ACU's responsibilities to conduct the types of audits required by INTOSAI[12]. Now the ACU is tasked to perform control over ownership entities, as well as over SOEs supervised by them, although this remit has some limitations

8 A decision of the Constitutional Court of Ukraine in September 2010 excluded local government budgets and extra-budgetary funds from the scope of ACU's annual audits.

9 World Bank (2012), Ukraine: Public Financial Management Performance Report, https://openknowledge.worldbank.org/handle/10986/11898?locale-attribute=en

10 EUROSAI Task Force Municipality Audit (2018) Overview of External Audit Systems in Local Government. Available at http://www.eurosaiop.org/docs/upload/documents/TFMA_Overview_external_audit_systems_2018_1555656170.pdf

11 Before 2015, the ACU operated under the 1966 Law and only had powers to control expenditures and not revenues.

12 DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2018.

Implementation	Law no. 576-VIII on Accounting Chamber entered into force in August 2015. Apart from reinforcing transparency and public accountability by establishing the publication of audit reports, it sought to extend the Accounting Chamber's remit to SOEs.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no implementation deficit.
Evidence of benefits and contribution of MFA	*Stricto sensu* the condition is fulfilled – and there are attempts made by the ACU to use its mandate on SOEs (e.g. on Naftogaz, railways companies). However, the practice is not fully established. Between 2015 – 2017 a number of 14 SOEs were audited by the Accounting Chamber of Ukraine (ACU), this is 9 more audits than the minimum required by the conditionality[13]. In addition, more than 60 controls and inspections were conducted in SOEs in 2015-2017, notably as part of audits conducted on sectorial programmes. Apart from those classified as confidential, the reports on those audits were made available on the ACU's website[14]. However, some SOEs fail to report on their performance to their ownership entity who cannot fully evaluate their SOEs' performance[15]. The ACU expressed that performance evaluation of SOEs is usually purely formalistic and of poor quality[16]. Despite progress made, the new law did not give ACU the powers to audit the financial statements and records of SOEs. Although it receives original documentation as a matter of course, ACU is concerned that auditees still require a formal request before granting ACU access to information, which entails a considerable obstacle[17]. Besides, ACU has the right to audit SOEs provided that the audited activities may have detrimental impact on the public finances, which is used as a restriction.

[13] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

[14] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

See also:

https://rp.gov.ua/upload-files/Activity/Collegium/2019/8-1_2019/Zvit_8-1_2019.pdf

https://rp.gov.ua/upload-files/Activity/Collegium/2019/20-8_2019/Zvit_20-8_2019.pdf

https://rp.gov.ua/upload-files/Activity/Collegium/2019/39-2_2019/Zvit_39-2_2019.pdf

https://rp.gov.ua/upload-files/Activity/Collegium/2019/32-3_2019/Zvit_32-3_2019.pdf

https://rp.gov.ua/upload-files/Activity/Collegium/2019/28-6_2019/Zvit_28-6_2019.pdf

[15] OECD (2018) Anti-Corruption Reforms in Ukraine: Prevention and Prosecution of Corruption in State-Owned Enterprises. 4th round of monitoring of the Istanbul Anti-Corruption Action Plan. Available at https://www.oecd.org/corruption/acn/OECD-ACN-Ukraine-4th-Round-Bis-Report-SOE-Sector-2018-ENG.pdf

[16] ACU (2017) Accounting Chamber Report December 2017

[17] DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2018.

	To conclude, there is still a need to improve the transparency and accountability of SOEs activities. Amendment to the law would be needed to free up the ACU from some restrictions.

Table 4. Conditionality #2, 2nd tranche – Public Finance Management, Public procurement

Conditionality number 2 – Without prejudice to legitimate commercial secrets and intellectual property concerns of tenderers, after the finalisation of the tender process, publish information on public procurement contracts including obligations of the contractors, deliverables and related payments, so as to increase the transparency of the public procurement process.	
Relevance and importance	The inclusion of this condition built upon progress made under MFA I & II and came from the need to ensure an efficient and transparent procurement system that would avoid corrupt practices and foster a competitive environment. The establishment of the electronic procurement system Prozorro allows the general public to access all public tender information without any barriers – not even registration is required. Once a tender procedure is complete, all data is disclosed including the list of all participants, their bids, decisions of the tender committee and all qualification documents[18]. Given that public purchases accounts for a sizable part of Ukraine's GDP[19][20], an open and efficient e-system like Prozorro has been crucial to build a healthier environment[21].
Implementation	The Law 2087a, which entered into force in October 2015, amended the Public Procurement (PP) Law and established that public access to detailed evaluation records shall be provided on each public procurement bid procedures via a new e-procurement system. On 1 April 2016, the new e-procurement system website called ProZorro was launched (https://prozorro.gov.ua/en)[22]. On 12 September 2015, the new Law *"On openness of usage of public funds"* entered into force. This requires public entities and undertakings to publish information on their procurement contract payments, as well as other expenditures, on the website www.spending.gov.ua – a special publicly available website administered by the State Treasury Service under supervision of the Ministry of Finance[23].

[18] DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2018.

[19] In 2016, total value of public procurement in Ukraine represented 12.1% of GDP (UAH 273 billion or EUR 9,5 billion)

[20] Transparency International Ukraine (2017) Implementation Assessment of the Ukrainian Public Procurement Legislation. Available at https://www.tpp-rating.org/public/uploads/data/3/AOIL/5914ba099412aPPL_Implementation-Assessment-Ukraine.pdf

[21] https://prozorro.gov.ua/en

[22] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

[23] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit. 1.
Evidence of benefits and contribution of MFA	As from 2016, all public procurement processes are made via the ProZorro electronic procurement system. By the end of 2018, around 35,000 procurement organisers and more than 210,000 procurement participants were registered in the e-system ProZorro. Until then, the electronic procurement system included information about 2.73 million procurements with an expected value of almost UAH 2.07 trillion. Additionally, PEFA report shows that in 2018 78.1% of the total cost of all PP was made via competitive bidding using electronic auctions[24]. It is estimated that the increased transparency and competitiveness brought by the use of ProZorro has contributed to 10% of the overall public spending savings[25]. The e-procurement system has been fully implemented in 2017, which has been acknowledged as one of the most important achievements in the past years[26].

Table 5. Conditionality #3, 2nd tranche – Public Finance Management, Public procurement

Conditionality number 3 – Prepare the necessary changes to the legal framework to facilitate the use of electronic means in public procurement in line with relevant EU Directives and legal principles.	
Relevance and importance	This condition intends to pave the way to set up an open, competitive and efficient electronic procurement system harmonised with EU Directives and principles. Amendments to the PP law aimed to increase the level of control and transparency of procurement procedures and address a number of existing problems. According to the law, all public procurements above the thresholds of UAH 200,000 for goods and services and UAH 1,500,000 for works must be canalised through open competitive methods and be published on the Prozorro website[27]. This threshold is subsequently revised and reduced (see condition #2, 3rd tranche).
Implementation	On 24 December 2015, the draft law of the full e-procurement legislation was adopted[28]. It later entered in to force on 1 April 2016 (on the same day than the new e-procurement system website

[24] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[25] https://prozorro.gov.ua/en

[26] DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2018.

[27] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[28] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

	called ProZorro)
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	In line with EU procurement Directives, the law introduced legal and economic principles that must govern the procurement of supplies, works and services to meet the needs of central and local governments. Additionally, the PP Regulation Department of the MoEDT overseas and regulates public procurement, which includes the provision of analyses and the drafting of secondary legislation[29]. Efforts of the MEDT to make the draft EU-compliant have been remarked by experts from the EU technical assistance project[30]. The openness and transparency of the system is reflected on the higher number of appeals registered on Prozorro, many of which are successful. Appeals and disputes are processed online by the Prozorro system[31]. Between 2016-2018, the LPP was further revised to introduce a new framework of online monitoring of procurement by the State Audit Service using automatic risk indicators[32]. Additionally, quarter, semi-annual and annual reports are published to make procurement statistics available to the public[33].
Evidence of benefits and contribution of MFA	The final objective of rising tax revenues was widely achieved. Tax revenues in Ukraine grew by 50% in two years, from UAH 503.8 billion in 2016 to UAH 753.9 billion in 2018[34]. As of December 2015, all large taxpayers were brought under the Large Taxpayer Office (LTO), these are around 2,200 and represent about 55% of total revenues[35]. Besides, measures to reduce VAT refund arrears were introduced (see condition #4, 3rd tranche). In March 2015, rules for automatic VAT refund changed and set and increased the ratio of automatic refunds to two thirds of total amount of refunds. Additionally, the minimal wage criterion was removed[36]. On a

29 DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2018.

31 DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2018.

32 World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

33 These are published on The Ministry for Development of Economy, Trade and Agriculture website, available at http://www.me.gov.ua/Documents/List?lang=uk-UA&id=ca5d0012-c7f9-4750-b1f8-cf5550ecb270&tag=Zviti

34 World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

35 IMF (2016) Second Review under the Extended Fund Facility and requests for waivers of non-observance of performance criteria, rephasing of access and financing assurances review. IMF Country Report No. 16/319. September 2016. Available at https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Ukraine-Second-Review-Under-the-Extended-Fund-Facility-and-Requests-for-Waivers-of-Non-44318

36 IMF (2016) Technical Assistance Report – Reforming the State Fiscal Service. February 2016. IMF Country Report No. 16/48. Available at https://www.imf.org/external/pubs/ft/scr/2016/cr1648.pdf

	positive note, reliance on planned audits – as opposed to unplanned audits – has increased over the years[37]. The stock of revenue arrears at the end of 2018 represented less than 10% of the Ukraine's total revenue collection. Tax arrears older than 12 months represent between 50-75% of total revenue arrears[38]. This figure is partly justified by the SFS's inability to reach out to areas not under the control of the government in Crimea and Donbas regions[39]. Further to this, underreporting of Unified Social Contributions (USC) remains a challenge which the SFS is struggling to face. To address this, it is recommended to harmonise USC and personal income tax bases and provide a single filing and payment for business[40]. Overall, significant improvements in perception of tax administration have been visible in the past few years[41] indicating that the first steps have been made in the right direction. However, there has been no specific focus on high net-worth individuals due to the ongoing wider issue of bank secrecy. Despite Ukraine's intentions to join the OECD Multilateral Competent Authority Agreement for the automatic exchange of information[42], bank secrecy seems to be hard to lift as there is still some reluctant from members of the Parliament to rely on the storage and management of data. Since the publication of the Peer Reviews on the OECD website, comments on the implementation of the recommendations given have not been yet issued. For now, there is only progress on the legislative front.

Table 6. Conditionality #2, 3rd tranche – Public Finance Management, Public procurement

Conditionality number 2 – Adopt the necessary changes to the legal framework to facilitate the use of electronic means in public procurement in line with relevant EU Directives and legal principles.	
Relevance and	Following the fulfilment of condition #3 2nd tranche, this condition

[37] In 2018, a total of 5,299 planned audits and 15,689 unplanned audits were conducted. These in contrast to figures from previous years (see above). World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[38] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[39] UAH 14 billion of arrears older than 12 months come from Crimea and Donbas regions, which leaves the remaining arrears older than 12 months accounting for less than 50%.

[40] IMF (2016) Technical Assistance Report – Reforming the State Fiscal Service. February 2016. IMF Country Report No. 16/48. Available at https://www.imf.org/external/pubs/ft/scr/2016/cr1648.pdf

[41] Ukraine substantially improved its position in the ease of paying taxes Doing Business ranking from 108th place in 2015 to 54th place in the 2018 report. Likewise, trading across the borders ranked from 154th in 2015 to 78th in 2018. Doing Business Economy Profile 2015: Ukraine. Available at https://openknowledge.worldbank.org/handle/10986/20987. Doing Business Economy Profile 2018: Ukraine. Available at https://openknowledge.worldbank.org/handle/10986/28780

[42] It would provide for the abolition of bank secrecy as automatic exchange of tax information occurs between the countries that have signed the agreement.

importance	looked to put in place the necessary changes to foster transparency and competitiveness in the Ukrainian public procurement system. Amendments to the PP law allowed to implement a well-established e-procurement system (ProZorro), which is now accessible to all the general public, including all central authorities and customers.
Implementation	On 24 December 2015, the draft law on electronic procurement was adopted in final reading. The law was enacted in two phases[43]. On 1 April 2016 (first phase), the law entered into force for central executive authorities and customers operating in specific areas of economic management at the time the new e-procurement system ProZorro was launched at national level. On 1 August 2016 (second phase), the new system was extended to all customers.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	The ProZorro system is widely considered a success (see also Condition 3, 2nd)[44]. Additionally, amendments to the PP law are in force since April 2020, introducing further improvements to the usual procedures. Most notably, it reduced the sub-threshold purchase from 200 thousand UAH to 50 thousand UAH. Other important innovations included a new two-step procurement procedure with a limited number of participants and the introduction of a new term – an abnormally low purchase price is automatically marked by the system[45]. It is to be noted that the possible side-effects are not linked to the e-procurement system as such but to the automatic application of criteria where price criteria would have a too high weight – lowest price can be no less than 70% of weight (except for competitive dialogue where there are no restrictions)[46]. But although Ukraine does not define the weight of the price criteria, this is not believed to be a major issue. Ukraine has made considerable progress in the development of a modern and transparent PP system aligned with EU regulations. Transparent complaint and dispute resolutions systems have resulted in increased trust of the system; and the larger number of participants in the PP market brought by Prozorro have contributed to enhanced competition[47].

[43] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

[44] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

[45] Antika (2020) Amendments to the law of Ukraine "On Public Procurement". Available at http://antikalaw.com.ua/en/amendments-to-the-law-of-ukraine-on-public-procurement/

[46] ERBD (2019) Guidelines for non-Ukrainian suppliers on participation in public procurement tenders of Ukraine. Available at https://infobox.prozorro.org/upload/files/main/1145/484/gpa-guide-ukraine-fin.pdf

[47] DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. August 2018.

Table 7. Conditionality #4, 2nd tranche – Public Finance Management, Fiscal governance

Conditionality number 4 – In line with the provisions of the Constitution and the Budget Code, submit the draft 2016 State Budget to Parliament by mid-September, and publish it online.	
Relevance and importance	Delays in the approval of the State Budget were common at the time this condition was put in place[48]. This, among other issues, delayed availability of information for local governments. The introduction of this condition aimed to reinforce the fulfilment of Budget Legislation that sets a specific budget calendar, which was not always respected[49]. According to the Budget Code, the budget calendar specifies that the State Budget must be submitted to the Rada by 15 September.
Implementation	- After some adjustments, on 11 December 2015 the revised 2016 budget was re-submitted to the Parliament and successfully adopted on 25 December 2015[50]. - On 14 September 2015, the submission of the draft 2016 budget was published on the Rada's website. The full text and relevant annexes were published the following week.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no implementation deficit.
Evidence of benefits and contribution of MFA	Following this measure, duly submissions of the State Budget became an established practice in Ukraine. Since this condition was implemented, violations of the calendar budget are no longer the case[51]. In this sense, MFA acted as a reminder that it is important to follow the budget calendar and give the Parliament time to make informed discussions. Although the State Budget is presented every year, the Ukrainian government does not submit explanatory information of budget implications of new policy initiatives and major new public investments[52].

Table 8. Conditionality #5, 2nd tranche – Public Finance Management, Fiscal governance

Conditionality number 5 – To improve tax compliance: (i) adopt an action plan to simplify tax filing, address tax arrears and fight tax evasion, with an initial focus on the taxpayer segment of high net- worth individuals; and (ii) in an effort to fight offshore tax evasion, provide all relevant information to the OECD Secretariat to ensure the launch of the peer review by the Global Forum on Transparency and Exchange of Information for Tax Purposes.

[48] For instance, the 2014 State Budget of Ukraine was approved late on 16 January 2014; and the Draft Budget 2015 was submitted to the Rada only at the end of the calendar year on 29 December 2014.

[49] Article 3 of the Budget Code of Ukraine. Available at http://gogov.org.ua/wp-content/uploads/2016/05/THE-BUDGET-CODE-OF-UKRAINE.pdf

[50] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

[51] Draft State Budgets in the last few years were submitted in due time: September 15, 2016; September 15, 2017; September 15, 2018.

[52] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

Relevance and importance	Based on three pillars – taxes, customs, and tax police- the SFS was created in 2014 as a single tax and duties administration department. In a context of a low level of public confidence in tax administration, the main intention of this condition was to establish more fairness in the administrative system of tax collection and to balance demands for urgent revenues through a more effective tax collection. The SFS was unable to address the country's shadow economy - estimated to be between 38 to 60% of GDP-[53], as SFS's powers to carry out audits were seriously constrained by law. Audit resources were mainly focused on formal business operations, paying little attention to taxpayers operating in the informal sector. For years, a large proportion of high net worth individuals has been out of the SFS's focus. Additionally, tax evasion in Ukraine was encouraged by the fact that the SFS needed to link all tax liabilities to a business's documentary trail[54]. Other contributing factor to a low tax collection was the limited number of planned audits and the declining audit coverage[55]. The high level of offshorization of the economy in Ukraine can be explained by companies looking to a) take advantage of better taxation conditions; b) and/or protect their assets from the crisis momentum Ukraine experienced during 2010-2016[56]. In this contest, exchange of information for tax purposes is considered to be an effective way to fight offshore tax evasion[57]. The Ukrainian authority responsible for exchange of information for tax purposes is the SFS. Ukraine has a total of 109 exchange of information relationships for tax purposes based on double tax conventions and the Multilateral Convention, being China its main partner[58]. However, the lack of international exchange of information and the absence of initiatives in Ukraine to actively engage in the global exchange of information action led by the OECD left wide room for tax avoidance and evasion during the past years.[59]
Implementation	(i) - On 11 November 2015, the Ministry of Finance adopted the reform plan for the State Fiscal Service (SFS)[60]. The

[53] Romanyuta (2017) Systematization of Tax Strategies for Shadow Economy Prevention under Conditions of Globalization. EUREKA: Social and Humanities. Number 4. pp. 44-51

[54] IMF (2016) Technical Assistance Report – Reforming the State Fiscal Service. February 2016. IMF Country Report No. 16/48. Available at https://www.imf.org/external/pubs/ft/scr/2016/cr1648.pdf

[55] In, 2014 the SFS conducted 4,867 planned audits and 28,013 unplanned audits, which accounts for 5.5% of total legal entities (600,000). This suggests a declining trend when compared with the 32,496 unplanned audits performed in 2013.

[56] Maslak et. Al (2017) The offshorization of the economy: the present realities. SHS Web of Conferences 39, 01019 (2017). Available at https://www.shs-conferences.org/articles/shsconf/pdf/2017/07/shsconf_ies2017_01019.pdf

[57] https://www.oecd.org/tax/transparency/#default

[58] OECD (2016) Global Forum on Transparency and Exchange of Information for Tax Purposes Peer Reviews: Ukraine 2016. Phase 1: Legal and Regulatory Framework. Available at https://dx.doi.org/10.1787/9789264258716-en

[59] The Agency for the Modernisation of Ukraine (2015) Ukraine Modernisation Programme. Milestones for Tomorrow.

[60] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

	objective of the reform plan for the SFS is to increase tax revenues, amend the tax police and the Large Taxpayer office, reform the tax and customs code, restructure tax appeals, fight the shadow economy and modernise tax debt collection. (ii) - Ukraine submitted the first documents to the OECD Secretariat on 27 October 2015. - After some exchanges between the SFS and the Global Forum experts, the final document was passed in July and 2016 and later published on the OECD website (https://www.oecd.org/countries/ukraine/global-forum-on-transparency-and-exchange-of-information-for-tax-purposes-peer-reviews-ukraine-2016-9789264258716-en.htm)
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	The final objective of rising tax revenues was widely achieved. Tax revenues in Ukraine grew by 50% in two years, from UAH 503.8 billion in 2016 to UAH 753.9 billion in 2018[61]. As of December 2015, all large taxpayers were brought under the Large Taxpayer Office (LTO), these are around 2,200 and represent about 55% of total revenues[62]. Besides, measures to reduce VAT refund arrears were introduced (see condition #4, 3rd tranche). In March 2015, rules for automatic VAT refund changed and set and increased the ratio of automatic refunds to two thirds of total amount of refunds.

[61] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[62] IMF (2016) Second Review under the Extended Fund Facility and requests for waivers of non-observance of performance criteria, rephasing of access and financing assurances review. IMF Country Report No. 16/319. September 2016. Available at https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Ukraine-Second-Review-Under-the-Extended-Fund-Facility-and-Requests-for-Waivers-of-Non-44318

Additionally, the minimal wage criterion was removed[63]. On a positive note, reliance on planned audits – as opposed to unplanned audits – has increased over the years[64].

The stock of revenue arrears at the end of 2018 represented less than 10% of the Ukraine's total revenue collection. Tax arrears older than 12 months represent between 50-75% of total revenue arrears[65]. This figure is partly justified by the SFS's inability to reach out to areas not under the control of the government in Crimea and Donbas regions[66]. Further to this, underreporting of Unified Social Contributions (USC) remains a challenge which the SFS is struggling to face. To address this, it is recommended to harmonise USC and personal income tax bases and provide a single filing and payment for business[67].

Overall, significant improvements in perception of tax administration have been visible in the past few years[68] indicating that the first steps have been made in the right direction. However, there has been no specific focus on high net-worth individuals due to the ongoing wider issue of bank secrecy. Despite Ukraine's intentions to join the OECD Multilateral Competent Authority Agreement for the automatic exchange of information[69], bank secrecy seems to be hard to lift as there is still some reluctant from members of the Parliament to rely on the storage and management of data.

Since the publication of the Peer Reviews on the OECD website, comments on the implementation of the recommendations given have not been yet issued. For now, there is only progress on the legislative front.

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[63] IMF (2016) Technical Assistance Report – Reforming the State Fiscal Service. February 2016. IMF Country Report No. 16/48. Available at https://www.imf.org/external/pubs/ft/scr/2016/cr1648.pdf

[64] In 2018, a total of 5,299 planned audits and 15,689 unplanned audits were conducted. These in contrast to figures from previous years (see above). World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[65] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[66] UAH 14 billion of arrears older than 12 months come from Crimea and Donbas regions, which leaves the remaining arrears older than 12 months accounting for less than 50%.

[67] IMF (2016) Technical Assistance Report – Reforming the State Fiscal Service. February 2016. IMF Country Report No. 16/48. Available at https://www.imf.org/external/pubs/ft/scr/2016/cr1648.pdf

[68] Ukraine substantially improved its position in the ease of paying taxes Doing Business ranking from 108th place in 2015 to 54th place in the 2018 report. Likewise, trading across the borders ranked from 154th in 2015 to 78th in 2018. Doing Business Economy Profile 2015: Ukraine. Available at https://openknowledge.worldbank.org/handle/10986/20987. Doing Business Economy Profile 2018: Ukraine. Available at https://openknowledge.worldbank.org/handle/10986/28780

[69] It would provide for the abolition of bank secrecy as automatic exchange of tax information occurs between the countries that have signed the agreement.

Table 9. Conditionality #3, 3rd tranche – Public Finance Management, Fiscal governance

Conditionality number 3 – Strengthen the transparency and predictability of fiscal policy, notably by revising the Budget Code with a view to limiting, as from 2016, the number of budget amendments.	
Relevance and importance	The introduction of this condition can be justified by the lack of credibility the State Budget has, as there is no credible fiscal framework to support medium-term planning[70]. Contributing to this, the Budget Code attributed excessive powers to the Parliament and its Budget Committee to interfere in the budget process, resulting in a very high number of amendments to the Budget Law[71].
Implementation	On 24 December 2015, the law on amendments to Article 52 of the Budget code of Ukraine (regarding regulations on amendments to the budget) was adopted[72]. The law implemented restricts the circumstances under which the budget can be amended. For example, if the macroeconomic situation changes considerably during the budget year differing substantially from the economic forecast and impacting on revenues and expenditures, then it is allowed to amend the budget law[73][74].
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no implementation deficit.
Evidence of benefits and contribution of MFA	Changes to Article 52 of the Budget Code limited the number of cases requiring amendments to the appropriations. As a result, in 2017 amendments to the State Budget Law were restricted to 5 against 15 in 2016. However, it is observed that Ukraine still needs to take further actions to strengthen the top-down budgetary planning process that will improve the Budget's credibility[75].

[70] DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2018.

[71] This has been a typical situation in Ukraine in the past few years. As example, involvement of the Rada's Budget Committee resulted in a total of 15 amendments to the 2016 State Budget Law.

[72] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

[73] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[74] Article 52 of the Budget Code of Ukraine. Available at http://gogov.org.ua/wp-content/uploads/2016/05/THE-BUDGET-CODE-OF-UKRAINE.pdf

[75] DG ECFIN (2018) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2018.

Table 10. Conditionality #4, 3rd tranche – Public Finance Management, Fiscal governance

Conditionality number 4 – Substantially reduce public sector payment arrears, notably in the areas of VAT refunds (without resorting to the issuance of VAT bonds) and public procurement	
Relevance and importance	Delays and low transparency in VAT refunds have been a long-standing issue in the country[76]. In 2010, VAT refund arrears amounted to UAH 28.4 billion, which represented 2.6% of Ukrainian GDP. After five years, the amount of VAT subject to refund decreased to UAH 15 billion in December 2015[77]. Arrears of VAT refunds affect companies' liquidity and undermine the rules-based interaction of the fiscal authorities with the private sector, adversely impacting tax compliance[78]. The absence of VAT refunds is implicitly taxing and depressing prices, thus impacting companies' profitability. Additionally, there is clear evidence of unequal treatment of companies when it comes to VAT refunds, which sends the wrong signal to businesses.
Implementation	On 1 April 2017, a new unified public register for VAT refund applications was implemented. This enabled the administration to accelerate VAT reimbursements noticeably[79]. The Prozorro system and the law on electronic procurement were implemented in 2016 to combat arrears in public procurement. Procuring entities are now required to publish procurement contracts and information on contract payments on the ProZorro web portal, while information on payments made by public authorities to the procuring entities is accessible on a dedicated website on the use of budget funds (www.spending.gov.ua). As a result, late payments under public procurement contracts no longer appear among the

[76] Ukraine has been known for years for its enormous accumulation of VAT refund arrears to domestic and foreign-owned companies. Causes for VAT refund arrears are: i) Ukraine's weak fiscal position; ii) fraudulent behaviour of some private companies in the VAT chain; iii) and corruption in the public sector which gives unequal treatment to companies. ; iii) and corruption in the public sector which gives unequal treatment to companies.

American Chamber of Commerce in Ukraine (ACC) (2010) VAT Refund Arrears in Ukraine. Analysis and Recommendations on How to Solve the Problem, with a Special Focus on Agriculture.

[77] OECD (2016) OECD Investment Policy Reviews: Ukraine 2016, OECD Investment Policy Reviews, OECD Publishing, Paris. Available at https://www.oecd.org/countries/ukraine/oecd-investment-policy-reviews-ukraine-2016-9789264257368-en.htm

[78] DG ECFIN (2014) Operational Assessment of the financial circuits and procedures in Ukraine. Final Report, August 2014.

[79] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

	subjects of complaints commonly raised by businesses operating in Ukraine. The new law provides for automatic and non-automatic VAT refund. Additionally, Vat refund does not require any tax audit or inspection since 1 July 2015[80].
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	Expenditure arrears[81] – its definition excludes VAT refund arrears – have slightly decreased ranging from 0.7% of the State Budget expenditures in 2016 to 0.5% in 2017 and 2018[82]. As to the specific point on arrears in public procurement, no statistics have been made available. An interviewee noticed that there was anecdotical evidence that it was a problem for some, but the government was denying the existence of a problem on this. On a positive note, the adoption of the law on electronic procurement in 2016 and the launch of the ProZorro system improved considerably arrears in public procurement. After almost being eradicated in 2014, VAT refund arrears[83] increased rapidly in 2015. This promptly increase in VAT refund arrears can be partly explained by the fact that rules for automatic VAT refund changed and the coverage of automatic refunds grew from around half to two thirds of total amount of refunds. Other contributing factors were i) the removal of the minimal wage criterion; ii) and the introduction of a new criterion requiring the taxpayer to have fixed assets exceeding three times the value of VAT requested for refund[84]. After 2015, VAT refund arrears considerably

[80] OECD (2016) OECD Investment Policy Reviews: Ukraine 2016, OECD Investment Policy Reviews, OECD Publishing, Paris. Available at https://www.oecd.org/countries/ukraine/oecd-investment-policy-reviews-ukraine-2016-9789264257368-en.htm

[81] The Ministry of Finance defines expenditure arrears as the amount of accounts payable occurring on the 30th day after the expiration of the payment deadline

Order No. 372 dated 2 April 2014 "On Approval of the Procedure for Accounting of Certain Assets and Liabilities of Budget-Sustained Institutions and Amendment of Certain Regulatory Legal Acts on Bookkeeping of Budget-Sustained Institutions".

[82] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[83] These are described as those being more than 74 days old

[84] IMF (2016) Technical Assistance Report. Reforming the State Fiscal Service. IMF Country Report No. 16/48. February 2016

	decreased from UAH 4.7 billion in 2015 to UAH 0.012 billion in 2016[85] - notably due to the implementation of a new unified public register for VAT refund applications. However, in the past few years a timid upward trend has been observed[86]. Spending units provide and submit to the Treasury data on expenditure arrears on a monthly and annual basis[87]. Likewise, the State Fiscal Service (SFS) must publish monthly reports on the budget refund of the VAT, including information on the budget arrears of VAT refunds[88][89]. Further steps in terms of transparency measures have been taken. As example, it is available a list mapping who requested VAT refunds and who was paid in order to show that the requests are dealt on a first-come first-served basis. These improvements are visible on the statistics of last years, where, despite the slight upward trend seen between 2016-2018, there has been a drastic reduction in VAT refund arrears compared with 2015 figures.

A5.2 Governance and transparency

Table 11. Conditionality #6, 2nd tranche – Governance and transparency, Anti-corruption

Conditionality number 6 – Establish a National Anti-Corruption Bureau (NABU), a Specialised Anti-Corruption Prosecution Office (SAPO) and a National Agency for the Prevention of Corruption (NAPC), ensuring that they are independent and operational, i.e. endowed with the financial resources, staff and equipment required to perform their functions	
Relevance and importance	Corruption was affecting many areas of life at individual, organisational (business climat) and macroeconomic level (including high level corruption).

[85] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[86] VAT refund arrears reveal amounted to UAH 0.012 billion (1.77% of total State Budget expenditures) in 2016; UAH 0.015 billion (1.81% of total State Budget expenditures) in 2017; and UAH 0.028 billion (2.91% of total State Budget expenditures) in 2018

[87] World Bank (2019) 2019 Public Expenditure and Financial Accountability (PEFA) Performance Assessment Report. Available at https://www.pefa.org/node/3676

[88]In accordance to paragraph 4 of part 3 of Article 59 of the Budget Code of Ukraine

[89] These reports can be found on the SFS's website: http://sfs.gov.ua/diyalnist-/vidshkoduvannya-pdchv/informatsiya-pro-obsyagi-vidshkoduvannya/

	The 'Revolution of Dignity' was a striking emanation of the public demand supported strongly by the civil society organisations and the IFIs assistance to tackle the corruption and break with the past. Creating new institutions, including NABU, NAPC and SAPO, was a part of the approach.
Implementation	Establishment of NABU was discussed by the authorities and donors already in 2014. The IMF report[90] that was part of the diagnostics work feeding into the design of the IMF SBA conditionality focused on the corruption in Ukraine and some possible measures to tackle it. This report proposed, inter alia, the establishment of NABU. In addition, the IMF Legal Department provided some critical inputs into the law underpinning NABU. The NABU was created on the April 16th, 2015 (Decree 217/2015). The Head of the NABU (Artem Sytnyk) was elected in the result of transparent and competitive selection and appointed by the President of Ukraine on April 16th, 2015 (Decree 218/2015). The Deputy-Heads of the NAB were also appointed. In summer 2015, some 30 administrative staff of the NABU as well as 70 investigators have been recruited, bringing the overall staff to about 100. The figure that was subsequently increased to 518 by September 2016 (including 201 detectives). The official investigations meant to start in Autumn 2015, albeit NABU's operations were conditional on the establishment of the SAPO. The latter, due to the politicisation of the selection of its members (and concerns relating to potential influence of the General Prosecutor), had a delayed start and became operational only in 2016. Provisioning of the adequate resources to NABU was a crucial aspect. According to the Law of Ukraine "On the State Budget of Ukraine for 2016" (with amendments) the expenditures for the NABU were redoubled compared to 2015 (or EUR 8.1 mln) and amounted to EUR 16,1 mln. Furthermore, the budget of the agency was increased to ~EUR 25 mln in 2017. In addition, donors were explicit in rising the argument about appropriately high level of renumeration for NABU staff. Overall, there were no major issues in ensuring adequate resources for the agencies and lower allocations at the initial period reflected lower level of staffing and overall roll-out. Regarding the establishment of NAPC, this started in May 2015 with the selection of the members of the selection committee, half of which (four) were to be elected by and from civil society. The first election of the civil society members took place on 17th May 2015 but the process was marred with allegations of manipulation by the government. Following intense lobbying by civil society and the EU,

[90] IMF, 2014. Government of Ukraine Report on Diagnostic Study of Governance Issues Pertaining to Corruption, the Business Climate and the Effectiveness of the Judiciary Available at: https://www.imf.org/external/pubs/ft/scr/2014/cr14263-a.pdf

	the government agreed to repeat the process and new elections took place on 28th August 2015. As a result, the new selection committee, composed in a fair and transparent manner, enjoyed the support of civil society. Interviews of candidates took place on 28th September and 5th October 2015, but then then process was yet again obstructed[91]. In late March 2016, the inauguration meeting of the NAPC was held. During this event NAPC Board has elected Head (Nataliya Korchak) and Deputy Head (Ruslan Radetskiy). In August 2016, NAPC officially announced the launch of its work as a public authority in all areas of anti-corruption activities. Yet, as of early August 2016, only about 25 percent of the NAPC Staff were already appointed. As of end-December 2016, 213 staff members had been recruited (out of 311 staff members envisaged), while the fifth NAPC Board member remained to be still appointed. The funds for the NAPC's activities assigned in the annual State Budgets were ~EUR 3.7 mln and EUR 3.5 mln in 2015 and 2016 respectively. This envelope was increased to EUR 5.5 mln in 2017.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. Some caveats: While there has been a consensus about the broad independence of NABU, there have been major doubts about the independence of NAPC as well as number of other internal (e.g. insufficient staffing) and external factor hampering its effectiveness. Likewise, SAPO independence, according to number of stakeholders including the EU Delegation, has been compromised. In hindsight, the selection process of the management of all of the agencies was perceived as absolutely crucial for their subsequent independence and effectiveness. In addition, while all three organisations were appropriately funded, the delineation of their competences (e.g. NABU's competence to wiretap independently[92]) and relationship with each other was problematic and led to major delays.
Evidence of benefits and contribution of MFA	Reforms initiated in 2014 resulted in the creation of the new dedicated institutional architecture focused on the fight against the corruption with three separated branches: NABU, NAPC and SAPO. At the operational level, in 2017 the Ukrainian anti-corruption authorities (SAPO and NABU) forwarded to courts first corruption-related cases where the suspects were high-ranking officials, action that gave the country a slight uplift it the Transparency Corruption Index[93]. By March 2019 NABU investigated a total of over 1,000 cases[94]. These were at various stages:

[91] Lack of agreement of the selection committee on two members in late 2015, and a need to organise new call for applications.

[92] Granted only in the second half of 2019

[93] Council of Europe, 2018. Ukraine most corrupt country in Europe after Russia.

[94] Of these over 1,000 cases, 65 were based on illicit enrichment, either partly (among other offences) or exclusively. Out of the 65 cases involving illicit enrichment, 3 had reached the courts

692 investigations ongoing at the initial stage

149 cases of suspicion

314 accusations submitted to prosecution

189 in court

27 court convictions

Yet, to the knowledge of the study team, three years since the establishment of NABU there has been still no single court ruling leading to the prison sentence of a corrupted official. According to the Transparency International '…NAPC lacks political independence and credibility and it has yet to make a notable progress or bring about any significant investigations'95. At the independence level, there is a broad consensus that NAPC has been a subject of significant and frequent political interferences. Whistle-blowers, including some from the former NAPC leadership, have reported multiple cases highlighting the agency's corruption and abuses of power96. NABU has remained broadly independent though and has been often seen as a success story, though it still has not avoided some controversy. There has been also some media reports casting some doubts on the role of the NABU in the high profile embezzlement case in the army carried out in 2019[97].

Overall, the MFA III was certainly a material factor in exerting the pressure on the authorities and advancing this reform. However, it was the IMF which held a leading role in the conceptualisation and establishment of the NABU[98] (see also detailed conditionality under EFF), while the WB had also contributed to the process. The EU-Ukraine Visa Liberalisation Action Plan (VLAP) also incorporated the anti-corruption reforms (e.g. Specialised Anti-Corruption Prosecution Office) that was relevant in an explicit (and very meaningful) way for the implementation of this condition[99]. Besides, other actors were also involved at various stages e.g. training for senior staff at NABU provided by American's FBI.

Interviewees from the EU Delegation, WB and the IMF expressed the view that without the concerted effort of the donors' community, neither NABU nor other key anti-corruption institutions in Ukraine would have been set up. All pointed out to the 'deterrent effect' of those institutions.

If this condition is assessed in a narrow, literate sense where the set-up of both agencies would be a primary outcome desired (leaving aside their prospect operations), the condition was a definite success.

[95] Transparency International, 2019. Corruption high on the agenda as Ukrainians go to the pools. Available at: https://voices.transparency.org/corruption-high-on-agenda-as-ukraine-goes-to-polls-57a7ed6001c9

[96] Atlantic Council, 2018. Why Ukraine's Major Achievement in Government Transparency May Fail. Available at: https://www.atlanticcouncil.org/blogs/ukrainealert/why-ukraine-s-major-achievement-in-government-transparency-may-fail/

[97] Reuters, 2019. Ukraine's Anti-Graft Agency Accused of Concealing Military Fraud. Available at: https://www.bloomberg.com/news/articles/2019-03-12/ukraine-s-anti-graft-agency-accused-of-concealing-military-fraud

[98] Through its conditionality of a detailed character

[99] The Economist, 24th August 2017. Ukraine's reform activists are under attack. Available at: https://www.economist.com/europe/2017/08/24/ukraines-reform-activists-are-under-attack

Table 12. Conditionality #5, 3rd tranche – Governance and transparency, Anti-corruption

Conditionality number 5 – set up an electronic asset disclosure system for public officials, including a verification mechanism, while starting to verify assets and possible conflicts of interest on the basis of the paper-based asset declarations submitted by officials in 2015.	
Relevance and importance	The e-declaration system aimed to help to prevent corruption (widely recognized as one of Ukraine's biggest problems), to avoid conflicts of interest and to enable citizens to inspect online public officials' earnings and assets. The system also meant to make it easier for Ukraine's new anti-corruption bodies to unearth graft and expose corruption[100]. By the time when Ukraine set up the system, more than 150 countries had introduced the asset disclosure requirements for the public officials[101].
Implementation	After some delays, the electronic asset declaration system[102] introduced by the Corruption Prevention Law (2014) was launched on 1 September 2016. There was a material difference in views between the EC and the IMF regarding the scope of the system. The IMF argued that the number of declarants should be fairly limited at the outset (e.g. 3,000 declarations as per discussions in May 2017) and focused mostly on the top officials. The Fund was also keen to concentrate the core responsibilities for managing the system at NABU, rather than splitting it between NABU and NAPC. The EC in turn was of a view that the simple establishment of the system should be a priority first, and then further adjustment could be made. It also argued that the donor community should not actively argue for restricting it (even though it acknowledged that imposing this obligation on over 1 million public servants could be excessive), as this would most probably require legislative changes which would entail a risk that interested groups attempt to get exempted from the obligation to declare their assets. Also, in the EU's view, a more effective way to ensure that declarations are effectively examined and, where needed, followed by a legal procedure, would be to establish a verification mechanism with clear criteria targeting the declarations to be

[100] UNDP, 2018. Electronic asset declarations for Public Officials. Available at: https://www.ua.undp.org/content/ukraine/en/home/blog/2018/the-expectations-and-reality-of-e-declarations.html

[101] World Bank, 2016. Asset Declarations: A Threat to Privacy or A Powerful Anti-Corruption Tool. Available at: https://www.worldbank.org/en/news/opinion/2016/09/26/asset-declarations-a-threat-to-privacy-or-a-powerful-anti-corruption-tool

[102] https://public.nazk.gov.ua

	checked as a priority. Furthermore, the EC argued that this would achieve the same purpose as the measure advocated by the IMF, without requiring any legislative change. That said, restricting the number of people subject to the asset declaration obligations, as supported by the IMF, was not in direct contradiction to the condition. Overall, the World Bank assessed that the characteristics of the system are comparable with other countries in the region both in terms of the scope of the information declared and its approach towards public access[103]. The failure to submit the declaration carried circa USD 14,000 criminal lability104. The first round of the submission of the declarations took place in March 2017 when over 1 million civil servants submitted their declarations. Since then, however, the system has been still developed and adjusted (e.g. development of the screening software). The system has been managed by NAPC with some partial access granted to NABU.
Evidence of Implementation deficit	The condition has not been assessed as met by the Commission and was one of the conditions blocking the disbursement of the third tranche. Despite the system being officially set up in September 2016, by mid-2017 there was no mechanism in place to ensure the efficient verification of the submitted asset declarations. As of mid-2017, the National Agency for the Prevention of Corruption (NAPC) was still far from performing its functions related to the verification of electronic asset declarations of which hundreds of thousands have been submitted by public officials since September 2016. According to DG ECFIN mission from May 2017: '…inefficient management and divergences among NAPC Board members, combined with poor cooperation with other institutions involved in the fight against corruption (including the Ministry of Justice and the National Anti-corruption Bureau of Ukraine, NABU) can largely explain the institution's lack of progress with verification. For instance, the NAPC needed to obtain access to databases/ state registers from the relevant official bodies (notably the Ministry of Justice and State Fiscal Service) to be able to cross-check the information submitted by declarants. Finally, it needed to deploy software that would enable it to verify asset declarations in a systematic way according to pre-defined criteria, rather than only manually, case by case. A first version of such an automatic verification system was designed by UNDP and proposed to NAPC in August 2016, but the NAPC did not introduce the software (on the grounds of IT security concerns), neither it launched successful tenders for other potential providers (all

[103] Ibidem

[104] Rasmussen Global, 2018. Electronic Asset Declaration System Goes Live in Ukraine – A new stage in the fight against corruption. Available at: https://rasmussenglobal.com/media/electronic-asset-declaration-system-goes-live-ukraine-new-stage-fight-corruption

	tenders included discriminatory requirements limiting the range of potential participants and preventing reputable international auditors from participating[105]. Other issues that became problematic at one point or another included, inter alia, completeness of the submitted declaration and the requirement for family members of officials to file a declaration, or the requirement that anti-corruption activists declare their private assets via the online system in the same way that public officials do[106]. By May 2017, over 1.2 million declarations were submitted but only 25 asset declarations were duly verified by the NAPC, the figure that rose to 163 by May 2018 and 600 by March 2019. The issues with access to the state databases/ registers (still persisted with decision of Rada made by mid-2018) and the efficiency of the system still remained unresolved by 2018. The system of automated verification was operational in January 2019, though full interoperability between the databases/ registers, the malfunctioning and technical problems occasionally experienced by the e-declaration system and allegations of unlawful interference still remains an issue to some extent (though NAPC does have access to all 16 registers)107. Overall, in terms of the ownership for this reform, while Ukrainian authorities tended to point out to the IT related challenges in its implementation. Yet, the EC was of a view that the lack of political will was a key impediment for the progress of this reform.
Evidence of benefits and contribution of MFA	The table in the **Annex 1** outlines the key statistics, including the numbers on the declarations submitted/ verified and follow-up cases in courts. Overall, despite the delays in the set-up and persisting deficiencies of the system itself, its establishment was a symbolic moment and major breakthrough in further strengthening of the anti-corruption infrastructure in Ukraine. The set-up has of a paramount importance towards Ukraine's broader drive towards reforming its post-Soviet legacy[108]. It was also widely recognised at the international stage[109].

[105] Atlantic Council, 2018. Why Ukraine's Major Achievement in Government Transparency May Fail. Available at: https://www.atlanticcouncil.org/blogs/ukrainealert/why-ukraine-s-major-achievement-in-government-transparency-may-fail/

[106] UNDP, 2018. Electronic asset declarations for Public Officials. Available at: https://www.ua.undp.org/content/ukraine/en/home/blog/2018/the-expectations-and-reality-of-e-declarations.html

[107] https://nazk.gov.ua/wp-content/uploads/2020/03/Greco.pdf

[108] Rasmussen Global, 2018. Electronic Asset Declaration System Goes Live in Ukraine – A new stage in the fight against corruption. Available at: https://rasmussenglobal.com/media/electronic-asset-declaration-system-goes-live-ukraine-new-stage-fight-corruption

[109] See for instance: Chatham House, 2016. Full Disclosure. Available at: https://www.chathamhouse.org/expert/comment/full-disclosure-tackling-public-corruption-ukraine and Atlantic Council, 2018. Why Ukraine's Major Achievement in Government Transparency May Fail. Available at: https://www.atlanticcouncil.org/blogs/ukrainealert/why-ukraine-s-major-achievement-in-government-transparency-may-fail/

Although the verification process and the enforcement still require an improvement, the anti-corruption agencies, law enforcement bodies, journalists, civil society and citizens themselves have now access to over 1 million declarations per year. The donors agree that despite of its weaknesses, and apart from increasing the transparency, the benefit of the system has been also its role 'as a deterrent' for some officials who would contemplate the graft.

A GfK/UNDP survey conducted in 2017 has revealed that an overwhelming majority of Ukrainians (72 per cent) have positive or somewhat positive opinions about the system and its resulting transparency. Civil servants who submitted their declarations in 2016 expressed an even higher level of support for the system and its openness (82 per cent)[110].

Existing research suggest that there is close and positive correlation between the existence of the disclosure systems and the lower level of corruption[111].

Regarding the key ownership for this reform and the relative impact of the MFA III conditionality, this was certainly one of the main incentives, albeit not the only one. The set-up of the system was linked to the discussions on EU visa liberalisation, and was also promoted by, *inter alia*, the IMF EFF conditionality[112] that played a decisive role, Danish Ministry of Foreign Affairs (financial support to develop the system's software) and UNDP (e.g. supported the tool development). There were also number of governments (e.g. the US) who consistency pushed for the advancement of this reform (e.g. conditioning the deployment the US debt guarantee facility on the sufficient progress with the system).

The asset declaration system has been included in the subsequent MFA IV and IMF program (SBA 2019).

Annex 1: Statistics

Year	Number of declarations published in the Unified State Register of declarations*	Number of cases of failure to submit or late submission of Declarations (based on messages received by NAZK)	Number of processed messages on possible false information in the declarations	Number of processed requests for special inspection of the information specified in the declaration of the person applying for the position of a person authorized to perform the functions of the state or local self-government	Number of complete verification of declarations (completed)	Number of d made on the of complete verification o declarations
2016	106997	1700	n/a	n/a	n/a	n/a
2017	987116	18688	1089	8398	634	143
2018	856857	17000	2719	11133	615	472

110 UNDP, 2018. Electronic asset declarations for Public Officials. Available at: https://www.ua.undp.org/content/ukraine/en/home/blog/2018/the-expectations-and-reality-of-e-declarations.html

111 Djankov, S. 2009. Disclosure by politicians. Available at: https://www.nber.org/papers/w14703

112 See for instance the pressure exerted by the IMF in the context of the delays in certification of the system. Available at: https://concorde.ua/rs/daily/item_58548/

2019	845220	23000	3292	9110	1133	1 535

Table 13. Conditionality #6, 3rd tranche – Governance and transparency, Anti-corruption

Conditionality number 6 – Following the establishment of an online database on beneficial ownership of companies, put in place mechanisms to verify, post-registration and on a selective basis following clear criteria, the accuracy of the information provided by companies and enforce compliance with this obligation.	
Relevance and importance	In accordance to art. 17 of the Law of Ukraine «On the state registration of legal persons and private entrepreneurs», the Single state register of legal persons and private entrepreneurs (hereafter referred to as "Single State Register") contains information on the final beneficiary owner of a legal person including the final beneficiary owner of its founder, should this founder be a legal person. The register was in place prior to the signature of MoU (May 2015) and by summer 2015 contained records on circa 1.5 million companies. The full data was published in open format on the Unified State Web Portal in August 2015. Generally, financial monitoring of beneficiary owners of the companies has been relevant in the context of a number of areas including prevention and counteraction to legalization of the proceeds from crime (money laundering), to terrorism financing as well as to financing of the proliferation of weapons of mass destruction[113]. The anonymous corporate structures have often been a cloak for corrupt and criminal activities such as embezzlement, contract fraud, organized crime and money laundering. The resulting capital flight has deprived the citizens of Ukraine of much-needed revenue, degraded the business environment, and entrenched corruption and poverty at the expense of the many for the benefit of the few[114]. Yet, the Ministry of Justice notified DG ECFIN in 2015 that the procedure for the check of the information provided by companies on their beneficiary owners cannot be established in the state registration of legal persons and private entrepreneurs, since the state registration is based on the «declarative» principle. In addition, relevant Ukrainian institutions were not able to perform this monitoring (and identify relevant infringements of the law caused by legal persons) given restrictions on seeking this information[115] and frequent failures of legal persons to submit the information on the final beneficiary owner to the state register. Therefore, while the register was in place, the mechanism to verify in an effective way the accuracy of the information submitted by

[113] See for instance Art. 14 of the Law of Ukraine 'On prevention and counteraction to legalization (money laundering) of the proceeds from crime or terrorism financing, as well as financing of the proliferation of weapons of mass destruction'

[114] Open Ownership, 2018. Beneficial ownership transparency in Ukraine – Technical Report. Available at: https://www.openownership.org/uploads/improving-beneficial-ownership-transparency-in-ukraine.pdf

[115] Only in the context of prevention and counteraction to legalization (money laundering) of the proceeds from crime or terrorism financing as well as financing of the proliferation of weapons of mass destruction

	companies on the "Unified State Register of Legal Entities, Private Entrepreneurs and Public Associations" (USR) was still missing[116] and there were no provisions to enforce compliance with this obligation (such as a dedicated unit responsible for the verification with explicit procedures, possibilities for stakeholders outside the administration to flag irregularities and a clearly designated institution responsible for follow-up and possible sanctions). Consequently, this meant that the likelihood that companies submitting false or incomplete information would be traced and sanctioned remained low. Indeed, in the January 2016 – October 2017 period, there were only five cases in which sanctions were taken for the falsification of beneficial ownership data[117] and only around 20 per cent of companies complied with the obligation to report the data to the register. There were also number of other issues related to, inter alia, data quality, maintenance of records and data validation[118][119]. More broadly, however, the ex-post evaluation found out that the request to fulfil this condition was demanding, arguably too demanding for Ukraine back in 2015-17. Prior to its implementation, there was no single country in the EU with the public register of the beneficial owners of corporate entities registered in country. Despite that, Ukraine became the second country in the world (after the UK) to implement a public register of the beneficial owners of corporate entities registered in country in 2016[120]. In 2017, Ukraine became the first country in the world to commit to integrating with the OpenOwnership Register, which links beneficial ownership data from around the world[121].
Implementation	The key stakeholder responsible for implementation of this condition was the Ministry of Justice that was working in close cooperation with the Anticorruption Action Centre (ANTAC)122, an NGO specialised in the fight against corruption, to design a system that would allow the Financial Intelligence Unit of Ukraine and the new Asset Recovery Office to efficiently verify the information submitted to the "Unified State Register of Legal Entities, Private Entrepreneurs and Public Associations" (USR) by companies regarding their beneficial

[116] DG ECFIN, October 2016. Mission Report.

[117] DG ECFIN, 2018. Note to the EP and Council on compliance with conditions underpinning the third tranche of the MFA III.

[118] Open Ownership, 2018. Beneficial ownership transparency in Ukraine: what's next? Available at: https://www.openownership.org/news/beneficial-ownership-transparency-in-ukraine-whats-next/#:~:text=In%202016%20Ukraine%20became%20the,corporate%20entities%20registered%20in%20country.&text=To%20date%2C%20approximately%20253%2C000%20Ukrainian,ownership%20to%20the%20companies%20register.

[119] Global Risk Affairs, 2017. Investigating Ultimate Beneficial Ownership in Ukraine. Available at: https://www.globalriskaffairs.com/2017/12/investigating-ultimate-beneficial-ownership-in-ukraine/

[120] Open Ownership, 2018. Beneficial ownership transparency in Ukraine: what's next? Available at: https://www.openownership.org/news/beneficial-ownership-transparency-in-ukraine-whats-next/#:~:text=In%202016%20Ukraine%20became%20the,corporate%20entities%20registered%20in%20country.&text=To%20date%2C%20approximately%20253%2C000%20Ukrainian,ownership%20to%20the%20companies%20register.

[121] Open Ownership, 2018. Beneficial ownership transparency in Ukraine – Technical Report. Available at: https://www.openownership.org/uploads/improving-beneficial-ownership-transparency-in-ukraine.pdf

[122] AntAC, 2020. Zero Corruption State. Available at: https://antac.org.ua/en/

	ownership. The role of the ANTAC was, inter alia, to provide and independent feedback on the actual effectiveness of solutions put forward by the Ministry of Justice. At the EU side, the key responsibilities laid with DG ECFIN and the EU TAIEX. The key task that had to be performed (by the Ministry of Justice) was the introduction of a search function in order to make the information it contains usable and verifiable by the general public[123]. The introduction of a search function did not require any legislative changes.
Evidence of Implementation deficit	The implementation of this condition was problematic, had subsequent delays and was eventually insufficient to categorise this condition as 'met'. It was one of the conditions blocking the disbursement of the third tranche. On 26.10.2016 the vice-prime-minister of Ukraine on European and Euro-Atlantic Integration of Ukraine requested the Ministry of Justice and Finance, MEDT and SFMS to speed up the process of fulfilment of this condition. By October 2017, DG ECFIN mission that travelled to Kyiv was still awaiting for some evidence of how incomplete or false entries would be identified and dealt with. In the information note to the EP and the Council sent by DG ECFIN as part of the assessment underpinning the disbursement of the third tranche, the DG summarised: "Although Ukraine took steps to increase the transparency of the register of companies' beneficial owners, the authorities have not put in place an effective mechanism to verify the information that companies are requested to submit on their beneficial ownership, and to enforce compliance with this obligation. As a result, the possibility that companies submitting false or incomplete information will be traced and sanctioned remains low, which limits their incentives to comply with this obligation". Consequently, this condition became one of four conditions that alltogether contributed to the decision not to disburse the third tranche under the MFA III. The condition, in modified and more specific form, became subsequently part of the MFA IV conditionality[124]. DG ECFIN mission from June 2018 points towards discussions between both sides, including on some existing constraints e.g. lack of existence of the international data exchange for beneficiary ownership data, making cross border verification impossible
Evidence of benefits and contribution of MFA	In a narrow sense, given that the condition was not eventually met, the explicit benefits of this condition up until late 2017 was limited. Going forward, however, the benefits have been very substantial. The MFA IV condition on beneficial ownership has been already met. The system is now fully operational. Even if the official portal may be

[123] DG ECFIN, June 2017. Mission Report.

[124] See Memorandum of Understanding for the MFA IV. Available at: https://ec.europa.eu/info/sites/info/files/economy-finance/mou_protocol_version_eu.pdf

	still clunky, all records are publicly available. According to local experts, the reliability of the data is satisfactory. The system has been prised internationally on number of occasions[125]. Among users of the register have been, inter alia, civil society organisations specialising in fight against the corruption. Apart from the EU (via the MFA III and MFA IV), WB and the IMF[126] were also promoting the progress in this reform[127], though unlike for some other anti-corruption reforms in Ukraine, the role of IMF and WB did not appear to be more critical than the EU one.

Table 14. Conditionality #7, 3rd tranche – Governance and transparency, Anti-corruption

Conditionality number 7 – In order to ensure that officials accused of corruption cannot benefit from the proceeds of their corruption offences: (i) designate an institution to act as Asset Recovery Office; and (ii) adopt operational guidelines, including a framework for inter-agency cooperation, for the implementation of extended and civil confiscation provisions.	
Relevance and importance	Asset recovery is an important component of the system of effective fight against corruption, money laundering and organized crime128. Assets stolen and siphoned off from the state by the former regime prior to Maidan were huge with some estimates reaching up to USD 40 billions[129]. However, the lack of legal and institutional mechanisms did not allow the state to trace and manage stolen assets. The need to trace and recover the corrupt assets became particularly apparent after Maidan Revolution130. In addition, the General Prosecutor's Office of Ukraine (GPO) that was in charge of the investigation, prosecution and subsequent asset recovery of corruption crimes committed by Yanukovych and his associates between 2014 and 2016 was perceived as prone to political interference. For instance, during 2014-2016 there have been four changes of General Prosecutors and current General Prosecutor, also for political reasons. Ukrainian Anti-Corruption Strategy for 2014-2017 which defined asset recovery as one of the main benchmarks of ongoing anti-corruption reform. Asset seizure per se is not an ARMA function – it traces assets and then manages them if they are frozen by court

[125] EITI, 2017. Kyrgyzstan receives the first EITI Chair's Award for Beneficial Ownership Transparency. Available at: https://eiti.org/news/kyrgyzstan-receives-first-eiti-chairs-award-for-beneficial-ownership-transparency

[126] IMF, 2014. Request for SBA.

[127] WB, 2018. Beneficial Ownership Transparency. Available at: https://olc.worldbank.org/content/beneficial-ownership-transparency

[128] WB, 2017. Asset Recovery in Ukraine – Practical Guide. Available at: https://star.worldbank.org/sites/star/files/ar_guide_ukraine_english.pdf

[129] AAC, 2017. Ukraine's experience in Asset Recover. Available at: https://ti-ukraine.org/news/will-the-agency-for-yanukovych-s-assets-recovery-really-work/

[130] Transparency International, 2017. Will the Agency for Yanukovych asstes' recovery really work? Available at: https://ti-ukraine.org/news/will-the-agency-for-yanukovych-s-assets-recovery-really-work/

	order.
Implementation	The law establishing the "Asset Recovery and Management Office " (ARMA) was adopted on 10 November and promulgated on 11 December 2015. It came into force on 11 June 2016. However, as of late 2016, the agency was not operational yet as its head still needed to be appointed and selection process for an independent candidate was dragging. As a result, operational guidelines, including on aspects related to cooperation with other anti-corruption agencies, also remained to be developed. In December 2016, Mr. Anton Yanchuk, Deputy Minister of Justice, was appointed as the Head of the Asset Recovery and Management Office (ARMA). The action plan to ensure that ARMA can properly exercise its functions was adopted on 14 December 2016. However, ARMA could only become operational once at least 30 per cent of its staff would be recruited. This target was planned to be reached by August 2017, which should enable ARMA to start exercising its functions related to the tracing and finding of assets illegally acquired. Only then ARMA planned to start negotiating operational guidelines, including on aspects related to its cooperation with other anti-corruption agencies.[131] In Autumn 2017 the Ministry of Finance provided a hardcopy of the "Joint Order" approved on 20th October that aimed to establish cooperation between ARMA and relevant law enforcement bodies e.g. NABU and GPO (collaboration at the stage of pre-trail investigation) and the financial sector regulators and the Ministry of Justice. According to the ECFIN mission report from October 2017, subject to the verification of the content of this Joint Order, this condition was considered as broadly fulfilled. As of late 2017, ARMA was not still fully operational with staff recruitment and training activities still being undertaken[132]. By the end of 2017, ARMA recruited 52 employees and 20 more transferred from other agencies so it reached ca 55 per cent of full capacity, albeit it already started to fulfil its functions ie managing frozen assets. By end of 2018, it had 108 employees out of 130 envisaged. Another 240 staff were authorized for regional offices in later 2018. In 2019 ARMA had 134 employees (out of increased target of 195) in central office and 40 in regional offices[133].
Evidence of Implementation deficit	This condition has been considered as fulfilled by the EC. Some delays, to certain extent unavoidable, took place while establishing and operationalising the agency e.g. at the stage of recruitment of the key management staff. The ARMA's critical competence were also envied by some political groups seeing it as potentially powerful tool in exercising pressure on

[131] DG ECFIN, June 2017. Mission Report.

[132] OECD, 2018. Training on asst recovery for Ukraine's Asset Recovery and Management Agency. Available at: http://www.oecd.org/corruption/acn/firsttrainingonassetrecoveryforukrainesnewassetrecoveryandmanagementagency.htm

[133] ARAM Annual Reprots

	their opponents.
Evidence of benefits and contribution of MFA	There is no comprehensive and reliable statistics and reports on the asset recovery matters made by the government. On 28 April 2017, the GPO informed about confiscation of approximately of 1.5 bln USD held in governmental bonds previously frozen during the investigation of corruption crimes of Yanukovych and his associates[134]. Some rough estimates show that since its establishment up until 2019, the ARMA traced and helped to seize the sizable assets including USD 2 bln in shares and bonds, and over 1,200 of real estate items and cars[135]. Yet, the evidence from years 2016-2018 suggest that vast majority of convictions in corruption cases relate to low-middle level public officials[136]. In terms of the relative contribution of the MFA to progress with this reform, apart from the EU (via MFA III), the condition was also promoted by the IMF as part of its EFF program. In addition, other organisations in promoting the asset recovery system included the WB[137], OECD[138], and EUACI (technical assistance) and Swiss Ministry of Foreign Affairs (via financing of TA)[139]. Overall, the relative weight of the MFA III in supporting progress in this reform vis-à-vis the efforts of other donors and agencies was not superior. Generally, the EU seems to have led technical assistance efforts and it should be also noted that ARMA was part of Visa Liberalization conditionality.

[134] Kyiv Post, April 2017. Lutsenko: confiscated USD 1.5 bln of Yanukovych team's funds transferred to Ukraine's budget. Available at: https://www.kyivpost.com/ukraine-politics/lutsenko-confiscated-1-5-billion-yanukovych-teams-funds-transferred-ukraines-budget.html

[135] ARMA Annual Reports

[136] AAC, 2017. Ukraine's experience in Asset Recover. Available at: https://ti-ukraine.org/news/will-the-agency-for-yanukovych-s-assets-recovery-really-work/

[137] WB, 2017. Asset Recovery in Ukraine – Practical Guide. Available at: https://star.worldbank.org/sites/star/files/ar_guide_ukraine_english.pdf

[138] AAC, 2017. Ukraine's experience in Asset Recover. Available at: https://ti-ukraine.org/news/will-the-agency-for-yanukovych-s-assets-recovery-really-work/

[139] Swiss Ministry of Foreign Affairs, 2018. Asset Recovery Support Project. Available at: https://www.eda.admin.ch/eda/en/fdfa/fdfa/aktuell/dossiers/alle-dossiers/engagement-der-schweiz-in-ukraine/strategie-2015_2018.html/content/dezaprojects/SDC/en/2017/7F09386/phase1?oldPagePath=/content/eda/en/home/das_eda/aktuell/dossiers/alle-dossiers/engagement-der-schweiz-in-ukraine/strategie-2015_2018.html

Table 15. Conditionality #7, 2nd tranche – Governance and transparency, Public administration

Conditionality number 7 – Adopt the legislative package on the Civil Service and ensure its entry into force, so as to depoliticise and professionalise the civil service through a clear delimitation between the political and administrative function and to foster effective human resource management.	
Relevance and importance	The reform of the public administration was long overdue in Ukraine. Already in 2011, the government intended to reform the 1993 law on Civil Service. The 2011 reform law was however never enacted. A new draft legislation was sent to the parliament after significant delay in March 2015, just at the time of the MFA III negotiations[140]. In that historic context of previous failed attempts to reform the public administration, an MFA condition to make sure that the new law would be adopted (and enacted without postponement) was welcome. It reinforced the message of the Association Agenda which had explicit reference to the need to finalise and adopt of the draft Law on Civil Service Reform141 and of the budget support programme on Public Administration Reform whose launch was encountering delays
Implementation	- The law "On the Civil Service" was approved by the Parliament in December 2015. - It entered into force on 1 May 2016 - The EU-OECD SIGMA programme and key stakeholder supported the drafting of this law. - The law aims to address political interference in the selection and daily activities of civil servants to guarantee professionality and efficiency in the public service. One of the focus of the new law is on reforming wage setting (e.g. the share of bonus given on a rather discretionary basis). This is achieved by capping variable salary at 30% of the total amount of the annual fixed salary payroll[142].
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. - There is no evidence of implementation deficit.
Evidence of benefits and contribution of	The adoption of the law represented a major step forward. The legal framework is now in line with European standards. Ukraine has also

[140] OECD report on anti-corruption measures in Ukraine Round 3, March 2015; available at : https://www.oecd.org/daf/anti-bribery/Ukraine-Round-3-Monitoring-Report-ENG.pdf

[141] EU-Ukraine Association Agenda - endorsed by the EU-Ukraine Association Council on 16 March 2015 available at: http://eeas.europa.eu/archives/docs/ukraine/docs/st06978_15_en.pdf

[142] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

MFA	started its application in practice. The position of state secretaries has been created and their effective recruitment started. State secretaries are in charge of key functions (including publication of vacancies, competitive selection, appointment, career planning, promotion and training, discipline and the complaints of civil servant) and thereby helping with the effective delineation of political and civil service positions[143]. Despite the new law and improvements made, challenges with the efficiency of the civil service, especially in view of its size, remain. The remuneration system of civil servants does not yet allow to for recruit, motivate and retain civil servants with required education level and professional skills, according to the NACS itself. Besides, the provision of the Civil Service law to limit the share of bonuses to 30% entered into force only after a long transition period in January 2019. According to the latest estimates the share was still at 55% in 2019 (down from 70% in 2015). Exceptions had however been voted for 2019, an election year, through Law "On State budget of Ukraine for 2019" permitting additional incentives to the civil servants[144]. Some negative developments have also taken place most recently. In September 2019, the law on the Civil Service has been substantially amended[145], with harmful consequences for the stability of the civil service. Of particular concern is that procedures for dismissal of civil servants have been simplified. Category A officials can notably be dismissed without the need for further justification within 4 months of the appointment of a new minister, leaving the door open for politically motivated dismissals. The EU has advocated against this policy reversal following which a provision making sure htat those dismissed be provided a new occupation was inserted. The legislative package on the Civil Service was a reform that was heavily supported by the EU through the MFAIII, its Budget Support programme and technical assistance. Stakeholders largely agree that no such progress would have been made without the EU support. The wider international community including the OECD, the GIZ and the EBRD[146] also provided technical assistance to UA authorities in this area. The Sigma Programme notably reviewed the law upon the request of the EU Delegation.

Table 16. Conditionality #8, 2nd tranche – Governance and transparency, State-owned enterprises

[143] OECD (2018) Anti-Corruption Reforms in Ukraine: Prevention and Prosecution of Corruption in State-Owned Enterprises. 4th round of monitoring of the Istanbul Anti-Corruption Action Plan.

[144] OECD (2019) Anti-Corruption Reforms in Ukraine: Prevention and Prosecution of Corruption in State-Owned Enterprises. 4th round of monitoring of the Istanbul Anti-Corruption Action Plan. Available at https://www.oecd.org/corruption/acn/OECD-ACN-Ukraine-4th-Round-Bis-Report-SOE-Sector-2018-ENG.pdfhttps://www.oecd.org/corruption/acn/OECD-ACN-Ukraine-Progress-Update-2019-EN.pdf

[145] https://voxukraine.org/en/imore-focus-new-civil-service-legislation/

[146] The EU joint support with European Bank for Reconstruction and Development (EBRD) for Ukrainian Reforms Architecture amounted €27 million

Conditionality number 8 – In order to strengthen reporting obligations, adopt a list of state-owned enterprises to be converted from unitary into joint stock companies. In addition, audits will be launched for a substantial share of the 100 largest state-owned enterprises.	
Relevance and importance	SOEs represent a large share of the economy, representing 22% of value added in the non-financial corporation sector in 2015[147]. A weak governance of SOEs may however lead to a mismanagement of public revenues. In Ukraine, many enterprises have been making losses. In 2014, the Ministry of Finance estimated that almost 2.5% of GDP had to be directed to SOEs for mandated programs and cost-recovery purposes. SOE operations are also a source of corruption because of the lack of appropriate control mechanisms and insufficient transparency. An OECD report had in particular recommended that unitary enterprises be incorporated, as unitary enterprise, a special corporate form exclusively reserved to SOE, had been associated with high risk of corruption because of the absence of any independent external control – i.e. no obligation to have supervisory boards a no external independent audit,
Implementation	In September 2015, a decree aiming to smooth the conversion of state-owned companies (SOEs) from unitary to joint stock companies was passed by the Cabinet of Ministers[148]. Further decrees were adopted by the Ministry of Economy and Trade, which enabled the conversion of a total of 14 SOEs into joint stock companies. A number of 49 state-controlled companies had been audited as of July 2016, including some of the largest SOEs such as Naftogaz, the State Railway Company and the Odessa Seaport. Further contracts for financial audits of 15 SOEs (incl. 11 large companies) have been signed by mid-July 2016 according to the MEDT[149].
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. - There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	Conditions were met but the progress in this area was challenging. There is no up-to-date comprehensive overview on the outcome of those reforms (e.g. number of SOEs from the list which had been established which have been converted to joint stock companies). In the field of corporate governance more generally, one milestone - concerning all SOEs- was achieved when the legal foundations for establishing independent and professional supervisory boards at

[147] IER calculation based on data on p. 143 of “National accounts of Ukraine for 2015” Ukrstat publication found at http://www.ukrstat.gov.ua/druk/publicat/kat_u/2017/zb/02/zb_nru2015pdf.zip

[148] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

[149] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

	SOEs were adopted. This significant horizontal legislative change aside, improvements in this field are rather incremental, one SOE after the other, as technical assistance (from e.g. the EBRD) becomes available. Concerning the requirement for largest SOEs to undertake an independent external audit which is now in place, according to the OECD[150], results of implementation of this requirement are extremely poor. Overall EU/MFA contribution to the SOE reform process seems quite limited, though the EU/MFA contribution is more substantial in some specific fields, notably external audit of SOEs (see also PFM conditions).

Table 17. Conditionality #8, 3rd tranche – Governance and transparency, Public administration

Conditionality number 8 – Adopt a comprehensive strategy and implementation plan for Public Administration Reform at both central and sub-central levels in compliance with relevant SIGMA benchmarks.	
Relevance and importance	For it to be effective, PAR needs to be well managed, i.e. based on an overall vision and prioritised objectives and more detailed implementation plan to realistically and coherently plan the sequencing of reforms. As such having a well thought through strategy is a key starting point, even if it does not bring about legislative changes. In fact, the adoption of the PAR strategy was a pre-condition for the EU PAR programme. According to EU stakeholders, delays with the adoption of the PAR strategy had delayed the PAR programme for one year before the MFA condition came into play.
Implementation	In June 2016, the Cabinet of Ministers adopted the public administration reform (PAR) strategy for 2016-2020. The PAR incorporates a matrix of objectives and performance indicators, an indicative cost estimate for implementation of the strategy and an implementation plan for 2016-2020[151]. The strategy and the implementation plan follow the structure of the "Principles of Public Administration" as set out by SIGMA (Support for International Governance and Management), a joint EU and OECD initiative that provide expert advice on public administration reforms. In the second half of 2018, a mid-term review of the PAR strategy is foreseen following a baseline measurement of Ukraine's public administration against OECD/SIGMA principles of public administration.

[150] OECD (2018) Anti-Corruption Reforms in Ukraine, Prevention and Prosecution of Corruption in State-Owned Enterprises

[151] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	The strategy and the implementation plan were assessed as being of good quality as per OECD/SIGMA principles of public administration. Quality strategic documents are being in place. There were a few caveats to the otherwise positive assessment. First of all, the strategy contains limited information on costs and sources of funding[152]. Secondly it does not draw enough on reliable civil service statistics. The lack of a unified registry has been making the planning and implementation of PAR more complex. Ukraine has started working on a human resources portal called Integrated Human Resource Management Information System (HRMIS) in 2017, after the adoption of the PAR strategy, with the support of the World Bank and the EU[153]. HRMIS is a unified system integrating all the currently fragmented HR systems of the various public institutions. It will help consolidating and automating the management of human resources and payroll information for all civil servants (efficiency objective) and allow the provision of up-to-date civil service statistics (transparency objective and decision aid). In that context, a baseline measurement of Ukraine's public administration against OECD/SIGMA principles of public administration was conducted in 2018, following which the PAR strategy was reviewed and amended. Overall EU/MFA contribution to the elaboration of the PAR strategy was key, alongside the role of the OECD/SIGMA programme.

Table 18. Conditionality #9, 3rd tranche – Governance and transparency, Public administration

Conditionality number 9 – Adopt the by-laws relevant for the legislative package on the Civil Service.	
Relevance and importance	Given how past reform efforts had stalled, insisting on the adoption of secondary legislation was important. It aimed at ensuring that the law on the Civil Service (whose adoption was a condition of the second tranche) would effectively be implemented.
Implementation	On 1 May 2016, the law on the civil service entered into force[154]. Prior this law, the Ukrainian authorities had adopted the key legislative acts and by-laws required for the effective

[152] OECD (2018) Baseline Measurement Report: The Principles of Public Administration Ukraine June 2018

[153] https://www.worldbank.org/en/news/press-release/2017/06/30/ukraine-to-increase-transparency-efficiency-in-public-resource-management-with-european-union-and-world-bank-support

[154] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

	implementation of the law. These include, among others, standard regulation on performance assessment of civil servants, a procedure to verify the knowledge of the state language (Ukrainian), and recommendations concerning the definition of individual performance indicators for civil servants of categories B and C[155]. A total of 40 legislative acts were adopted. Out of these, the Cabinet of Ministers of Ukraine adopted 23 resolutions and one order, while the National Agency of Ukraine on Civil Service (NACS) adopted 16 orders.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	see table on condition #7, 2nd tranche

Table 19. Conditionality #10, 3rd tranche – Governance and transparency, Public administration

Conditionality number 10 – Consistent with the new legal framework on the Civil Service, start running open competitions for the recruitment of civil servants.	
Relevance and importance	The previous legal framework (prior to the new law on Civil Service) did not make any reference to the principle of merit-based recruitment. While recruitment to positions of civil servants of categories 3 to 7 had to be carried out on competitive basis, recruitment to higher positions of civil service (categories 1-2) was carried out without competition. The law on the Civil Service addressed the issue. However, at the time of the MFA negotiations, when the law was still a draft, there were concerns that the provisions on merit-based recruitment would be applied with delay, as from 2017 according to the transitional provisions of the Draft Law on Civil Service (provision 9). While recognising possible capacity issues given the workload at the time, experts like those from the OECD had highlighted the need to promptly start with merit-based recruitment to ensure the professionalism and avoid politicisation of civil service.
Implementation	Since the entry into force of the law on the civil service, Ukrainian

155 DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

	authorities started running open competitions for the recruitment of civil servants. In September 2017, the Government started practical implementation of the concept of reform staff positions adopted in November 2016[156]. In mid-June 2016, the Senior Civil Commission was set up for selecting top (Category A) public officials. A large recruitment process was announced to fill in positions in newly established policy directorates in 13 pilot institutions (10 ministries, 2 agencies and the Secretariat of the Cabinet of Ministers). The creation of a dedicated web portal (www.career.gov.ua), where vacancies are published and allows potential candidates to submit their applications online, seeks to ensure transparency.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	- Recruitment to civil service positions through open competitions is now an established practice. The launch of the competition started within the timeframe for top officials and reform positions. It has now been rolled out and no exceptions to filling the positions by open competitions are being reported. - Some challenges have been flagged[157] but these are of a different nature and relate to the capacity, professionalism and independence of the members of the commissions selecting the candidates or the lack of publication of the job advertisements. Continuous progress is reported though in this regard. For instance, non-governmental experts and the public in the selection commission are now involved in the selection process and additional channels are mobilise to disseminate job vacancies[158].

A5.3 Energy sector

Table 20. Conditionality #9, 2nd tranche – Energy sector

Conditionality number 9 – Strengthen the independence of the National Energy and Utilities Regulatory Commission by adopting the relevant law on the energy market regulator compliant with Energy Community acquis requirements and endowing the NEURC with sufficient administrative capacity.	
Relevance and	Since its creation in 1994 and until 2016, the NEURC, the energy's

[156] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

[157] OECD (2017) Anti-corruption reforms in Ukraine, 4 th round of monitoring of the Istanbul Anti-Corruption Action Plan

[158] OECD (2019) Progress update. 4 th round of monitoring of the Istanbul Anti-Corruption Action Plan

importance	regulatory body, was subordinated to the President and accountable to the Parliament – which seriously conflicted with the requirement of independence.
Implementation	A new law on the energy regulator entered into force in November 2016[159]. The first draft of this law, submitted in May 2015, had to be amended after its rejection by the Parliament. The new draft law was supported by an independent group of experts that included civil society representatives and parliamentary members. The Energy Community Secretariat has expressed that the law is deemed to be compliant with the EU energy acquis[160].
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	The adoption of the law has generally positively affected the NEURC's activities, particularly in terms of transparency of information and data. In addition, the new procedure for the selection of the Commissioners (based on open competition and setting up of a selection board) can be legitimately regarded having increased the independence of the actions of the NEURC and having reduced the informal political pressure[161]. However, the regulator still needs to improve its reporting procedures, better substantiate its decisions, and enhance the protection of consumers.[162] MFA III was not the only instrument promoting the independence of Ukraine's energy regulator. The World Bank had the same objective through its programme Development Policy Loan. The IMF through its 2014 SBA programme had already supported energy reforms for both the NERC (gas price regulator) and the NURC (the utility price regulator) before the merger. The EBRD has responded to a request from the NEURC to deploy consulting services to support implementation of reforms in the electricity sector.

159 DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

160 DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

161 http://dixigroup.org/storage/files/2018-09-14/neurc_e.pdf. Regarding the Dixi Group report's, member of the Commission may not be affiliated to a political party during a period of at least three months before application.

162 http://dixigroup.org/storage/files/2018-09-14/neurc_e.pdf

Table 21. Conditionality #10, 2nd tranche – Energy sector

Conditionality number 10 – In preparation of the entry into force of the Gas Market Law in October 2015, adopt the relevant secondary legislation to ensure full consistency and effectiveness.	
Relevance and importance	The new Gas Market Law aimed mainly to increase Ukraine's natural gas independency from Russia. In addition, since its accession to the Energy Community in February 2011, Ukraine is legally bound by the *acquis communautaire* (based on article 11) and thus must meet the EU's natural gas standards. This condition reinforced IMF's EFF condition requiring a new Gas market law to be approved by the Parliament.
Implementation	On 1 October 2015 the Gas Market Law entered into force[163]. For the effective implementation of the Gas Market Law, several regulations and implementing provisions were adopted in the course of 2015 by the NEURC and other Ukrainian authorities. These involve, among others, codes on natural gas distribution and transmission, gas supply rules and methodology for network tariffs
Evidence of Implementation deficit	√ This condition has been considered as broadly fulfilled by the EC. There is no evidence of implementation deficit. The Energy Community Secretariat considered that the regulations implemented generally conform to the requirements specified in the natural gas acquis for the Contracting Parties of the Energy Community and to best regulatory practices[164]. Although the main part of the secondary legislation required by the Gas Market Law is in place, several legal acts are still to be approved or modified in order to fully transpose the Energy Community legislation in this area[165].

163 DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

164 DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

165 https://energy-community.org/implementation/Ukraine/secondary.html

Evidence of benefits and contribution of MFA	Beyond the needed compliance with the European Policies, the unbundling of gas sector monopoly, developed of a competitive market and allow customers to choose or switch their gas natural suppliers.[166] The EU provided technical assistance through the project EU4Energy (2016-2020), helping with the preparation of the secondary legislation.

Table 22. Conditionality #11, 3rd tranche – Energy sector

Conditionality number 11 – Make substantial progress with the implementation of the Gas Sector Reform Implementation Plan adopted by the Cabinet of Ministers on 25 March 2015, notably its provisions on unbundling, including the adoption of an unbundling model for gas transmission and the provisions on unbundling of distribution companies.	
Relevance and importance	In order to comply with Energy Community Treaty and Association Agreement, Ukraine needed to make substantial efforts to provisions on unbundling model for gas transmission and the distribution companies. Indeed, in 2015, the monopolistic structure of the market was reportedly contributing to making the market inefficient. The introduction of this new model was intended to allow competition in the sector and ensure a better delivery of this utility.
Implementation	In March 2015, the reform plan for the gas sector was approved[167]. In October 2015, the new gas law entered into force. In October 2016, a draft law amending 14 laws in line with the 2015 Gas Law was submitted to the Parliament. In July 2016, the Cabinet of Ministers approved a comprehensive plan for restructuring Naftogaz that was endorsed by the Energy Community Secretariat. Over the lifetime of MFAIII, a total of 42 distribution companies have been legally unbundled[168].However, the unbundling of oil and gas company Naftogaz had at first advanced at a slower pace than initially expected. In January 2017, a new company called Trunk Gas Pipelines of Ukraine, was registered by the Ministry of Energy and Coal Industry

166 Explanory note to the draft Resolution of the Cabinet of Ministers of Ukraine “On Approval of the Regulations on Imposing Specific Duties on Natural Gas Market Participants to Meet General Public Interests in Course of Natural Gas Market Performance (Relations in 2017-2019)”.

https://www.energy-community.org/dam/jcr:5478c9e0-c0ae-4c70-8637-41c603fb391f/UKR_PSO%20Resolution_explanatory%20note.pdf

167 DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

168 DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

	to act as a gas transport operator, .
Evidence of Implementation deficit	√ This condition has been considered as broadly fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	Ukraine announced in January 2020 the completion of gas transmission unbundling. In fact, the new Operator GTS Ukrainy replaced Ukrtransgaz, the former public gas transmission company.[169] Since, gas transmission became independent and regulated as its peer in the EU. In this specific area, the strong support of the EBRD was key. Indeed, the Bank has supported the Natfotgaz reforms through a first project "Emergency Pipeline Upgrade and Modernization" signed in 2014 and a complementary one in 2015, to bridge the gap between purchase and sale of natural gas. The total amount of the projects amounted € 300 million[170].

Table 23. Conditionality #12, 3rd tranche – Energy sector

Conditionality number 12 – Amend the electricity market law in line with Ukraine's commitments under the Energy Community Treaty.	
Relevance and importance	This new legislation was meant to help Ukraine modernize its ageing electricity-producing and transmitting infrastructure by introducing a new set of tariffs that help to recover revenues. The overarching objective was to allow Ukraine to enter in the European electricity market called ENTSO-E, as required by both Energy Community Treaty and the Association Agreement.
Implementation	The new electricity market law was drafter in cooperation with the Energy Community Secretariat[171]. In September 2016, the new law was passed in first reading by the Parliament. In mid-April 2017, the second and final reading took place.

169 https://www.kyivpost.com/business/ukraines-naftogaz-announces-completion-of-gas-system-unbundling.html

170 https://www.ebrd.com/work-with-us/projects/psd/naftogaz-gas-purchase-facility.html

171 DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

	In June 2017, the draft law was signed by the Ukrainian President. Following a transition period, most of the provisions of the new law entered into force on 1st January 2019, as Ukraine opening a retail electricity market allowing customers to choose their supplier. Also, on 1st July 2019, the wholesale market was created in order to replace the previous single buyer model[172].
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit. In line with the Third Energy Package, the law establishes the legal and organisational separation of distribution and transmission of electricity from other activities.
Evidence of benefits and contribution of MFA	Ukraine, through Ukrenergo, has signed agreements on July 2017 to undertake a series of measures over the next 5 years (until 2022) in order to fully integrate the ENTSO-E[173]. The process is thus still ongoing. For now, Ukraine has 8 interconnections with some European countries[174]. Compared with the gas market, Ukraine's progress with the reform of the electricity market is lagging behind.

172 Energy Community report, "Ukrainian electricity wholesale market opening A critical assessment of the first two months

173 https://www.entsoe.eu/news/2017/07/07/entsoe-ce-agreement-conditions-future-grid-connections-with-ukraine-moldova/

174 https://ec.europa.eu/energy/sites/ener/files/documents/2nd_report_ic_with_neighbouring_countries_b5.pdf

Table 24. Conditionality #13, 3rd tranche – Energy sector

Conditionality number 13 – In order to improve energy efficiency: (i) initiate the process of extending the coverage of heat meters and temperature control devices, including by adopting a law on heat metering with clearly assigned responsibilities and deadlines; and (ii) strengthen the legal framework for the efficient use of energy resources by adopting legal acts on energy efficiency, in particular a national energy efficiency action plan and a law on energy efficiency in buildings, in line with Ukraine's commitments under the Association Agreement and the Energy Community Treaty	
Relevance and importance	As a high consumer of gas energy during winter, Ukraine has to diversify its energy mix in order to ensure its energy security – far from external influence. To do so, Ukraine is committed to achieving a target of 11% of final energy consumption from renewable sources by 2020. Energy Efficiency is one of Ukraine's commitments under the Association Agreement and the Energy Community Treaty.
Implementation	In June 2017, the draft law on metering and billing of heat water was voted by the Parliament. This draft law was prepared with the support of the European Commission[175]. In July 2017, the draft law was signed by the President. In November 2015, the Cabinet of Ministers adopted a national energy efficiency action plan for the period to 2020. In June 2017, the law on the energy efficiency of buildings was approved by the Parliament. This law was prepared with the assistance of the Energy Community Secretariat. The law establishes a new regulatory framework for energy efficiency that is in line with the EU legislation and foresees mandatory energy certification for buildings as from 1 July 2019. In July 2017, the law on the energy efficiency of buildings was signed by the President.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of	Since 2015 Ukraine has installed 4 000 MW of renewable-energy

175 DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

benefits and contribution of MFA	capacities, amounted 3,3 billion euros of investment and 103 completed projects in this sector[176]. In addition, it has been observed a substantial growth in the heat metering coverage for district heating-connected multi-apartment buildings in the past two years: the percentage of buildings equipped with a central heat meter increased from 48% in the end of 2015 to 78% as of 1 November 2017[177]. Also, the Eurostat data, showed that RE made up almost 8% of total energy mix of the country in 2018[178] - up from 4% in 2015.[179] Aside through the MFA, the reform in the energy efficiency sector was notably supported by a multi-donor trust fund (EUR 50 million grants in 2018), funded by EU, Germany, UNDP and IFC.

Table 25. Conditionality #14, 3rd tranche – Energy sector

Conditionality number 14 – Publish Ukraine's first Extractive Industries Transparency Initiative report.	
Relevance and importance	In 2018, the extractive sector was a major source of revenue, representing UAH 120 billion (EUR 3,6 billion) for the state budget in Ukraine and made up in 2016 almost 12% of job creation in the industrial sector (232 000 occupations), mainly located in the east of the country[180]. Thus, the enhancement of the governance and transparency in the extractive sector is a much-needed initiative in the overall governance and transparency reforms undertaken by the government, to ensure that natural resources benefit all.
Implementation	In December 2015, Ukraine published its first report under the Extractive Industries Transparency Initiative (EITI)[181] the second report was published still within the lifetime of the MFA, in February 2017. [182]

176 https://www.rferl.org/a/can-renewable-power-reenergize-ukraine-/30228294.html

177 DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

178 https://ec.europa.eu/eurostat/documents/3217494/10165279/KS-DK-19-001-EN-N.pdf/76651a29-b817-eed4-f9f2-92bf692e1ed9

179 https://www.researchgate.net/figure/The-structure-of-renewable-energy-sources-in-Ukraine-and-EU-28-in-2015-Source_fig1_328086741

180 https://eiti.org/ukraine

181 https://eiti.org/sites/default/files/migrated_files/uaeiti-2013-report-en.pdf)181.

Evidence of Implementation deficit	√ This condition has been considered as fully fulfilled by the EC. There is no implementation deficit. These reports cover the situation of Ukraine's extractive industry, its regulatory and fiscal oversight, as well as results of reconciliation of data on taxes and other payments to the state from extractive companies[183].
Evidence of benefits and contribution of MFA	Since then, Ukraine has published many reports in the following years: a final annual report in 2017[184] and In April 2017, a new draft law of Ukraine on disclosure of information in extractive industries was submitted to the Parliament and adopted on September 2018. A report on the law (Law 2545-VIII 'On ensuring transparency in extractive industries') was published in 2018. Preparation of EITI reports slowed in the last years. Fourth report covering 2017 was published in June 2020. Since July 2017, Ukraine has been undergoing the EITI validation assessment analysing Ukraine's performance towards the EITI global standard. The validation assessment report published in May 2018, triggered the decision from the EITI Board to validate the progresses made mainly on the legislative side (see adoption of a law on "Transparency in the Extractive Industries", and amendments to the laws on "State Registration of Legal Entities and Individual Entrepreneurs" and to the "Budget Code")[185].

A5.4 Social safety nets

Table 26. Conditionality #11, 2nd tranche – Social safety nets

Conditionality number 11 – With a view to protecting vulnerable households from the increase in energy tariffs, ensure that the compensation mechanisms are fully functional, taking into account the expected increase in the number of beneficiaries.	
Relevance and importance	Ukraine has been considered as one of the least energy-efficient countries in Europe[186]. The Ukrainian energy market has historically been heavily regulated and subsidised – holding energy tariffs below market levels. Traditionally, Ukraine has been one of the most energy-intensive economies in the world and, until recently, the average cost of gas supply in the country was one of the highest.

183 DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

184 https://eiti.org/sites/default/files/ documents/uaeiti_2014-2015_report_eng_final.pdf

185 https://eiti.org/files/documents/revised_board_paper_40-6-g_validation_of_ukraine_final.pdf

186 U.S. Energy Information Administration (2014) Comparison of International Energy Intensities across the G7 and other parts of Europe, including Ukraine. Available at https://www.eia.gov/workingpapers/pdf/international_energy_Intensity.pdf

	Contradictorily, residential gas and district heating tariffs were amongst the lowest in Europe. Energy provision to households at artificial low prices by quasi state-owned companies was generating a significant burden for the state. In 2013, average households paid just around 20% of the full import price of gas. However, the universality of the subsidy and different levels of energy consumption patterns across income deciles ended up benefitting mainly richer household consumers against more vulnerable households - only 13% of the implicit subsidies were used by the bottom quintile[187]. Further to a regressive structure, the energy model generated disincentives to enhance energy efficiency levels and eliminate waste. Additionally, the subsidy structure in place was extremely costly for public finances. In view of the above, reforms to the energy market in Ukraine considerably increased energy prices. The retail price of gas raised by 587% in 3 years - from UAH 1,089 in 2014 to UAH 6,958 in 2017. To counter this increase and protect vulnerable households, Ukraine introduced different subsidy schemes that aimed to better target subsidy beneficiaries. The most relevant were the Housing and Utility Subsidies (HUS) scheme and the Housing and Utilities Privileges (PRIV) scheme. The former (and larger) scheme sought to cushion the effects of tariff increases for households most affected by energy reform (the evolution of this policy is considered throughout the SIA). The latter was established to grant certain categories of the population (e.g. war veterans, people disabled during hostilities in the east, Chernobyl victims) a discount on their energy bills irrespective of their income.[188]
Implementation	An envelope of UAH 24.4 billion was allocated to the subsidies scheme in 2015. This includes UAH 19.9 billion allocated to the subsidies scheme (under which subsidies are inversely proportional to income) and around UAH 5 billion to the privileges programme, whereby certain categories of population (war veterans, people disabled during hostilities in the east, Chernobyl victims, etc.) are granted a discount on their energy bills irrespective of their income[189]. The 2016 budget initially assigned UAH 35 billion to the subsidies scheme and the privileges programme, but it had to be topped up in the course of the year to a total of UAH 47.1 billion. The same budget allocation (UAH 47.1 billion) was maintained for 2017. Information campaigns were launched to capture potential beneficiaries through national and local TV, radio, press, leaflets and announcements made in supermarkets.
Evidence of	√ This condition has been considered as broadly fulfilled by the EC.

[187] World Bank, ESMAP (2017), "Ukraine", (http://documents.worldbank.org/curated/en/884621506493335975/pdf/120076-26-9-2017-11-9-3-FINALESMAPCountryBriefUkraine.pdf).

[188]

[189] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

Implementation deficit	There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	By end-2016, almost 50% of households in Ukraine were benefitting from the subsidies scheme that compensated them for the energy tariff hikes introduced in 2014 and 2015. Around 7 million households were beneficiaries of this scheme, out of a total of 15 million households[190]. The Social impact analysis shows that increases in energy tariffs coincided with increases in the value of assessed subsidies. The growth in annual subsidies also considerably outstripped inflation over the period of MFA operations, implying a real increase in assessed subsidies of 173% per annum over 2014-17[191] Ukrainian authorities launched an information campaign aimed at potential beneficiaries to raise awareness about the schemes[192], including advertisements in national and local TV and radio programmes, the press, leaflets, and announcements made in supermarkets. The Ukrainian authorities also simplified the application process, in order to reduce access barriers for vulnerable groups. The application forms were shortened to one page and income/expense declarations were also simplified[193]. As application volumes increased (starting around autumn 2015), administrative capacity to manage these applications was also reportedly increased[194]. By the end of 2016, approximately 7 million households were benefitting from the subsidies scheme[195]. This conditionality required policy action to accommodate the increase in the number of beneficiaries and to ensure that compensation mechanisms were fully functional. However, it did not specify the efficiency with which vulnerable groups were targeted, but instead prioritised coverage in the first instance.

Table 27. Conditionality #15, 3rd tranche – Social safety nets

Conditionality number 15 – To cushion the effect of energy tariff increases, make substantial progress towards consolidating and better targeting relevant existing social assistance programmes, i.e. the privileged housing utilities programme, the means-

[190] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

[191] The corresponding nominal increase is 240%.

[192] European Commission (2017) "Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III".

[193] Muzychenko Vitalii (2018), "Reform of the program of housing and utilities subsidies in conditions of increase energy prices", [in association with the Ministry of Social Policy of Ukraine, World Bank and Social Protection and Jobs Learning Forum] (http://pubdocs.worldbank.org/en/721741520534548015/SSLF18-Economic-Shocks-Ukraine.pdf).

[194] European Commission (2017) "Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III".

[195] Ibid.

tested transfers for housing utilities and the tariff compensation scheme introduced in 2014.	
Relevance and importance	The third-tranche conditionalities maintained the requirement of compensating vulnerable households, but additionally specified the need for consolidation across social assistance programmes and better targeting. In light of significant increases of energy prices, the focus was on protecting and compensating vulnerable households via subsidy schemes, but these needed to be redesigned in most cases to ensure eligible beneficiaries were the right recipients of these subsidies. The fact that in 2013 only 13% of the implicit subsidies were used by the bottom quintile[196] indicates that subsidy schemes were far from well-targeted and needed to adjust and tighten eligible criteria.
Implementation	In order to cover the growing number of beneficiaries, the 2017 budget increased the resources allocation for the housing and utilities subsidies scheme in the course of the year. The initial envelope of UAH 47.1 billion approved in December 2016 raised to UAH 68.8 in the latest revision of the 2017 budget. [197] Households benefit from subsidised prices for a lower consumption volume and have to pay the market price for their consumption exceeding this volume as a result of i) the volume of gas consumption being subsidised was cut from 7 m3 per square meter in 2015 to 5.5 m3 per square meter in May 2016 and to 5 m3 per square meter in May 2017; ii) the reduction of consumption norms for centralised heating and for electricity used for individual heating (from 65 to 51 kWh per m2), which became effective in May 2017. The MoSP has reinforced controls and eligibility to the subsidies scheme is re-checked every year. This is mainly driven by the suspicious of consumers underestimating their income in their declarations in order to benefit from the subsidies scheme. These measures have led to a percentage of 6-7% of cases not being renewed. Additionally, the income taken into account to be eligible for the subsidised prices has changed and now it better reflects the salary increases that were effective in January 2017. As of May 2017, it is taken into consideration the past four quarters rather than the previous calendar year. Since 2016, benefits under the privileged housing utilities programme and under the subsidies scheme can no longer be cumulated. In this way, better targeting is also addressed via the phasing out of the system of privileges granted to certain categories of the population (veterans, combatants in the east, etc.), whose beneficiaries are gradually being transferred to the housing subsidies scheme. In May 2017, the monetisation of subsidies was implemented by the

[196] World Bank, ESMAP (2017), "Ukraine", (http://documents.worldbank.org/curated/en/884621506493335975/pdf/120076-26-9-2017-11-9-3-FINALESMAPCountryBriefUkraine.pdf).

[197] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

	MoSP with the aim to improve household incentives for energy efficiency. This allows that a household consuming less than its 5 m^3 per square meter can now be reimbursed in cash for the savings that it has realised (up to a ceiling of 100 m^3 of gas or 150 kWh of electricity)
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	In the years following the tighter measures, the number of households receiving subsidies and the average payment of housing and utility services decreased. In the period 2018-2019 period, over 4 million households received subsidies and the average payment was about UAH 1700[198]. By early 2020, the number of households receiving subsidies decreased to 2.8 million and the average payment decreased to UAH 1200[199]. The Ministry of Social Policy in Ukraine adjusted the benchmarks of the housing and utilities subsidies scheme to limit outlays, improved targeting and encourage energy efficiency. Specifically, this involved lowering the subsidised threshold for gas consumption from 7m3 gas per m2 floorspace to 5.5 m3 gas per m2 floorspace. Additional measures involved tightening controls to prevent applicants underreporting their income, and the gradual phasing out of energy privilege programs (including PRIV)[200]. The social impact analysis reveals that increases in non-cash subsidies for housing and utilities is unable to fully offset the increases to average household expenditure in this category. It does however succeed in cushioning the impact of increased expenditure. If non-cash support remained at 2015 levels from 2015 onwards (and assuming unchanged expenditure patterns), then the deficit between expenditure and state support would have peaked at UAH 86,000 by 2017 (compared to a deficit of UAH 64,000 which was observed). However, this analysis includes some limitations and does not provide any information regarding the targeting of the social safety net. In 2018, the procedure for the provision of housing subsidies was amended and changed the approach to calculating the income of able-bodied persons, encouraging them to formally work and pay a single social contribution, taking into account the property state and incomes of family members of persons living in the household, as well as simplifying the conditions for granting subsidies to internally displaced persons.

[198] Ministry of Social Policy (2020), *Interviews*.

[199] Ibid.

[200] Beneficiaries of energy privileges schemes are gradually being transferred to the housing and utilities subsidies scheme and (since 2016) benefits from the two schemes cannot be cumulated.

	Evidence from stakeholder interviews did not highlight any significant issues with this conditionality. However, it did include discussion of the need to articulate the rationale for greater targeting in a clear and effective way. The concern was felt that, if miscommunicated, ambitions to improve the targeting of utility subsidies could be misinterpreted as a part of a programme of austerity or public sector cuts. The government is studying measures to ensure that the subsidies scheme remains targeted to vulnerable households.

Table 28. Conditionality #12, 2nd tranche – Social safety nets

Conditionality number 12 – Ensure the effective provision of social benefits and services to internally displaced persons (IDPs) through adequate legislation and funding.beneficiaries.	
Relevance and importance	An assistance programme for persons that were forced to leave their homes as a result of the conflict in eastern Ukraine was launched by the Ukrainian government in November 2014 for an initial period of 6 months (Resolution No. 505). A few months later, at the time of the MFA III negotiations, it became clear that there was a need to extend that programme beyond the initial period and the MFA III leverage was used with that specific purpose in mind, to ensure that the programme would be renewed beyond its original timeframe.
Implementation	The programme was launched by the Ukrainian government in November 2014[201]. In April 2015, the duration of the programme was extended for another six-month period because of the prolongation of the conflict. In February 2016, the Ukrainian Ministry of Social Policy suspended social payments to around 500,000 IDPs (up to 600,000 according to UN estimates) in five eastern regions, pending verification of their status. As a result, approximately one third of the 1.75 million registered IDPs were deprived of social transfers, including pensions and IDP allowance. On 8 June 2016, the Ukrainian government adopted a resolution implementing procedures enabling IDPs concerned by the suspension to apply for the renewal of their IDP certificate and for the reinstatement of their social payments. The local social authorities are responsible for verifying those applications. In July 2016, the Ukrainian administration had only processed less than 9% of applications for the reinstatement of social benefits, with hundreds of thousands of people still lacking access to social benefits. Closer to the time of disbursement, notable progress had been

[201] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

	accomplished towards the resumption of social benefits to IDPs. By February 2017, 95.8% of applications received had been processed (of which 77% received a positive decision).
Evidence of Implementation deficit	❌This condition was not fulfilled, but in view of the tangible progress achieved on this issue (with the reinstatement process well on track) and of the satisfactory overall implementation by Ukraine of the MFA policy programme, the Commission deemed it justified to waive the full implementation of Condition 12 ahead of the disbursement of the second instalment.
Evidence of benefits and contribution of MFA	The condition was a useful reference incentivising the authorities to renew the programme in 2015, and above all to reinstate it once it had been suspended in 2016 following its suspension. It is reasonable to assume that the process of reinstatement may have taken more time without the MFA condition and in itself, this is already an achievement. The limitation is that a substantial share of applicants saw their applications rejected (13.5% of the submitted applications as per MoSP figures for January 2020, or 369,055 IDP applications). The rejection rate reflects a different understanding on the EU and on the Ukrainian side when it comes to the access to social payments (and pension) of those living in the NGCA. Since 2014, the Ukrainian legislation requires persons from NGCA to register as IDPs in the GCA in order to continue receiving their social payments (including their pensions). Many (among those who are not mobile and not able to leave the NGCA and travel to GCA) have been deprived of their rights as result – which was a first reason of concern for the EU/ UN. In addition, this policy distorted IDP statistics, as pensioners from the NGCAs, even if they were not internally displaced and did not intend to relocate to GCAs, had incentives to register as IDPs, if they wished to receive their pension. In that context, it is understood that many frequently crossed the contact line back and forth, to receive their social payments while maintaining their actual place of residence in the NGCA. At first the authorities, despite being aware of the situation, accepted it[202] but the suspension of payments and subsequent verification process suggest that the government, as from 2016, sought to more stringently restrict the access to pensions for persons who reside in non-government-controlled areas[203]. According to the EU and the UN, pension is a fundamental right protected by the Ukrainian Constitution and pension payments should not be dependent on obtaining the status of IDP (delinking). However, as long as this is not achieved, the EU and international partners like the CoE highlight the importance of stopping the inspections linked to the verification process and maintain those actually living in NGCA into the IDP programme[204]. The MFA condition was not designed to tackle the broader issue of the non-payment of pensions of those living in NGCA and in that sense it was

[202] United Nations (2019) Pensions for IDPs and persons living in the areas not controlled by the Government in the east of Ukraine, Briefing Note//February 2019

[203] UN (2019)," Pensions for IDPs and persons living in the areas not controlled by the Government in the east of Ukraine", (http://www.un.org.ua/images/documents/4719/Briefing%20Note%20on%20Pensions-eng.pdf).

[204] Council of Europe (2019) Enhancing the Legal Framework of Ukraine on Protecting the Human Rights of IDPs

	not fit for that purpose. Note that this MFA condition is subject to one case study (Annex 7) and some lessons learned from this condition are discussed in section 12.2 of the main report.

Table 29. Conditionality #16, 3rd tranche – Social safety nets

Conditionality number 16 – Prepare a first evaluation of social service delivery to IDPs and ensure effective follow-up.	
Relevance and importance	By the end of 2015, Ukraine transitioned from having no IDP population to having the world's eighth largest population of displaced persons, after Syria, Colombia, Iraq, Sudan, Yemen, Nigeria and South Sudan[205] without prior experience of dealing with the challenges of such an IDP crisis (Ukraine has had IDPs in relation to Chernobyl in the eighties but the magnitude and triggers of the crisis were different). The speed at which the crisis unfloded, and its scale, made it problematic to find an immediate and appropriate response. There was a need to acknowledge the crisis and better understand the problem be it for the Ukrainian government, the Ukrainian CSOs and the international donors which were already active in the country by that time. The independent evaluation promoted by MFA III was meant to fill the gap of comprehensive and neutral information at the time.
Implementation	In the first half of 2016, two independent experts undertook the evaluation of the policy steps taking by Ukraine towards the delivery of social services to internally displaced persons[206]. In July 2016, the results of the evaluation were presented. The evaluation report was published and is available on the website of the Ministry of Social Policy (http://www.msp.gov.ua/news/13403.html). On 15 August 2017, the Ukrainian authorities provided a detailed document describing the state of play with the implementation of the recommendations contained in the evaluation report.
Evidence of Implementation deficit	√ This condition has been considered as broadly fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	Condition #16 ahead of the third tranche consisted of preparing a first evaluation of social service delivery to IDPs and ensuring effective follow-up. The MFA condition on this was useful as not only the report was undertaken by two independent experts but also,

[205] "Database," Internal Displacement Monitoring Centre (IDMC), http://www.internal-displacement.org/database/.

[206] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

	following DG ECFIN's request, it was made available on the website of the Ministry of Social Policy[207] and shared with CSOs and international organisations like the UNHCR to help inform the delivery of their humanitarian response. The evaluation provided various recommendations, and follow-up actions have been subsequently reported by the Ministry of Social Policy. It is understood from ECFIN documentation as well as insights gathered from other stakeholders within the Commission that no major gap in the implementation of the recommendations have been identified. One recommendation was for instance the adoption of an IDP strategy. The 2018-2020 IDP strategy was adopted and an MFA IV condition followed up on its implementation by requesting the adoption of Action Plan (itself approved in November 2018). One exception to this rather positive assessment regarding the follow up on the recommendations formulated as part of the evaluation concerns the social benefits. More specifically, the evaluation had recommended to harmonise the requirements for IDPs and non-IDPs to access social payments. Yet, IDPs are still subject to additional verification requirements, which are onerous especially for those actually living in the NGCA. Last but not least, another area of impact stems from the fact that the report in itself was widely shared with CSOs and international organisations like the UNHCR. It has subsequently been used to inform the delivery of humanitarian response by donors in Ukraine, as reported consistently during stakeholder interviews.

A5.5 Business environment

Table 30. Conditionality #13, 2nd tranche – Business environment, Trade and Customs

Conditionality number 13 – Refrain from introducing new trade-restricting or trade-distorting measures, in line with Ukraine's WTO obligations	
Relevance and importance	According to the AA/ DCFTA, Ukraine should work towards an EU-Ukraine Free Trade Area and open its market for goods and services based on predictable and enforceable trade rules in an overall effort to improve business climate and promote investment and growth. The evaluation of MFA I & II reminded how, in the past, a lot of trade-distorting measures had typically been considered, taking the example of Ukraine's 2012 WTO renegotiation request. The choice of the condition was still timely in 2015 as the Ukrainian Parliament adopted the wood export ban on unprocessed wood in

[207] http://www.msp.gov.ua/news/13403.html

	April 2015, concomitantly with the adoption of the MFA decision by the European Parliament and the Council. Ex ante, this condition seemed to be relevant. With the benefit of hindsight though, given the issues which unfolded during its implementation, the use of this type of conditions may be not be recommended going forward (see also section 12.2 of the main report)
Implementation	✗The condition was not fulfilled, but in view of the tangible progress recently achieved by mid-2017 (with a submission of a law to the Parliament to resolve the issue) and considering the satisfactory overall implementation by Ukraine of the MFA policy programme, the Commission deemed it justified to waive the full implementation of Condition 13 ahead of the disbursement of the second instalment.
	This condition required the Ukrainian authorities not to introduce trade irritants. A major trade irritant has arisen in 2015 with the wood export ban (adopted by the Parliament in April 2015 and entered into force in November of the same year)[208]. Over the course of 2016, there has been concerns with another law, raising export duties on scrap metal but the final law was softened (duration limited to one year) and therefore considered acceptable. Aside this, no other major trade irritants have arisen over the lifetime of MFA III.
Evidence of Implementation deficit	There was implementation deficit. From the Commission point of view, the wood export ban was in breach of Ukraine's international trade commitments. Commission assessments did not buy in the arguments in favour of the wood ban indicated by the Ukrainian government, linked to (i) the need to address an environmental issue and prevent deforestation of the Carpathian Mountains and (ii) the ambition to export furniture, processed wood rather than raw wood with a view to protect / develop local industries. This was in light of Ukraine's limited efforts to attract investment into wood processing, put in place better forestry management schemes and fight against wood smuggling. Ukrainian authorities made repeated engagements to resolve the issue and also took concrete steps, which triggered the disbursement of the second tranche.

[208] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

	On 11 October 2016, a legislative proposal to amend the export ban was transmitted to the Commission. This had been developed by the Ministry for Economic Development and Trade and the Ministry of Agrarian Policy and Food[209]. On 6 February 2017, the draft law was registered in the Parliament after months of discussions between the Commission and Ukraine. Experts from the Commission services confirmed that the law would repeal the wood export ban and broadly remove the trade aggravation. The issue was escalated up to a point that Juncker and Porochencko were discussing this at the EU-UA summit in 2017. However, for years, the Parliament's Committee on economic policy was not making any progress (i.e. not considering the draft law). Finally, on 20 June 2019, in accordance with Article 306 of the Association Agreement between the European Union and Ukraine, the European Union initiated arbitration procedure on restrictions applied by Ukraine on exports of certain wood products. The arbitration panel to examine this matter was established on 28 January 2020[210]. The final decision could be taken within a year time.
Evidence of benefits and contribution of MFA	Despite being escalated at the political level, the issue of the wood export ban – of a relatively minor macro-economic importance - could not be solved over the lifetime of the MFAIII. MFAIII was one means to exert pressure in this domain. The pressure on this issue was however very negatively perceived in the Ukrainian civil society as illustrated in CSO reports[211], in the media[212] and discussions during the focus group held as part of this evaluation. Given the stalemate which has been reached regarding that particular issue, it has been chosen not to include trade-related conditions under MFAIV and rather tackle through a DCFTA dispute settlement. Overall, no other major trade irritants have arisen over the lifetime of the MFA – and the MFA may have reinforced the message on Ukraine's existing commitments in this regard. Broader reflections and lessons from the wood ban issue are drawn in section 12.2 of the main report.

[209] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

[210] https://trade.ec.europa.eu/doclib/press/index.cfm?id=2109

[211] http://www.enpi-fleg.org/news/ukrainian-timber-export-ban-to-be-or-not-to-be/

212 Note that this was also captured by the social media analysis conducted as part of the evaluation of the MFA I and II to Ukraine

Table 31. Conditionality #17, 3rd tranche – Business environment, Trade and Customs

Conditionality number 17 – In addition to refraining from introducing new trade-restricting or trade-distorting measures, in line with Ukraine's WTO obligations, let the import surcharges temporarily introduced for balance-of-payments purposes expire at the end of 2015, as planned.	
Relevance and importance	Ukraine policies should be aligned with the country's commitment to WTO as well as the AA and DCFTA principles. This condition follows up on Conditionality #13, 2nd tranche.
Implementation	The import surcharges introduced in 2015 for balance-of-payments purposes expired as agreed on 1 January 2016. The wood export ban was discussed in the table on condition #13, 2nd tranche.
Evidence of Implementation deficit	✗This condition could not be considered as fulfilled by the EC. There was no implementation deficit in relation to the import surcharges but the discussions around the wood export ban reached stalemate.
Evidence of benefits and contribution of MFA	The MFA condition may have helped to underline the importance of preventing any slippage with the removal of the import surcharges. For information on wood ban issue and contribution of MFA regarding other trade irritants, see table on condition #13, 2nd tranche.

Table 32. Conditionality #18, 3rd tranche – Business environment, Trade and Customs

Conditionality number 18 – With a view to facilitating cross-border trade: (i) take steps towards making the Authorised Economic Operator system EU-compatible; and (ii) advance the preparations to accede to the Common Transit Procedure Convention by adopting an action plan for implementing the Convention, in particular with regard to the New Computerised Transit System.	
Relevance and importance	In order to deepen its integration with the European internal market and to comply its commitments taken under the AA/DCFTA, Ukraine has to move towards EU compatible customs systems used within the internal market for homogenisation purposes and also to prevent the introduction of trade-distortion measures.
Implementation	In relation to (i): • In March 2016, the Ministry of Finance drafted two laws amending the Customs Code and the Tax Code concerning authorised economic operators. After positive feedback from

	DG TAXUD, these two draft laws were submitted to the Parliament on 3 June 2016[213]. • On 21 June 2017, the parliamentary Committee on Taxation and Customs policy returned the draft laws to the government for revision. • Following an exchange of views on the state of play with the draft laws between the Rada's Taxation and Customs Policy Committee, DG TAXUD and DG TRADE, the revised version of the draft laws were approved by the government. At the time of assessing compliance with the condition, these were pending to be signed by the President before their submission to the Parliament. In relation to (ii) • The Working Group for the accession of Ukraine to the Common Transit Procedure (CTP) Convention and the New Computerised Transit System (NCTS) adopted the Action Plan for joining the CTP and NCTS was adopted on 22 May 2015,
Evidence of Implementation deficit	√ This condition has been considered as broadly fulfilled by the EC. There is no implementation deficit. Key milestones were achieved in September 2019 when the Parliament adopted the Law on the Regime of Common Transit and the Law on Authorised Economic Operators[214]. Government approved detailed regulations implementing the laws in July 2020.
Evidence of benefits and contribution of MFA	The preparatory work was done under MFAIII and the key milestones achieved beyond its scope. Related conditions were included under MFAIV to facilitate this. Other EU programmes were also playing a key role in the advancement of reforms in this particular customs area (notably through the sectoral budget support programme in the area of PFM already at the time of MFA III, and the new EU4PFM technical assistance programme and its Customs Component launched in 2019). The longer term impacts in terms of trade facilitation will only be seen over the longer term – laws have only been recently adopted. Expectations are high that the impacts will be material.

Table 33. Conditionality #14, 2nd tranche – Business environment, Competition policy

Conditionality number 14 – Reinforce the efficiency of competition policy by: (i) reducing the room for discretion of the competition authority in terms of the time allocated to the collection of documents for a merger application; (ii) raising the thresholds above which notification of mergers is mandatory; and (iii) adopting and

[213] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

[214] EEAS (2019) Association implementation report

publishing a document explaining the principles to be used in the setting of any pecuniary sanctions imposed for infringements of the competition laws.	
Relevance and importance	As Ukraine moved from a planned to a market economy in the 90's, the Ukraine's Antimonopoly Committee (AMCU) acquired a key role in this transition in order to ensure a competition regime is aligned with international standards. However, the AMCU remains one of the most poorly funded government agencies in the country[215], which impacts on its mandate and independence. Despite that, the AMCU and its staff have still shown a strong commitment to raise the quality of the agency's performance and the efficiency of the country's competition policy[216]. Sub-conditions introduced within conditionality #14 aimed to address some weaknesses of the Ukrainian competition regime, by reducing the level of discretion of the AMCU whilst providing a higher degree of transparency and predictability to businesses and investors (e.g. introduction of guidelines on calculation of fines). Regarding mergers requiring the AMCU's approval, previous thresholds were established in Ukraine back in 2001, and these were considered to be extremely low when compared to neighbour countries[217]. Low thresholds imposed restrictions on a large number transactions, which in turn attributed greater powers to the AMCU. However, this constraint, among others, prevented Ukraine from attracting foreign investment and more specifically made business transactions like mergers more costly and time-consuming. Additionally, it also posed the risks of corruption for businesses and investors[218].
Implementation	On 26 January 2016, Draft law 2168a was adopted in final reading[219]. In March it was signed as Law 935-VIII Law 935-VIII raised the turnover and assets thresholds above which potential concentrations must be authorised by the Anti-Monopoly Committee of Ukraine (AMCU). Prior consultations and a simplified merger assessment procedure were also introduced following the adoption of Law 935-VIII. In July 2015, the AMCU published a draft document explaining the principles to be used in the setting of pecuniary sanctions and the calculation of the base amount of fines. Following suggestions by the Commission, the document was revised, and the final version was published on the AMCU website on 15 September 2015.
Evidence of Implementation	√ This condition has been considered as fulfilled by the EC. There was no evidence of implementation deficit.

[215] As an example of the AMCU's resource constraints, on average, staff earned less than USD 200 per month in 2016.

[216] OECD (2016) OECD Reviews of Competition Law and Policy: Ukraine

[217] Even ten times lower than thresholds in the nearest western neighbours of Ukraine.

[218] Deloitte (2015) «Monopoly» Game in Ukrainian: Key Tasks and Challenges of the New Antimonopoly Committee. Available at https://www2.deloitte.com/ua/en/pages/press-room/deloitte-press/-monopoly--game-in-ukrainian--key-tasks-and-challenges-of-the-ne.html

[219] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

deficit	
Evidence of benefits and contribution of MFA	i) Merger control procedures have been simplified, providing more transparency to the process and less discretion to the AMCU. Now, undertakings are able to conduct preliminary consultations with the AMCU. Additionally, the disclosure requirements for parties during the course of filing preparation have also been simplified, although they require now an economic analysis for transactions. Last but not least, a fast-track procedure for certain cases was also introduced, which allows decisions to be issued within 25 calendar days rather than 45 calendar days[220]. ii) Following Law 2168a, when jurisdictional thresholds are met, the transaction will require the AMCU's pre-merger clearance. Therefore, since May 2016, the AMCU requires to approve business transactions in the following cases: • the parties' combined worldwide turnover or assets exceeds the hryvnia equivalent of €30 million, and the domestic turnover or assets of either of the two parties exceeds the hryvnia equivalent of €4 million; • the target's domestic assets or turnover exceeds the hryvnia equivalent of €8 million, and the buyer's worldwide turnover exceeds the hryvnia equivalent of €150 million; or • in the case of the establishment of a business entity, the domestic assets or turnover of one of the parties exceeds the hryvnia equivalent of €8 million, and the worldwide turnover of the other party exceeds the hryvnia equivalent of €150 million. If a transaction is closed without notification, the AMCU will investigate the proceedings and may impose a fine as a result. According to the law, fines shall be up to 5% of the annual revenue for the previous financial year of the undertakings participating in the transaction. However, the calculation of fines is determined following the Guidelines on Fines[221] and in practice, they are normally below the 5% of the company's annual revenue. iii) The implementation of law 2168a enshrines into law the requirement for the AMCU to publish a methodology for the calculation of fines imposed on companies breaching competition

[220] Baker McKenzie (2019) Competition law implications of M&A transactions in Ukraine. Available at https://www.lexology.com/indepth/the-mergers-and-acquisitions-review/ukraine

[221] http://www.amc.gov.ua/amku/doccatalog/document?id=128682&schema=main

	rules[222]. In this sense, the publication of a number of guidelines, including the guideline on the calculation of fines, have raised the transparency of decisions, which now provide further guidance and predictability to the bar and the private sector[223]. In the view of DG COMP and MS experts, the Guideline represents a positive step towards increasing the transparency of Ukraine's competition policy and aligning it with international standards[224]. According to recent reports, Ukraine continues bringing its competition and state aid law closer to that of the EU, as foreseen by the AA/DFCTA[225]. In this sense, complete reforms in this area exemplify Ukraine's effort to make the country a more business friendly place, by harmonising the national competition law with that of the EU.

Table 34. Conditionality #19, 3rd tranche – Business environment, Justice sector

Conditionality number 19 – With a view to improving the enforceability of contracts and the business environment, implement the following measures under the National Justice Sector Reform Strategy 2015-2020: (i) implement the qualification and performance evaluation systems for judges foreseen in the law on fair trial; (ii) adopt a law establishing a more effective enforcement system for civil and administrative cases in line with European standards; and (iii) amend legislation on the judiciary in line with recommendations of the Venice Commission in order to increase the performance and efficiency of the judiciary.	
Relevance and importance	The reform of the judiciary has been acknowledged as a pressing issue for Ukraine. The general public trust in the judiciary in Ukraine remains dramatically low. As an illustration, 79% of population did not trust the judiciary in in 2015[226]. Furthermore, the principle of the respect for the rule of law features prominently in the Association Agreement and is indispensable for Ukraine to further associate politically with the EU. This condition, considered as relevant and important contains three subconditions. Subconditions i) and iii) are related to judiciary while

[222] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

[223] OECD (2016) OECD Reviews of Competition Law and Policy: Ukraine

[224] DG ECFIN (2016) Mission Report: MFA to Ukraine. Prospects for the second and third disbursements following ECFIN's mission to Kyiv (26-29 September 2016)

[225] Action Document for Technical Cooperation Facility 2020. Annex 3 of the Commission Implementing Decision on the financing of the Annual Action Programme, part 1, in favour of Ukraine for 2020 to be financed under the general budget of the Union. Available at https://ec.europa.eu/neighbourhood-enlargement/sites/near/files/annexes/c_2020_3294_f1_annex_en_v1_p1_1079334.pdf

[226] https://newjustice.org.ua/wp-content/uploads/2018/05/2015_FAIR_July_Public_Survey_Lustration__ENG.pdf

	ii) is related to the business environment. The relevance and importance of each subcondition is addressed in turn here. Sub condition (i): After Maidan, there was pressure from the general public to clean up the judiciary. At some point[227], there had a proposal to dismiss all sitting judges and make them reapply for their positions but the proposal was seen as too drastic, raising concerns about judicial independence and rule of law. Another process was put in place, a qualification assessment (with vetting) meant to check the judicial integrity and professional ethics and qualification of judges. It started in February 2016 and concerned all sitting judges. It was planned that the judges could be sent to retraining or face disciplinary measure if considered necessary at the end of the exercise. Sub condition (iii): Overhauling the legal system was seen by the CSOs as another key step to clean up the judiciary. At this point in time however, the Commission refrained from asking the needed constitutional reforms and required the law to be amended. It was seen as beyond the scope of an MFA to enter this field considering for instance that constitutional amendments typically require a two-third party majority (see also discussion under section 12.2 in the main report). Sub condition (ii): with the percentage of enforced court judgements reaching only 20%[228] (at best, other statistics mention 6%[229]) the system was notoriously inefficient and it was important to find better solutions to collect what was awarded by the courts . The profession of licensed private enforcement officers was introduced, alongside the state enforcement officers, to give the concerned parties an option to have their court decision enforced by either a state or a private enforcement officer (from those licensed to operate in a particular region). This mostly applies to civil and commercial disputes between private parties. The creation of this profession implied standard legal change.
Implementation	Sub condition (i): in line with the Venice Commission recommendations, the Supreme Qualification Commission of Judges developed a procedure and methodology for the assessment of qualification of judges. The methodology was adopted by the Council of Judges in November 2015 The process started in February 2016. From the 9000 judges, half of the judges were re-screened through this exercise Then the resources which had been reserved for this exercise were

[227] OECD (2017) Anti-corruption reforms in Ukraine 4 th round of monitoring of the Istanbul Anti-Corruption Action Plan. Available at : https://www.oecd.org/corruption/acn/OECD-ACN-4th-Round-Report-Ukraine-ENG.pdf

[228] https://www.lexology.com/library/detail.aspx?g=033cb484-9575-4713-9386-7421127c3ce4

[229] https://newjustice.org.ua/en/news/private-enforcement-officers-are-improving-enforcement-of-judgments-efficiency/

	diverted to issues related to the staffing of High Anti-Corruption Court and the new Supreme Court. Sub condition (iii): In June 2016, the Parliament also approved both relevant constitutional amendments and a Law on the Judicial System and the Status of Judges. The changes enhance judicial independence, including by abolishing the probationary period for judges, and by setting more objective recruitment procedures. The changes were assessed as generally compliant with the recommendations of the Venice Commission. Sub condition (ii) The June 2016 legislative package covered the enforcement of court decisions for civil and administrative cases, through the Law On Enforcement Proceedings and a new Law On Agencies and Persons Performing Compulsory Enforcement of Court Decisions and Decisions of Other Authorities. The laws are in line with European standards and introduce a new institute of a licensed private enforcement officers, having the same powers as those of the state enforcement officers (for certain types of cases).
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	Overall, there has been substantial progress over the last few years but challenges remain. Sub condition (i): the results of the process itself fell short of expectations. There is no comprehensive data set on the exact numbers but it seems that only few dismissals were proposed following the vetting exercise. For those few cases, the HCJ has not followed up on those few cases. The system had an ex ante announcement effect: 2,000 resigned to avoid going through the process, potentially opening positions for new legal professionals to enter the system. The new positions have however remained open in many cases, leaving the judiciary with acute staff level issues. Sub condition (iii): the 2016 package included both a constitutional reform and changes to the ordinary legislation. In that sense, it went beyond the MFA condition. Although reform of the judiciary is a long journey, the reform is considered as a major step forward which increases the independence of the judiciary, depoliticalize the process for the selection of judges and facilitates the dismissal of judges with tainted integrity. Sub condition (ii): the new laws brought about improvements,

	introducing the role of private enforcement officers who are authorized to enforce court decisions (with certain exceptions) alongside the state enforcement officers. Statistics on amount of debt collected by private enforcement officers indicate an amount of UAH 1.3 billion for the first half of 2019[230], for about 150 private enforcement officers. There are however challenges still ahead. The profession of private enforcement officers does not attract enough candidates – there are estimates than 4,000 of them would be needed[231]. According to the Deputy Head of the Council of Private Enforcement Officers of Ukraine, other challenges include "a need to equalize mandates of state and private enforcement officers, introduce electronic enforcement proceedings, create a unified database of all debtors, establish effective interaction with the National Police, and ensure transparency of procedures for access to the private enforcement officer profession and professional ongoing training programs". Today's shortcomings mean that there are still many applications pending before the European Court of Human Rights[232] in relation to Ukraine's "systemic problem of non-execution of national judgments"[233].
	Efforts in the justice domain are very much concerted as evidenced by the establishment Judicial Reform Council (JRC), uniting many actors at the highest policy-making level, donors and representative of the civil society (CSOs) in 2014, with an aim to act as a justice sector reform 'owner' and coordinate the implementation of the Justice Sector Reform Strategy 2015 – 2020 (JSRS)[234]. Under this coordinated pressure (notably from the civil society and the general public for whom cleaning up the judiciary was key after Maidan), the Ukrainian authorities implemented changes which went beyond the MFA conditions and included e.g. constitutional amendments and the set up of a new Supreme Court. The EU plays a big role notably through its technical assistance programmes (notably the PRAVO project and its predecessor projects). The PRAVO project is for instance supporting the JRC and the training of private enforcement officers. Overall, the MFA conditions reinforced the EU message which was central on the EU-UA political agenda.

Table 35. Conditionality #20, 3rd tranche – Business environment, Deregulation

Conditionality number 20 – In order to streamline administrative procedures for carrying out business activity in Ukraine, reduce the number of permits and simplify

[230] https://newjustice.org.ua/en/news/private-enforcement-officers-are-improving-enforcement-of-judgments-efficiency/

[231] https://www.pravojustice.eu/post/lack-private-enforcement-officers-ukraine-deputy-minister-explains-reasons

[232] https://echr.coe.int/Documents/Stats_pending_2017_BIL.pdf

[233] https://strasbourgobservers.com/2017/10/26/non-execution-of-a-pilot-judgment-ecthr-passes-the-buck-to-the-committee-of-ministers-in-burmych-and-others-v-ukraine/

[234] https://www.pravojustice.eu/what-we-do

	permit and licensing procedures on the basis of a thorough analysis of their costs to businesses and benefits to society.
Relevance and importance	The regulatory environment of Ukraine has been one of the biggest obstacles for businesses in the country, mainly in the shape of permits and licensing procedures. In the past few years, Ukraine has deployed significant efforts to liberalise the permitting system of economic activity. As for that, the country has reduced the list of permitting documents as well as the cost of permitting documents[235]. According to data collected by Doing Business in 2014, starting a business there required 6.0 procedures, took 21.0 days, costed 1.2% of income per capita and required paid-in minimum capital of 0.0% of income per capital[236].
Implementation	Ukrainian authorities adopted a number of legislative acts aiming to reduce the number of permits and simplified permit and licencing activity[237]. The Cabinet of Ministers has abolished a large number of regulatory acts, in particular in the areas of telecommunications and agriculture.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There was no major implementation deficit. The first steps towards these measures were implemented without the sufficient cost-benefit analysis that conditionality #20 required. As a consequence, the Cabinet of Ministers approved an updated methodology for the assessment of impacts of existing regulations that aimed to address this shortcoming[238].

[235] Checkh & Vinnyk (2017) Regulatory Environment of Business Activities in Ukraine. Innovative technologies and scientific solutions for industries. 2017. No. 1 (1)

[236] World Bank (2015) Doing Business 2015. Ukraine Economy Profile 2015. Going Beyond Efficiency. Available at http://documents1.worldbank.org/curated/en/420501468128422209/pdf/921520WP0Box3804580Ukraine00Public0.pdf

[237] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

[238] DG ECFIN (2016) Mission Report: MFA to Ukraine. Prospects for the second and third disbursements following ECFIN's mission to Kyiv (26-29 September 2016)

Evidence of benefits and contribution of MF	As a result of these deregulation efforts, the number of permits was reduced to 30 from 57 according to information provided by the State Regulatory Service[239]. The Better Regulation Delivery Office (http://en.brdo.com.ua) supported the reforms in the area of deregulation. Further to this, this body carries out impact assessment of the various permits and licencing procedures that are in place. As example of the simplification exercise that Ukraine undertook, the Parliament approved a bill in October 2019 on simplifying the conditions of licensing of economic activity, which included the unification of the amount of penalties for violation of licensing legislation and the improvement of appeal procedures . Overall, the simplification of permitting procedures has had a positive impact on the business environment and investment climate of Ukraine[240]. This is evidenced by the World Bank's Doing Business ranking. Ukraine is ranked 64 among 190 economies in the ease of doing business, improving from 87 in 2014 to 64 in 2019[241]. Compared to 2014 data, Ukraine improved from 21.0 to 6.5 days the time required to start a business. Likewise, costs to open a business diminished from 1.2% in 2014 to 0.5% of income per capita in 2019[242].

A5.6 Financial sector

Table 36. Conditionality #15, 2nd tranche – Financial sector

Conditionality number 15 – As part of ongoing efforts to limit related-party lending by banks and close remaining loopholes that may facilitate circumvention of the rules, the National Bank of Ukraine will adopt a regulation on the procedure of identifying individuals and legal entities as banks' related parties based on defined criteria.	
Relevance and importance	This condition aimed at solving one of the most pressing issues for the banking sector. During the pre-crisis years, Ukraine built on a high level of exposure to related party lending. With an extended presence of *pocket banks*[243], lending to insiders has been a common practice in Ukraine - developing a long-structural impediment. Given the legislative requirements which were in place however, third-party lending was neither properly identified nor restricted. This became

[239] DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

[240] Checkh & Vinnyk (2017) Regulatory Environment of Business Activities in Ukraine. Innovative technologies and scientific solutions for industries. 2017. No. 1 (1)

[241] World Bank (2015) (2020). Doing Business: Ukraine. 2015 and 202 Reports.

[242] World Bank (2015) Doing Business 2015. Ukraine Economy Profile 2015. Going Beyond Efficiency. Available at http://documents1.worldbank.org/curated/en/420501468128422209/pdf/921520WP0Box3804580Ukraine00Public0.pdf

[243] Def. *Pocket banks: Banking outfits that actually function as extended financial departments for oligarchic owners or their firms.*

	one of the main factors contributing to the concentration of risks in the banking system which was uncovered by the crisis in the country.[244] The problem was particularly affecting the corporate portfolios of private Ukrainian banks, meaning these banks were disproportionately lending businesses related to the banks' shareholders – at a level of profitability[245]. The NBU committed to addressing this problem and embarked on a diagnostics process on lending practices.
Implementation	In May 2015, Regulation 315 "On the Approval of the Regulation on the Procedure of Identifying Banks' Related Parties" was passed by the Board of the National Bank of Ukraine (NBU). This intended to address the high share of related-party lending in Ukraine by, among other measures, indicating the features that the regulator may use in identifying individuals and legal entities as banks' related parties[246]. In July 2015, the NBU approved a regulation on the establishment of a Verification Commission on related-party lending that should submit to the central bank proposals on how to unwind lending to related parties. It led to the review of about 50,000 loans. 22 banks were initially found to have violated related-party lending laws.
Evidence of Implementation deficit	√ This condition has been considered as fulfilled by the EC. There is no evidence of implementation deficit.
Evidence of benefits and contribution of MFA	Following the entry into force of the regulation no. 315 and the new criteria to define related-party247, Ukrainian banks were obliged to achieve a volume of RP loans which would not exceed 25% of their regulatory prudential capital by early 2019. The excess had to be unwound. Although there are still some banks (5) with portfolios exceeding the limit allowed, this should be solved in the coming months. Additionally, the NBU has been reporting on new potential related-party exposures on a monthly basis.248 It is suggested that today all banks in Ukraine are in line with EU regulation and that there is no longer a systematic risk.

[244] Barisitz & Lahnsteiner (2017) Ukraine's banking sector: still very weak, but some signs of improvement. Financial Stability Report, June 2017

[245] NBU (2018) Financial Stability Report

[246] DG ECFIN (2017) Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III. Note to the European Parliament and the Council

[247] Financier Worldwide (2015) Dealings with a bank's related parties in Ukraine – shake up in search of confidence. Available at https://www.financierworldwide.com/dealings-with-a-banks-related-parties-in-ukraine-shake-up-in-search-of-confidence#.Xpg7NchKiUk

[248] Kuznetsov – Obserwator finansowy (2016) Ukraine's banking sector is out of the woods, but significant challenges remain. Available at https://www.obserwatorfinansowy.pl/in-english/financial-markets/ukraines-banking-sector-is-out-of-the-woods-but-significant-challenges-remain/

Table 37. Conditionality #21, 3rd tranche – Financial sector

Conditionality number 21 – With a view to strengthening credit risk assessment by banks and lowering over the medium term the share of non-performing loans, the National Bank of Ukraine will establish a central credit registry.	
Relevance and importance	The creation of a public and unified credit registry has been truly significant to sustain financial stability in the country. It has improved Ukraine's credit information system, since now all banks are obliged to transfer data to the registry covering legal entities and individuals' credits. Before, banks had to rely on credit bureaus that received banks' information on borrowers on a voluntary basis. This generated high risks and high transaction costs, creating an inefficient banking system (e.g. rejections of good quality credit applications by banks)[249]. Additionally, the registry reinforces the supervision role of the NBU, by providing the national bank with information on the concentration of credit risks and related party lending[250]. Different international organisations had called for the set-up of such registry[251], as the centralisation of this data is key to monitor the financial sector stability and take preventive measures where needed[252]. Since the NBU credit registry makes publicly available more information on borrowers, this system is due to enhance banks' decision making and increase the effectiveness of the credit process as a whole[253].
Implementation	A draft bill on the establishment of a credit registry with the National Bank of Ukraine (NBU) was submitted to Parliament in 2015. However, this draft proposal was not considered for a vote by the Parliament[254]. In August 2017, a new draft bill authorising the NBU to create and manage a central credit registry was approved by the Cabinet of Ministers. On 16 November 2017, the draft law was adopted in first reading by the Parliament. Finally, on 4 March 2018, the Law of Ukraine On Amendments to Certain Laws of Ukraine on Establishing and Maintaining of the Credit Register of the National Bank of Ukraine and Improving Credit Risk Management of Banks came into effect.

249 OECD (2016), OECD Investment Policy Reviews: Ukraine 2016, OECD Publishing, Paris Available at https://doi.org/10.1787/9789264257368-en

250 Girault, Matias Gutierrez, and Jane Hwang (2010). "Public Credit Registries as a Tool for Bank Regulation and Supervision." Policy Research Working Paper 5489, World Bank, Washington, DC. Available at http://documents.worldbank.org/curated/en/934021468177872103/Public-credit-registries-as-a-tool-for-bank-regulation-and-supervision

251 World Bank and International Finance Corporation (2014) Ukraine – Opportunities and challenges for private sector development, Washington, Available at http://documents.worldbank.org/curated/en/449191468309835374/Opportunities-and-challenges-to-private-sector-development-in-Ukraine

252 World Bank Group (2019) Credit Reporting Knowledge Guide 2019. Available at http://documents.worldbank.org/curated/en/262691559115855583/pdf/Credit-Reporting-Knowledge-Guide-2019.pdf

253 Bielova & Savchenko (2016) Impact of Credit Information on the Banks Stability: Global Experience and Lessons for Ukraine. Risk governance & control: financial markets & institutions / Volume 6, Issue 2, Spring 2016

254 DG ECFIN (2018) Macro-Financial Assistance to Ukraine: Third Instalment Under MFA III. Note to the European Parliament and the Council

	In 2018, the Specifications of banks' submission to the NBU of a report on bank's lending transactions with individual and corporate borrowers and the maintenance of the NBU Credit Register was improved, so was the software application.
Evidence of Implementation deficit	✗This condition could not be considered as fulfilled by the EC within the timeframe of the MFA, given some delays with the implementation. √ It was fulfilled shortly after the expiry of the MFAIII. There has been delays – sorted out quickly afterwards the expiry of MFAIII, demonstrating NBU's ownership on this issue.
Evidence of benefits and contribution of MFA	Unlike condition #15 of the second instalment, this condition was imposed only by the MFA instrument – not included under IMF. The approval of this measure was subject to a strong opposition coming from local credit bureaus. Ukrainian credit bureaus base their business mainly on sharing information rather than on scoring. Therefore, their argument was that banks would not use their information services if they can access directly the registry. Since April 2018, all banks in Ukraine must submit information to the NBU Credit Register. Banks shall transfer information on their debtors if the total loan amount granted is equal to, or exceeds, 100 minimum wages (472,300 UAH - 16,082.98 EUR at present[255]). As of January 2019, the NBU Credit Register contained information on more than 80,000 borrowers – where 53,200 are individuals and 27,200 are legal entities[256]. Although the level of NPLs in the system remains high, this does not pose a risk to financial stability (the level of provisioning in the system is 87% as of January 2019)[257] Likewise, since January 2019 banks were obliged to consider the information contained in the NBU Credit Register when doing credit risk assessment. The purpose is to guarantee the resumption of lending by facilitating that loans are provided to honest borrowers. According to the NBU, the Credit Registry has proved to be a very good source of information to reduce the level of credit risks and raise the reliability and stability of the banking system. Although

[255]Minimum wage in Ukraine is 4,723 UAH (190 USD) since January 2020. Prior to that, minimum wage was 4,173 UAH - and 3,723 UAH in March 2018 https://112.international/finance/minimum-wage-in-ukraine-exceeds-figures-of-belarus-and-russia-47184.html

[256] NBU (2019) NBU Annual Report 2018 Available at https://bank.gov.ua/files/annual_report_en_2018.pdf

[257] IMF (2019) IMF Country Report No. 19/3 Ukraine. Request for Stand-by Arrangement and Cancellation of Arrangement under the Extended Fund Facility. January 2019

	there is more to do in the future, the NBU recognise their goals have been broadly achieved with this measure. It is in the NBU's plans to endow the Credit Register with a broader functionality in the future (e.g. adding nonbank financial institutions; expanding the data that are filed and made available)[258]. Additionally, it is also the NBU's ambition to reduce the debt limit that prompts the transfer of information to the Registry. The NBU argues that the current threshold should be lower so small loans can be also covered by the Registry. Note that the rule on the mandatory use of the Registry has been temporarily suspended due to the outbreak of Covid-19. A wave of restructuring is expected over the next 6 months. To avoid spiral effects (failure to do timely loan restructuring by one bank considered as a default in the Registry and leading to downgrades by other banks), the mandatory use of the Registry will not be re-activated until January 2021.

[258] MoF (2020) Strategy of Ukrainian Financial Sector Development until 2025. Available at https://mof.gov.ua/storage/files/Strategy_FS_2025_eng.pdf

Annex 6 Coherence tables

Table 38. High level comparison of MFA vs IMF and WB conditionality and EBRD support programmes

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
Public Finance Management									
Public procurement	✓ Broad terms: PP system in line with EU standards	✓ Annual PP plans	✓ Publication of award notices E-tendering		✓ Adopt a new PP law	✓ Adopt new PP law (reduction of exemptions in competitive procurements)	.	✓ Commitments to engage in TA projects, trainings, concertation in the area of PP	A priority for all, not much overlapping; the reforms are rather complementary Progression of reforms/ increase in specificity under the three MFAs
Internal / external audit	✓ Training and certification for staff in internal audit Increase the financial resources of the external audit	✓ Extend the remit of the powers of the ACU to do audits on SOEs	✓ Publication of the audit reports / follow-up notes of the ACU Allow the ACU to effectively do audits x number of audits of SOEs			✓ Extend the remit of the powers of ACU to state budget revenue	✓ Extend the mandate of the Accounting Chamber to cover external audits.		An EU and WB priority (IMF addresses PFM issues in relation to NBU and Naftogaz specifically) A key focus area for MFAs Progression of reforms/

Reform area	**MFA I**	**MFA II**	**MFA III**	**MFA IV**	**IMF SBA / EFF**	**WB DPL 1 and FSDPL 1**	**WB DPL 2 and FSDPL 2**	**EBRD**	**Comments / conclusions**
	Adoption of PIFC standards								increase in specificity under the three MFAs
Governance and transparency									
Public administration			✓ Strategy and implementation plan for public administration reform Legislation on de-politicisation of the civil service Open competition for recruitment of civil servant	.	✓ Preparation and implementation of revenue administration reform plan (2010 SBA) Public administration reform plan		✓ Introduce measures to increase transparency and efficiency of public investment allocation	✓ EBRD URA programme	New reform area for MFA III Links with the EBRD URA programme (partly finance by the EU) IMF focuses more on reform of administration linked to fiscal policy
Anti-corruption	✓ Broad terms: Implement anti-corruption legislation	✓ Broad terms: Implement anti-corruption legislation	✓ Set up of Anti-Corruption Bureau + Prosecution Office + National Agency	✓ Allocation of a financial envelope in the 2019 budget for the High Anti-Corruption Court and make it fully operational.	✓ Diagnostic study Set up and functioning of National Anti-Corruption Bureau (NABU) Legislatiamendments for more powers	✓ Anti-corruption dimension was strongly emphasised and incorporated in most of the FSDP 1 and DPL 1	✓ Create a centralised external verification function for financial disclosures of publicly elected and senior		Large degree of reinforcement between IFI conditions MFA I and II conditions formulated in broader terms

Reform area	**MFA I**	**MFA II**	**MFA III**	**MFA IV**	**IMF SBA / EFF**	**WB DPL 1 and FSDPL 1**	**WB DPL 2 and FSDPL 2**	**EBRD**	**Comments / conclusions**
			Specific conditions on asset disclosure / asset recovery	Adoption of an anti-money laundering law. Set up and operation of an automated verification system for electronic asset declarations. Ensure effective verification of information on companies' beneficial ownership	to NABU (New EFF): Prosecution function of NAB Amend AML law, Implement AML framework Specific conditions on asset disclosure	conditions Adopt new law to set up external verification of financial disclosures of public officials	public officials .		
State-owned enterprises (SOE)		✓ [see also audits of SOEs in PFM]	✓ Strengthen reporting obligations (conversion to joint stock companies) (+audits on SOEs) [see also audits of SOEs in PFM]	✓ Improvement of corporate governance in SOEs. Following the government's privatisation plan, put at least 200 small SOEs for sale via electronic	✓ Diagnosis, strategy, with aim to establish list of SOEs to keep as SO, privatise or liquidate. (New EFF): Adoption of action plan for the privatisation / restructuring of SOEs with largest fiscal risks			✓ Programmes with objective to promote privatisation and commercialisation in the public sector to increase competitiveness and	Addressed from the PFM perspective by the EU. IMF more involved in restructuring / privatisation

Reform area	**MFA I**	**MFA II**	**MFA III**	**MFA IV**	**IMF SBA / EFF**	**WB DPL 1 and FSDPL 1**	**WB DPL 2 and FSDPL 2**	**EBRD**	**Comments / conclusions**
				auction. Reduction of the high level of non-performing loans (NPLs), including in state-owned banks. Improvement of governance in state-owned banks.				foster good governance	
Fiscal governance / policy		✓ Draft national budget by X Data on budget execution	✓ Draft national budget by X Action plan to improve tax compliance Launch OECD peer review Broad condition TI and predictability fiscal policy		✓ Budget in line with new tax code Pass supplementary state budget Adopt supplementary state budget law and a package of tax and expenditure legislation	✓ Amend the law to improve public investment management framework (incl. Budget Code)	✓ Amend the Tax Code to improve transfer pricing legislation and reduce tax avoidance		

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
Business environment, trade and customs									
Trade	✓ WTO commitments Harmonised product coding system	✓ WTO commitments	✓ WTO commitments* EU-compatible Authorised Economic Operator system / Common Transit Procedure convention					✓ TA on approximation of EU standards	Compliance of WTO commitments is an EU concern only but repeatedly addressed via MFAs Not included under MFAIV (ongoing arbitration procedure)
Customs / tax	✓ VAT refunds incl introduction of penalties for arrears	✓ VAT refunds	✓ Reduced arrears incl VAT refunds	Issue of at least 7 general tax consultations on the practical application of tax legislation. Adopt a medium-term reform plan for the tax and customs administration with clear deliverables.	✓ VAT refunds (2010 SBA) Reversal of the general VAT rate reduction; revisions to sectoral VAT policy (e.g. agriculture) Merging of the customs and tax administration Other specific conditions	✓ Adopt law requiring publication of monthly data on VAT refunds/ revoke order of Ministry of Revenue and Duties that established targets for additional assessments and fines	✓ Extension of automatic VAT refund procedures and revision of automatic refund eligibility criteria guidelines.		VAT refunds is a recurring issue addressed by MFA / SBC and also one where domestic political commitment to reform was lacking IMF tackles the wider VAT reform needs (linked to fiscal policy)

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
				Better balance between customs control and trade facilitation. Fighting tax evasion.		Extension of automatic VAT refund procedures			
Competition			✓ Increase efficiency of competition policy e.g. by lowering discretion of competition authority					✓ Linked to fair treatment of business Detailed conditions on setting up and functioning of a Business Ombudsman Institution	An EU specific conditionality. EBRD and MFA III conditions can be seen as complementary
Deregulation			✓ Simplified permits and licences for businesses			✓ Adopt law that will ease the business and property registration/ reduce the number of permits	✓ Deregulation framework and harmonized standards and technical regulations and conformity assessments		

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
							with the EU requirements.		
Judiciary									
Judicial reform Constitutional reform Electoral reform			✓ Qualification and evaluation system of judges Law on effective enforcement system Amend legislation (Venice convention		✓ selective increase of court fees strengthening of the provisions in the Code of Civil Procedure on Order for Payment for domestic transactions and on garnishment of bank accounts				MFAIII and SBC address this from a wider perspective compared to IMF Not tackled by MFA I and II
NBU & Financial Sector									
Legislative and institutional reform	✓ IFRS Alignment to EU legislation	✓ Data on ownership of banks Draft law on financial services	✓ Draft law on financial services Central credit register		✓ Amendments to legislation re bank resolution Resolution strategy of problem banks Data on ownership of banks Legislation on liability of bank	✓ Entire focus of FSDPL 1 including reforms related to (i) bank recapitalization and restructuring, (ii) resolution and	✓ Strengthen the role of the Deposit Guarantee Fund (DGF) by (i) establishing a backup funding provision to DGF from government (ii)	✓ Policy dialogue	Key focus area for the IMF, Also pushed forward via MFA MFA: focused on improvement of laws, rules, standards

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
					owners on losses incurred Law on governance and autonomy of NBU (new EFF): strengthen insolvency and credit enforcement regimes, remove tax impediments Operationalise prosecutorial function of NAB Diagnostic studies on largest banks Recapitalisation of banks (by public funds under strict rules)	consolidation of the banking system i.e. norms and regulations on systemic banks, (iii) strengthening of Deposit Guarantee Fund	allowing DGF to speed up meeting its obligations to insured depositors and, (iii) increasing efficiency of DGF's asset management function. ✓ Resulting from a diagnostic process, undercapitalized banks (CAR<10%) are required to present credible recapitalization plans to complete the recapitalization process by end 2018. If not met, the bank will be transferred to the DGF for resolution.		IMF and EBRD: also on recapitalisation of viable banks. Ownership of banks: concern addressed under both MFA and IMF
National Bank of Ukraine		✓	✓		✓	✓		✓	Complementary reforms

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
reform		Norms and regulations on systemic banks	Rules to identify counterparties		Put in place internal control Governance and autonomy framework of the NBU	The formulation and implementation of a strategy for crisis management Governance framework for NBU including enhancement of management of DGF		Recapitalisation of viable banks Financing of corporates Provision of support / TA	promoted by the EU and IMF
Energy									
Naftogaz	✓ Increased collection rate / payment discipline	✓ Annual Financial report	✓ Targeted through the SOEs conditions		✓ Audit of Naftogaz Recapitalisation of Naftogaz			✓ Restructuring of Naftogaz	Complementary reforms aimed at increasing transparency and viability of Naftogaz
Compliance with EU / international obligations Legislative / market reform	✓ Broad condition: Implementation of obligations under Energy Community Treaty		✓ Strenghten independence of Regulatory Commission Amend Electricity market law	Make significant progress in implementing the electricity market law.	✓ Raising of households tariffs (already since 2008/10) Law on depolitisation of tariff settings (remit		✓ Strengthen the independence of the national regulation of the energy sector.	✓ Liberalisation legislation Independent regulator	Complementary reforms aimed at improving the functioning of gas and electricity markets as well as energy efficiency (MFA

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
			Adopt secondary legislation in line with Gas Market Law Gas sector reform implementation plan		of NURC) Law to improve payment discipline / improve Naftogaz collection rate (incl. lifting moratorium on enforcement proceedings for SOEs) New gaz market law		Adoption of the "Gas Sector Reform and Implementation Plan"		III) IFIs pushing for same issues e.g. MFA and EBRD on independent regulator, IMF and MFA on Gas market law (law itself and secondary legislation respectively)
Energy Efficiency			✓ Law on energy efficiency, Use of meters and control devices					✓ Implementing agency for the MDTF	New focus under MFAIII, consistent with EU contribution to MDTF managed by EBRD
Extractive Industries Transparency Initiative	✓ Reach candidate status		✓						
Social safety nets	✓ Compensation for increase in gas prices		✓ Compensation for increase in energy tariffs, higher targeting Effective	✓ Improvement of targeting, efficiency and fairness of social benefits.	✓ New Social assistance schemes for those not covered by existing schemes (New EFF) Reform	✓ Adoption of law and establishment of the system to compensate increase in gas and heating	✓ Remove provisions that allow the Borrower's Cabinet of Ministers to	✓ Policy dialogue on SSN related to energy	Both MFA I and III and IMF have conditions to improve social safety nets to counter the negative effects of tariff increases

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
			provision if social benefits and services to IDPs* Evaluation of social services for IDPs	Adoption of the Action Plan on the implementation of the strategy of integration of internally displaced persons.	utility-related social assistance (better targeting, within envelope)	bills of the poorest 30 percent of the population (very strong technical support of WB here)	develop a mechanism for setting utility tariffs below cost-recovery levels. Improve targeting of social assistance to the poor by introducing income testing of the housing and utilities subsides, reducing the amount of housing and utilities privilege benefits, among others.		SSN for IDPs was an EU only focus
Pensions					✓ (New EFF) Parliamentary passage of pension reform legislation,				
Health				✓ Implementation of the reform of healthcare financing.					

Reform area	MFA I	MFA II	MFA III	MFA IV	IMF SBA / EFF	WB DPL 1 and FSDPL 1	WB DPL 2 and FSDPL 2	EBRD	Comments / conclusions
Monetary policy					✓ Official exchange rate calculation				
Agriculture					✓ Submit law on agricultural land circulation to parliament		✓ Remove the possibility of counting land as bank capital.		

Source: ICF based on the EC, IMF, WB and EBRD documentation

Table 39. Technical assistance programmes

Reform area	Programme Start and End date	Total size of the programme EU contribution (UA envelope only for regional initiatives)	Focus and link to MFA condition	Condition number(s)
Anti-corruption	EU Anti-corruption Initiative in Ukraine 2017 - 2020	EU: €15 million	3 components: • 1- supporting the operational and policy-making capacities of the newly established Ukraine's anti-corruption institutions,	Condition 6 - 2nd tranche Condition 5 - 3rd tranche

Reform area	Programme Start and End date	Total size of the programme EU contribution (UA envelope only for regional initiatives)	Focus and link to MFA condition	Condition number(s)
			• 2- supporting the Parliament's Anti-corruption Committee, • 3- supporting local and regional civil society and media to contribute to the fight against corruption. Component 1 includes provision of IT solutions to ensure the integrity of the automatic verification process for asset declarations (eliminating options to manipulate results by hand)	
Anti-corruption and Governance	Anti-Corruption Initiative in Ukraine – Phase II 2020 - 2025	EU: €15 million	3 components: • 1- Further support to the institutional development of anti-corruption institutions, • 2- Improved governance, transparency and accountability at the local level • 3- Citizens, the civil society and the private sector empowered to promote integrity, the rule of law and good governance.	Condition 6 - 2nd tranche Condition 5 - 3rd tranche
Justice	PRAVO - JUSTICE 2017 - 2020	EU: €52.5 million	Its aim is to reform the justice sector in order to promote greater rule of law in Ukraine, in	Condition 19 - 3rd tranche

Reform area	Programme Start and End date	Total size of the programme EU contribution (UA envelope only for regional initiatives)	Focus and link to MFA condition	Condition number(s)
			line with European standards and comparative practices.	
PFM – Fiscal governance	EU4PFM – public expenditure component 2018 - 2020	EU: €6 million (Component 2) *EU4PFM EU total size: €50 million*	As part of Component 2: - Reinforce system of fiscal risks assessment, inter alia through the creation of a fiscal risk registry - analysis of fiscal risks. - Support in in legal, methodological and governance questions to further develop project management of public investment and public assets.	Condition 3 - 3rd tranche
PFM – Customs	EU4PFM – customs component 2018 - 2020	EU: €11 million (Component 3) *EU4PFM EU total size: €50 million*	As part of Component 3: - Support in the implementation of Customs reform strategy and Action Plan through, inter alia, (i) Harmonising Ukraine's Customs legislation with the EU Customs Code, (ii) Facilitating the accession to the Convention on a common transit procedure and implementation of New Computerized Transit System (NCTS), - Strengthen countering tax avoidance and	Condition 5 - 2nd tranche

Reform area	**Programme** **Start and End date**	**Total size of the programme** **EU contribution (UA envelope only for regional initiatives)**	**Focus and link to MFA condition**	**Condition number(s)**
			implementing customs trade facilitation measures	
PFM - External audit	EU4PFM – External audit 2018 - 2020	EU: €11 million (Component 3) *EU4PFM EU total size: €50 million*	As part of Component 3: - Strengthen capacities in external audit in line with international standards through, inter alia, establishing a third-party audit system in the Ministry of Finance - Implementation of IT systems development plan for PFM as regards, inter alia, budget process, expenditure controls, public procurement, internal control and external audit.	Condition 1 - 2nd tranche
PFM - PP	EU4PFM – PP 2018 - 2020	EU: €22 million (Component 4) *EU4PFM EU total size: €50 million*	As part of Component 4: - Support in procurement of IT equipment and IT solutions to support PFM reforms - Implementation of IT systems development plan for PFM as regards, inter alia, budget process, expenditure controls, public	Condition 2 - 2nd tranche

Reform area	Programme Start and End date	Total size of the programme EU contribution (UA envelope only for regional initiatives)	Focus and link to MFA condition	Condition number(s)
			procurement, internal control and external audit.	
Anti-corruption	EU4PFM – Anti-corruption 2018 - 2020	EU: €22 million (Component 4) *EU4PFM EU total size: €50 million*	As part of Component 4: - Design and implement integrity and anti-corruption policies across the PFM system institutions including full and independent vetting and re-appointment of staff.	Condition 6 - 2nd tranche
PAR	technical assistance to government agencies 2018 -	EU: €14 million	Amongst its objectives, PAR seeks to: - Strengthen policymaking by setting up policy-design functions and improving implementation capacity. - Promotion of open, merit-based and transparent recruitment - Reinforcement of political independence and competitive compensation	Conditions 6, 7 -2nd tranche Conditions 5, 8, 10 - 3rd tranche

Reform area	**Programme** **Start and End date**	**Total size of the programme** **EU contribution (UA envelope only for regional initiatives)**	**Focus and link to MFA condition**	**Condition number(s)**
PFM SOEs Energy Justice	joint support with European Bank for Reconstruction and Development (EBRD) for Ukrainian Reforms Architecture (URA) 2016 - 2020	EU: €27 million	Key reforms areas are, inter alia: - PAR and capacity building - Privatisation and SOEs - Deregulation - Public procurement - Tax reform - Energy policy and energy sector reform - Judicial reform	Condition 2, 2nd tranche Conditions 3, 5, 7, 8, 9, 10 - 2nd tranche Conditions 2, 8, 11, 12, 13, 14, 19, 20 - 3rd tranche
Energy efficiency	E5P 2014 -	EU: €40 million	The fund supports municipal sector projects, policy dialogue and regulatory reform in the energy efficiency area. This includes, among others, district heating, EE in public buildings, renewable energy, street lighting or urban transport.	Condition 14 - 3rd tranche
Energy efficiency	MDTF - EE4U 2018 - 2023	EU: €50 million	Objective is to support households in implementing EE investments in their homes. 3 components: • 1- EU contribution to MDTF supporting the Ukrainian Energy Efficiency Fund	Condition 14 - 3rd tranche

Reform area	Programme Start and End date	Total size of the programme EU contribution (UA envelope only for regional initiatives)	Focus and link to MFA condition	Condition number(s)
			(EEF), • 2- Setting up of a "technical office" to support the EEF, providing technical assistance and raising awareness, 3- Support to Reform and Policy Dialogue, providing technical assistance in the area of EE, RES, district housing and utilities subsidies.	

Sources:

AC: EU Anti-Corruption Initiative, 'What we do", https://euaci.eu/

E5P: https://ukraine.e5p.eu/about/

EE: ANNEX 1 of the Commission Implementing Decision on the Special Measure 2017 II for Ukraine https://ec.europa.eu/transparency/regdoc/rep/3/2017/EN/C-2017-7515-F1-EN-ANNEX-1-PART-1.PDF

PFM: ANNEX 2 of the Commission Implementing Decision on the Special Measure 2017 II for Ukraine https://eeas.europa.eu/delegations/brazil/37372/eu-set-provide-eur-55-mn-support-public-finance-management-reform-ukraine-2018-20-eu4pfm_en

PAR https://www.ebrd.com/documents/comms-and-bis/building-a-capable-state.pdf?blobnocache=true

PRAVO - JUSTICE https://www.pravojustice.eu/

Annex 7 Case Study: MFA III induced anti-corruption reforms

A7.1 Introduction

This case study provides an overview of the anti-corruption measures promoted as part of the conditionality under the MFA III to Ukraine related to the establishment of NABU, NAPC and SAPO, and the set-up of electronic asset verification system – two critical reforms among four anti-corruption measures that were incorporated into this operation. The Box 12.1 displays the exact content of these conditions, as per Memorandum of Understanding[259].

Full text of the two key MFA III conditions related to anti-corruption

Condition 6 (second tranche)

Establish a National Anti-Corruption Bureau in Ukraine (NABU), a Specialised Anti-Corruption Prosecution Office (SAPO) and a National Agency for the Prevention of Corruption (NAPC), ensuring that they are independent and operational, i.e. endowed with the financial resources, staff and equipment required to perform their functions.

Condition 5 (third tranche)

Set up an electronic asset disclosure system for public officials, including a verification mechanism, while starting to verify assets and possible conflicts of interest on the basis of the paper-based asset declarations submitted by officials in 2015.

The case study drew on the evidence gathered from the desk research including publications produced by national stakeholders, international donors like IMF, WB and UNDP, DG ECFIN mission reports, a review of available data on key performance indicators from both conditions, as well as review of documentation produced by some key national NGOs (e.g. Transparency International Ukraine) and selected articles from national and international press concentrating on the corruption in Ukraine. In addition, information collected via a number of interviews also fed into the case study. Some conducted as part of the Evaluation of the MFA III to Ukraine covering wider range of topics (including anti-corruption), and some with the explicit objective to contribute to this case study (the interview with the expert in anti-corruption measures from the EU Delegation in Kyiv).

Annex 1 provides the full reference list of reviewed documentation.

A7.2 Corruption in Ukraine

Weak institutions, low morale and an underdeveloped sense of public service have made many public officials liable to corruption over Ukraine's entire post-soviet era, and not much improvement took place under former President Viktor Yanukovich rules. In 2013, Transparency International ranked Ukraine 144 out of 180 countries in terms of level of corruption, with Corruption Perception Index of 25 on a scale from 0 (highly corrupt) to 100 (very clean). According to this index, Ukraine was the most corrupted country in Europe[260].

Endemic political corruption was a main trigger of the Maidan protests and population expectations to tackle it in early 2014 were exceptionally high. However, despite some progress, the Ukrainian revolution did not curtail it significantly and the corruption at virtually all levels[261] has remained of an endemic character. Widespread influence of the

[259] European Commission, 2015. Memorandum of Understanding between European Union and Ukraine (MFA III). Available at: https://ec.europa.eu/economy_finance/international/neighbourhood_policy/doc/mou_eu_ukraine_en.pdf

[260] Transparency International, 2013. CPI. Available at: https://www.transparency.org/cpi2013/results

[261] Financial Times, March 18th 2018. A multidimensional approach to corruption in Ukraine. Available at: https://www.ft.com/content/13bfac52-25ec-11e8-b27e-cc62a39d57a0

vested interest reaching the top echelon of the power in Ukraine (including the Parliament), powerful oligarchs, and inaction of the state apparatus (e.g. Ukrainian Prosecutor General and courts) in convincing fight against the corruption still positions that issue at the top of the policy agenda. Some argued that Ukraine has been fighting two wars: one near its eastern border where it faces Russian aggression, and the other at its core where it has been wresting with the worst corruption of any post-Soviet states[262].

A national public opinion survey of residents of Ukraine conducted between April 21st and May 5th 2017 by the International Republication Institute with support from the government of Canada revealed that the three most important issues for Ukraine are war with Russia, government corruption and low industrial production. Furthermore, according to European Business Association and Dragon Capital's survey of private business from Spring 2017, the widespread corruption was the most important obstacle to foreign investment in Ukraine (8.5 on the 1-10 scale where 10 most important)[263]. The more recent Gallup World Pool conducted in early 2019 revealed that 91 per cent of Ukrainians believe that the corruption in widespread in government, the lowest confidence in the world[264].

The IMF pointed to the *macro-economic* implications of the widespread corruption[265] while the World Bank argues that the corruption is a threat to national security[266].

In this context, the establishment of the new institutional architecture with NABU, NAPC and SAPO, and the set-up of the electronic asset disclosure system for public officials were two landmark anti-corruption reforms that followed Maidan.

A7.3 The rationale for the new anti-corruption institutional architecture and the electronic assets disclosure system

A7.3.1 NABU, NAPC and SAPO

Prior to Maidan events, Ukraine did not have dedicated institutions to fight the corruption. Set-up of a new institutional architecture was therefore a major undertaking and a breakthrough in a systemic approach to tackle this phenomenon in the country, and responded to the extraordinary demands of the general public and civil society. Eventually, a conceptual approach to split the competences and establish three branches of the anti-corruption architecture prevailed. At early stage of the democratic transition of Ukraine, the willingness to reduce the risk of the 'hostile' take-over of one central anti-corruption body that would concentrate most powers by a current political elite or/and vested interests was the key concern and rational for the split of competences and the choice of NABU, NACP and SAPO (rather than one central anti-corruption body). This approach was broadly consistent with the

262 The Economist, May 25th 2017. Ukraine is struggling with corruption, sometimes successfully. Available at: https://www.economist.com/europe/2017/05/25/ukraine-is-struggling-with-corruption-sometimes-successfully

263 EBA, 2017. Foreign Investor Survey – 2017. Available at: http://eba.com.ua/static/2017_09_13_InvestorSurveyResults_16_9.pdf

264 Gallup, 2019. World-Low 9% of Ukrainians confident in government. Available at: https://news.gallup.com/poll/247976/world-low-ukrainians-confident-government.aspx

265 IMF, 2014. Government of Ukraine Report on Diagnostic Study of Governance Issues Pertaining to Corruption, the Business Climate and the Effectiveness of the Judiciary Available at: https://www.imf.org/external/pubs/ft/scr/2014/cr14263-a.pdf

266 World Bank, 2016. Asset Declarations: A Threat to Privacy or A Powerful Anti-Corruption Tool. Available at: https://www.worldbank.org/en/news/opinion/2016/09/26/asset-declarations-a-threat-to-privacy-or-a-powerful-anti-corruption-tool

international guidelines (e.g. UN Convention against Corruption[267]) and some best practices like those promoted by European Partners against the Corruption (EPAC) network[268].

In terms of the key responsibilities, the NAPC monitors the process of asset declaration by civil servants, and ensures they are resistant to corruption risks. The NABU investigates high-level corruption and big bribery cases. Finally, the SAPO oversees NABU investigations and represents the state prosecution in court against those charged with top corruption or bribery.[269]

A7.3.2 Electronic asset disclosure system for public officials

The e-declaration system aimed at helping to prevent corruption (widely recognized as one of Ukraine's biggest problems), to avoid conflicts of interest and to enable citizens to inspect online public officials' earnings and assets. The system also meant to make it easier for Ukraine's new anti-corruption bodies to unearth graft and expose corruption[270].

By the time when Ukraine set up the system, more than 150 countries had introduced the asset disclosure requirements for the public officials[271].

A7.4 Implementation of the conditions

A7.4.1 NABU, NAPC and SAPO

Establishment of NABU was discussed by the Ukrainian authorities and donors already back in 2014 in the aftermath of the "Revolution of Dignity". The IMF report[272] that was part of the diagnostics work feeding into the design of the IMF SBA (2014) conditionality focused on the corruption in Ukraine and outlined some possible measures to tackle it proposing, *inter alia*, the establishment of NABU. The NABU was eventually created on April 16th, 2015 (Decree 217/2015). Its Head (Artem Sytnyk) was elected in the result of transparent and competitive selection and appointed by the President of Ukraine on April 16th, 2015 (Decree 218/2015). The appointments of the Deputy-Heads of the NABU followed. In summer 2015, some 30 administrative staff of the NABU as well as 70 investigators have been recruited, bringing the overall staff to about 100. The figure that was subsequently increased to 518 by September 2016 (including 201 detectives). The official investigations meant to start in Autumn 2015, albeit NABU's operations were conditional on the establishment of the SAPO. The latter, due to the politicisation of the selection of its members (and concerns relating to potential influence of the General Prosecutor), had a delayed start and became operational only in 2016[273]. Generally, NABU has

[267] United Nations, 2004. UN Convention against Corruption. Available at: https://www.unodc.org/documents/treaties/UNCAC/Publications/Convention/08-50026_E.pdf

[268] EPAC, 2020. About. Available at: http://www.epac-eacn.org/about/epac

[269] https://www.atlanticcouncil.org/blogs/ukrainealert/why-ukraine-s-anti-corruption-drive-is-failing/

[270] UNDP, 2018. Electronic asset declarations for Public Officials. Available at: https://www.ua.undp.org/content/ukraine/en/home/blog/2018/the-expectations-and-reality-of-e-declarations.html

[271] World Bank, 2016. Asset Declarations: A Threat to Privacy or A Powerful Anti-Corruption Tool. Available at: https://www.worldbank.org/en/news/opinion/2016/09/26/asset-declarations-a-threat-to-privacy-or-a-powerful-anti-corruption-tool

[272] IMF, 2014. Government of Ukraine Report on Diagnostic Study of Governance Issues Pertaining to Corruption, the Business Climate and the Effectiveness of the Judiciary Available at: https://www.imf.org/external/pubs/ft/scr/2014/cr14263-a.pdf

[273] DG ECFIN, March 2017. Mission statement.

been seen as broadly independent and generally a success story, even if it still did not avoid some controversies[274].

Provisioning of the adequate financial resources to all three bodies to ensure their effectiveness was crucial. According to the Law of Ukraine "On the State Budget of Ukraine for 2016" (with amendments) the expenditures for the NABU were redoubled compared to 2015 (EUR 8.1 mln) and amounted to EUR 16.1 mln in 2016. Subsequently, the budget of the agency was increased to EUR 25 mln in 2017. Donors insistence in rising the argument about appropriately high level of renumeration for the agencies' staff was also important.

Overall, there were no major issues in ensuring adequate resources for the three institutions and lower allocations at the initial period reflected lower level of staffing at their roll-out phase.

Regarding the establishment of NAPC, this started in May 2015 with the selection of the members of the selection committee, half of which (four) were to be elected by and from civil society. The first election of the civil society members took place on 17th May 2015 but the process was marred with allegations of manipulation by the government. Following intense lobbying by civil society and the EU, the government agreed to repeat the process and new elections took place on 28th August 2015. As a result, the new selection committee, composed in a fair and transparent manner, enjoyed the support of civil society. Interviews of candidates took place on 28th September and 5th October 2015, but then then process was yet again obstructed. In late March 2016, the inauguration meeting of the NAPC was held. During this event NAPC Board has elected Head (Nataliya Korchak) and Deputy Head (Ruslan Radetskiy)[275].

In August 2016, NAPC officially announced the launch of its work as a public authority in all areas of anti-corruption activities. Yet, as of early August 2016, only about 25 percent of the NAPC Staff were already appointed. As of end-December 2016, 213 staff members had been recruited (out of 311 staff members envisaged), while the fifth NAPC Board member remained to be still appointed.

The funds for the NAPC's activities assigned in the annual State Budgets were EUR 3.7 mln and EUR 3.5 mln in 2015 and 2016 respectively. This envelope was increased to EUR 5.5 mln in 2017. Like in case of NABU, the institution was provided adequate resources[276].

However, according to the Transparency International '…*NAPC lacked political independence and credibility and it has yet to make a notable progress or bring about any significant investigations'*[277]. More generally, there is a broad consensus that NAPC has been a subject of significant and frequent political interferences. Whistle-blowers, including some from the former NAPC leadership, have reported some cases highlighting the agency's corruption and abuses of power[278].

Finally, on 2nd July 2015 the amendments to the Law "On Prosecutor's Office" have determined the procedure on creating the SAPO. As a result, the Prosecutor's General Office (PGO) established an independent structural division within the PGO – called

[274] some media reports casting some doubts on the role of the NABU in the high profile embezzlement case in the army carried out in 2019. See for instance: Reuters, 2019. Ukraine's Anti-Graft Agency Accused of Concealing Military Fraud. Available at: https://www.bloomberg.com/news/articles/2019-03-12/ukraine-s-anti-graft-agency-accused-of-concealing-military-fraud

[275] DG ECFIN, March 2017. Mission statement.

[276] DG ECFIN, August 2016. Mission statement.

[277] Transparency International, 2019. Corruption high on the agenda as Ukrainians go to the pools. Available at: https://voices.transparency.org/corruption-high-on-agenda-as-ukraine-goes-to-polls-57a7ed6001c9

[278] Atlantic Council, 2018. Why Ukraine's Major Achievement in Government Transparency May Fail. Available at: https://www.atlanticcouncil.org/blogs/ukrainealert/why-ukraine-s-major-achievement-in-government-transparency-may-fail/

SAPO. The selection procedure, however, was a lengthy process and was *de facto* completed only in mid-2016. As of mid-2016, the organisation consisted of 24 prosecutors and its budget was ~EUR 2.4 mln.

Overall, the interviews with the key stakeholders including WB, IMF and the EU Delegation experts revealed that adequate selection procedures for all three bodies were of utmost importance and defined their subsequent propensity to be influenced by the vested interests/ political elite. In hindsight, they have also stated that some could have been organised differently. While initial euphoria following the Maidan events and relatively weak resistance of the vested interests allowed to choose the independent management of NABU, the task of staffing NAPC and SAPO was facing more obstruction and was less successful.

All three institutions were provided adequate financial resources to support their operations, not an obvious achievement given some well-documented practices of undermining the role of controlling institutions by the government by curtailing their funding – a quibble that was not infrequent in course of the transitional periods of several countries in the region, including Ukraine.

A7.4.2 Electronic asset disclosure system for public officials

Initially, there was a material difference in views between the EC and the IMF regarding the scope of the system. The IMF argued that the number of declarants should be fairly limited at the outset (e.g. 3,000 declarations as per discussions in May 2017) and focused mostly on the top officials. The Fund was also keen to concentrate the core responsibilities for managing the system at NABU, rather than splitting it between NABU and NAPC. The EC in turn was of a view that the simple establishment of the system should be a priority first, and then further adjustment could be made. It also argued that the donor community should not actively argue for restricting it (even though it acknowledged that imposing this obligation on over 1 million public servants could be excessive), as this would most probably require legislative changes which would entail a risk that interested groups attempt to get exempted from the obligation to declare their assets[279].

Also, in the EU's view, a more effective way to ensure that declarations are effectively examined and, where needed, followed by a legal procedure, would be to establish a verification mechanism with clear criteria targeting the declarations to be checked as a priority. Furthermore, the EC argued that this would achieve the same purpose as the measure advocated by the IMF, without requiring any legislative change. That said, restricting the number of people subject to the asset declaration obligations, as supported by the IMF, was not in direct contradiction to the condition.

After some delays, the electronic asset declaration system introduced by the Corruption Prevention Law (2014) was launched on 1st September 2016 covering broad typology of public officials. By mid-2017 there was no mechanism in place to ensure the efficient verification of the submitted asset declarations though.

As of mid-2017, the National Agency for the Prevention of Corruption (NAPC) was still far from performing its functions related to the verification of electronic asset declarations of which hundreds of thousands have been submitted by public officials since September 2016. According to DG ECFIN mission from May 2017: '*…inefficient management and divergences among NAPC Board members, combined with poor cooperation with other institutions involved in the fight against corruption (including the Ministry of Justice and the National Anti-corruption Bureau of Ukraine, NABU) can largely explain the institution's lack of progress with verification*'. For instance, the NAPC needed to obtain access to 16 databases/ state registers from the relevant official bodies (notably the Ministry of Justice and State Fiscal Service) to be able to cross-check the information submitted by declarants.

[279] DG ECFIN, March 2017. Mission statement.

In addition, NAPC needed to deploy software that would enable it to verify asset declarations in a systematic way according to pre-defined criteria, rather than only manually, case by case. A first version of such an automatic verification system was designed by UNDP and proposed to NAPC in August 2016, but the NAPC did not introduce the software (on the grounds of alleged IT security concerns), neither it launched successful tenders for other potential providers (all tenders included discriminatory requirements limiting the range of potential participants and preventing reputable international auditors from participating[280].

Other issues that became problematic at one point or another included, inter alia, completeness of the submitted declaration and the requirement for family members of officials to file a declaration, or the requirement that anti-corruption activists declare their private assets via the online system in the same way that public officials do.

By May 2017, over 1.2 mln declarations were submitted but only 25 asset declarations were duly verified by the NAPC. The system of automated verification was operational in January 2019, though full interoperability between the 16 specific state registers, the malfunctioning and technical problems occasionally experienced by the e-declaration system and allegations of unlawful interference still remain an issue to some extent (even though NAPC eventually gained an access all 16 state registers). There were also worrying signs of the interference of vested interest e.g. proposal to include NGOs as eligible parties for the disclosure[281].

In terms of the ownership for this reform, while Ukrainian authorities tended to point out to the IT related challenges in its implementation, the donors were of a view that the lack of political will was a key impediment for the progress of this reform.

A7.5 Impact of the conditions

A7.5.1 NABU, NAPC and SAPO

Reforms initiated in 2014 resulted in the creation of the new dedicated institutional architecture focused on the fight against the corruption with three separated branches: NABU, NAPC and SAPO. Despite the number of weaknesses of those institutions, including valid concerns about their independence, this was a remarkable achievement on its own considering the scale of these reforms, relatively short time, and the situation prior to the Maidan events.

At the operational level, in 2017 the SAPO and NABU forwarded to courts first corruption-related cases where the suspects were high-ranking officials, action that gave the country a slight uplift it the Transparency Corruption Index[282].

By March 2019 NABU investigated a total of over 1,000 cases[283]. These were at various stages:

- 692 investigations ongoing at the initial stage
- 149 cases of suspicion
- 314 accusations submitted to prosecution
- 189 in court
- 27 court convictions

- To the knowledge of the study team, however, three years since the establishment of NABU there was still no single court ruling leading to the prison sentence of a corrupted official.

[280] Financial Times, March 2017. Ukraine amends disclosure law. Available at: https://www.ft.com/content/a4144300-13c1-11e7-80f4-13e067d5072c

[281] Ibidem

[282] Council of Europe, 2018. Ukraine most corrupt country in Europe after Russia.

[283] Of these over 1,000 cases, 65 were based on illicit enrichment, either partly (among other offences) or exclusively. Out of the 65 cases involving illicit enrichment, 3 had reached the courts

Nonetheless, in the grand scheme of things, the MFA III conditionality in its literate sense was fully met. While there were major delays in setting up the institutions and independence of the NAPC and SAPO have been questioned, a new architecture emerged, just over two years since the dramatic events of Maidan.

A7.5.2 Electronic asset disclosure system for public officials

Annex 2 outlines the key statistics, including the numbers on the declarations submitted/ verified and follow-up cases in courts.

Overall, despite the delays in the set-up, numerous attempts to obstruct its effectiveness by vested interests and some politicians, and persisting deficiencies of the system itself, its establishment was a symbolic moment and major breakthrough in further strengthening of the anti-corruption infrastructure in Ukraine. The set-up has been of a paramount importance towards Ukraine's broader drive towards reforming its post-Soviet legacy. It was also widely recognised at the international stage[284].

Although the verification process and the enforcement still require an improvement, the anti-corruption agencies, law enforcement bodies, journalists, civil society and citizens themselves have now access to over 1 million declarations per year. In addition, the verifications may become a key source of evidence for the High Anti-Corruption Court that has been so strongly supported by civil society and donors and may soon start its proceedings. Besides, the donors agree that despite of its weaknesses, and apart from increasing the transparency, another benefit of the system has been also its role 'as a deterrent' for some officials who may contemplate the graft.

A GfK/UNDP survey conducted in 2017 has revealed that an overwhelming majority of Ukrainians (72 per cent) have positive or somewhat positive opinions about the system and its resulting transparency. Civil servants who submitted their declarations in 2016 expressed an even higher level of support for the system and its openness (82 per cent).

Existing research suggest that there is close and positive correlation between the existence of the disclosure systems and the lower level of corruption[285].

A7.6 Role and contribution of the MFA

Overall, the MFA III was certainly a material factor in exerting the pressure on the authorities and advancing the set-up of NABU, NACP and SAPO. However, it was the IMF which held a leading role in the conceptualisation and establishment of the institutional architecture[286] (see also detailed conditionality under EFF), while the WB had also contributed to the process. In Addition, the EU-Ukraine Visa Liberalisation Action Plan (VLAP) also incorporated the anti-corruption reforms (e.g. Specialised Anti-Corruption Prosecution Office) that was relevant in an explicit (and very meaningful) way for the implementation of this condition[287]. Besides, other actors were also involved at various stages e.g. training for senior staff at NABU provided by American's FBI.

Interviewees from the EU Delegation, WB and the IMF expressed the view that without the concerted effort of the donors' community, neither NABU nor other key anti-corruption institutions in Ukraine would have been set up.

Regarding the key ownership for the asset declaration system reform and the relative importance of the MFA III conditionality in establishing the system, the MFA III was certainly one of the main incentives, albeit again - not the only one. The set-up of the system was linked to the discussions on EU visa liberalisation, and was also promoted by,

[284] Transparency International, 2019. Corruption high on the agenda as Ukrainians go to the pools. Available at: https://voices.transparency.org/corruption-high-on-agenda-as-ukraine-goes-to-polls-57a7ed6001c9

[285] Djankov, S. 2009. Disclosure by politicians. Available at: https://www.nber.org/papers/w14703

[286] Through its conditionality of a detailed character

[287] The Economist, 24th August 2017. Ukraine's reform activists are under attack. Available at: https://www.economist.com/europe/2017/08/24/ukraines-reform-activists-are-under-attack

inter alia, the IMF EFF conditionality that according to the EU Delegation, WB and the IMF itself played a decisive role. Besides, the UNDP (e.g. supported the tool development) and number of governments including the US government who consistency pushed for the advancement of this reform (e.g. conditioning the deployment the US debt guarantee facility on the sufficient progress with the system) or the Danish Ministry of Foreign Affairs that provided financial support to develop the system’s software also played a role.

The asset declaration system has been included in the subsequent MFA IV operation and the IMF program (SBA 2019).

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A7.8 Statistics (Case study on corruption)

Year	Number of declarations published in the Unified State Register of declarations*	Number of cases of failure to submit or late submission of Declarations (based on messages received by NAZK)	Number of processed messages on possible false information in the declarations	Number of processed requests for special inspection of the information specified in the declaration of the person applying for the position of a person authorized to perform the functions of the state or local self-government	Number of complete verification of declarations (completed)	Number of decisions made on the results of complete (full) verification of declarations	Number of cases taken to the court	Number of approved substantiated conclusion made by NAPC and sent to specially authorized corruption bodies	Number of cases that ended up with the sentence for an offender (Number of follow-up cases resulting in courts' proceedings)
2016	106997	1700	n/a	n/a	n/a	n/a	11	n/a	4
2017	987116	18688	1089	8398	634	143	49	7	n/a
2018	856857	17000	2719	11133	615	472	310	243	n/a
2019	845220	23000	3292	9110	1133	1 535	371	269	n/a

Annex 8 Case Study: Social safety nets for the IDPs

A8.1 Introduction

This case study provides an overview of the Internally Displaced Person (IDP) conditions promoted as part MFA III to Ukraine. Box 12.1 displays the exact content of these conditions, as per Memorandum of Understanding[288].

Full text of the two key MFA III conditions related to Social safety nets for the IDPs

Condition 12 (second tranche)

Ensure the effective provision of social benefits and services to internally displaced persons (IDPs) through adequate legislation and funding.

Condition 16 (third tranche)

Prepare a first evaluation of social service delivery to IDPs and ensure effective follow-up.

The case study drew on the evidence gathered from the desk research including publications produced by national stakeholders (e.g. Ministry of Social Policy of Ukraine, Minister for Temporary Occupied Territories and Internally Displaced Persons of Ukraine), international organizations (e.g. the United Nations, the Global Protection Cluster, the International Office for Migration) and DG ECFIN mission reports. Annex 1 provides the full reference list of reviewed documentation.

In addition, information collected via a number of interviews also fed into the case study. Some conducted as part of the Evaluation of the MFA III to Ukraine covered a wider range of topics (including IDP conditions) while others had the explicit objective to contribute to this case study (the interview with DG ECHO and the then expert in IDP issues from SGUA).

A8.2 The IDP situation in Ukraine

The first IDPs began to flee in April 2014 as pro-Russian armed men gradually began to gain control over the Crimean Peninsula and parts of the Donetsk and Luhansk regions in east of Ukraine. IDPs, according to the *United Nations Guiding Principles on Internal Displacement,* are "persons or groups of persons who have been forced or obliged to flee or to leave their homes or places of habitual residence, in particular as a result of or in order to avoid the effects of armed conflict, situations of generalized violence, violations of human rights or natural or human-made disasters, and who have not crossed an internationally recognized state border."

IDP waves intensified in the summer and autumn of 2014.Drivers of displacement thus included: conflict, insecurity, violence, human rights violations, lack of access to adequate housing, livelihoods, welfare benefits, social services, healthcare and education. IDP waves intensified during the period of August to October 2014. The yearly flow of new displacement reached 647,000 in 2014 and 942,000 in 2015. By the end of 2015, Ukraine transitioned from having no IDP population[289] to having the world's eighth largest population of displaced persons, after Syria, Colombia, Iraq, Sudan, Yemen, Nigeria and South Sudan[290].

The quick increase in the IDP population is captured in the MoSP statistics on registered IDPs, although with some time lag. In the recent years, the flow of new displacement has

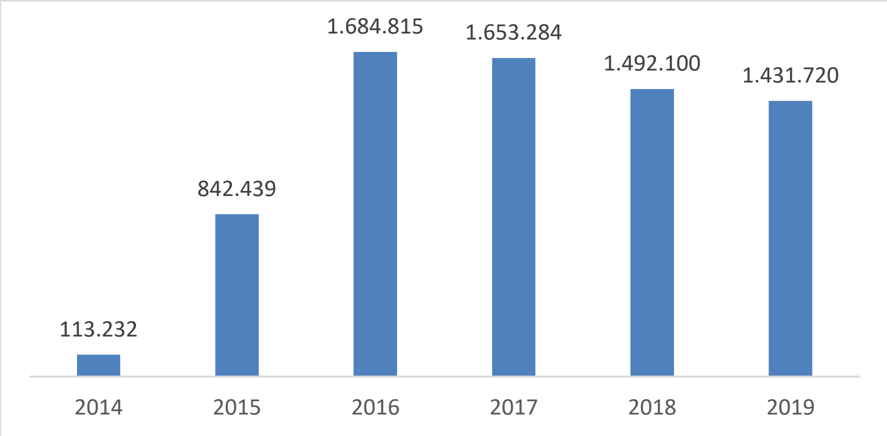
[288] European Commission, 2015. Memorandum of Understanding between European Union and Ukraine (MFA III). Available at: https://ec.europa.eu/economy_finance/international/neighbourhood_policy/doc/mou_eu_ukraine_en.pdf

[289] In the past, Ukraine had dealt with some flows of IDPs in relation to the Chernobyl disaster. This concerned about 120,000 people at the time. https://www.fmreview.org/crisis/meybatyan

[290] "Database," Internal Displacement Monitoring Centre (IDMC), http://www.internal-displacement.org/database/.

ceased. The stock of IDP population remains, however, high. 1.5 million people categorised as IDP represents roughly 3.5% of the Ukraine's population.

Figure 18. Number of registered IDPs



Source: MoSP data

IDP statistics concern mostly those who fled from the eastern regions of Donetsk and Luhansk to government-controlled areas (GCA) but also include those still living in the non-government controlled areas (NGCA) who registered as IDPs in order to be able to receive their social benefits (including pension). According to the 2020 Humanitarian Needs Overview (HNO), 730,000 IDPs out of the 1.4 million 'registered' IDPs permanently live in GCA. The rest of the registered IDPs live permanently in NGCA but it is not clear whether they are really displaced or needed to register as IDPs to receive their social benefits. There is no reliable information on the number of displaced people within the non-government controlled areas (NGCA).

Beyond IDPs, it is understood that some leaving in the conflict-affected areas left to Russia, or other neighbouring countries. UNHCR estimates that there were close to 350,000 refugees and asylum-seekers from Ukraine in 2015. The number decreased to around 125,000 in 2018[291]. The main destination country for Ukrainian refugees and asylum-seekers is into the Russian federation (90% of those concerned in 2015, 60% in 2018). The number of Ukrainian labour migrants working abroad is also substantial and concerned 1.3 million Ukrainian people in 2015–2017 according to a survey carried out by the State Statistics Service of Ukraine in 2017, or twice this estimate according to other studies reaching numbers between 2.2 and 2.7 million[292]. About a quarter of those would be living in the Russian federation according to the State Statistics Service of Ukraine.

A8.3 The rationale for the IDP conditions

Back in 2015, Ukraine was facing significant threats notably to its territorial integrity and to its socio-economic situation and had no experience of dealing with such an IDP crisis, which in turn made problematic an immediate and appropriate response. Besides, despite the efforts of the local CSOs the international community, and notably of the European Union and its Member States, there were signs that the humanitarian crisis remained underfunded with significant unmet needs of the crisis-affected population[293]. From the EU perspective, supporting Ukraine in addressing the IDP crisis was also important in

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292 European Commission (2020) The Impact of Labour Migration on the Ukrainian Economy. Available at: https://ec.europa.eu/info/sites/info/files/economy-finance/dp123_en.pdf

293 the UN Humanitarian Response Plan 2015 for Ukraine was funded only at about 55%. Plans for 2016 and 2017 were funded even more partially (35% and 37% respectively). Source: https://fts.unocha.org/appeals/464/summary.

order to avoid substantial flows of Ukrainian citizens needing to migrate or look for an international protection on the territory of the EU – even the EU is typically not the main destination of Ukrainian refugees and asylum seekers.

An assistance programme for persons that were forced to leave their homes as a result of the conflict in eastern Ukraine was launched by the Ukrainian government in November 2014 for an initial period of 6 months (Resolution No. 505). A few months later, at the time of the MFA III negotiations, it became clear that there was a need to extend that programme beyond the initial period and the MFA III leverage was used with that specific purpose in mind, including ensuring that the programme would be renewed beyond its original timeframe.

Furthermore, the MFA III also supported the undertaking of an evaluation of policies in favour of IDPs, as there was a lack of comprehensive and neutral information at the time.

A8.4 Implementation of the conditions

A8.4.1 First evaluation of social service delivery to IDPs and ensure effective follow-up

As per condition #16, 3rd tranche, Ukrainian authorities commissioned an evaluation of social service delivery to IDPs in 2016. The results of the evaluation were presented in July 2016. It took some time and DG ECFIN's insistence to have the evaluation report published on the website of the Ministry of Social Policy[294]. The evaluation provided various recommendations[295].

On 15 August 2017, the Ukrainian authorities provided a detailed document describing the state of play with the implementation of the recommendations contained in the evaluation report. Reportedly, by end 2017, many of the policy recommendations were either achieved or were in the process of being implemented[296].

A8.4.2 Provision of social benefits and services to IDPs

As said, an assistance programme for persons that were forced to leave their homes as a result of the conflict in eastern Ukraine was launched by the Ukrainian government in November 2014 for an initial period of 6 months (Resolution No. 505). The monthly targeted assistance was meant for registered IDPs to cover accommodation costs and utilities (UAH 884 or approx. EUR 34 for unemployable people, UAH 442 or approx. EUR 17 for able-bodied people, with a cap of UAH 2,400 or EUR 94 per family[297]). For comparison, between December 2013 and July 2015, the minimum wage in Ukraine was UAH 1,218. While the minimum wage was increased over the lifetime of the MFA operation, mostly to take into account the price developments but also in real terms (value multiplied by 1.3 in January 2018 compared to value before the beginning of the crisis in January 2014 using constant prices)[298], the amounts of the monthly targeted assistance remained the same.

In April 2015, the duration of the programme was extended for another six-month period because of the prolongation of the conflict (Resolution No.212-VII of 31 March 2015),

[294] http://www.msp.gov.ua/news/13403.html

[295] Recommendations covered the following themes: 'Suspension of Payments', 'Voting', 'Birth, Marriage and Death Certificates', 'Elderly and Disabled Pensions', 'Database', 'Legal Aid', 'Coordination', 'Strategy', 'Resources', 'Psycho-social support', 'Compensation', 'Sharing Data', 'Health System', 'Means Testing', 'Accommodation' and 'Employment'.

[296] European Commission (2017) "Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Third Disbursement Under MFA III".

[297] Conversion using the exchange rates at the time of adoption of MFA III (April 2015: 1 UAH = 0.03924 EUR. Source: InforEuro

[298] https://voxukraine.org/en/high-minimum-wage-as-a-driver-into-self-employment-or-the-ones-whose-salaries-have-increased/

before being made permanent. The social protection programme was initially judged by the European Commission as being sufficient to demonstrate the effective provision of social benefits, despite being modest in financial terms[299] (see also Figure 21).

In February 2016, however, the Ukrainian Ministry of Social Policy suspended social payments to around 500,000 IDPs (up to 600,000 according to UN estimates) in five eastern regions, pending verification of their status. As a result, approximately one third of the 1.75 million registered IDPs were deprived of social transfers, including pensions and IDP allowance. According to the UN, these policy measures were principally aimed at restricting the access to pensions for persons who reside in non-government-controlled areas[300].

Following pressure from the EU, the UN and Ukrainian NGOs, on 8 June 2016, the Ukrainian government adopted a resolution implementing procedures enabling IDPs affected by the suspension to apply for the renewal of their IDP certificate and consequently for the reinstatement of their social payments. This involved new applications (from IDPs who had social payments suspended) to have IDP certificates renewed.

By July 2016, local authorities who were responsible for verifying these applications processed only 9% of submissions and the vast majority of IDPs were still deprived from the access to social payments. The EU closely followed up on this, with VP Dombrovskis requiring weekly updates from Ukraine Prime Minister on the matter as part of the MFA monitoring. In the second half of 2016, notable progress was made towards the resumption of social protection for IDPs. By February 2017, 95.8% of applications received had been processed (of which 77% received a positive decision).

Thus, at the time of the disbursement of the second tranche (in April 2017), the EC judged the condition as not being fulfilled, though it waived it due to the progress made by Ukrainian authorities since July 2016. 98.9% of applications were processed by January 2020 (of which 85.4% received a positive decision).

A8.5 Impact of the conditions

A8.5.1 First evaluation of social service delivery to IDPs and ensure effective follow-up

Condition #16 ahead of the third tranche consisted of preparing a first evaluation of social service delivery to IDPs and ensuring effective follow-up. The MFA condition on this was useful as not only the report was undertaken by two independent experts but also, following DG ECFIN's request, it was made available on the website of the Ministry of Social Policy[301]. The evaluation provided various recommendations, and follow-up actions have been subsequently reported by the Ministry of Social Policy.

Figure 19. Themes covered by the recommendations

- 'Suspension of Payments',
- 'Voting',
- 'Birth, Marriage and Death Certificates',
- 'Elderly and Disabled Pensions',
- 'Database',

[299] European Commission (2017) "Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Third Disbursement Under MFA III".

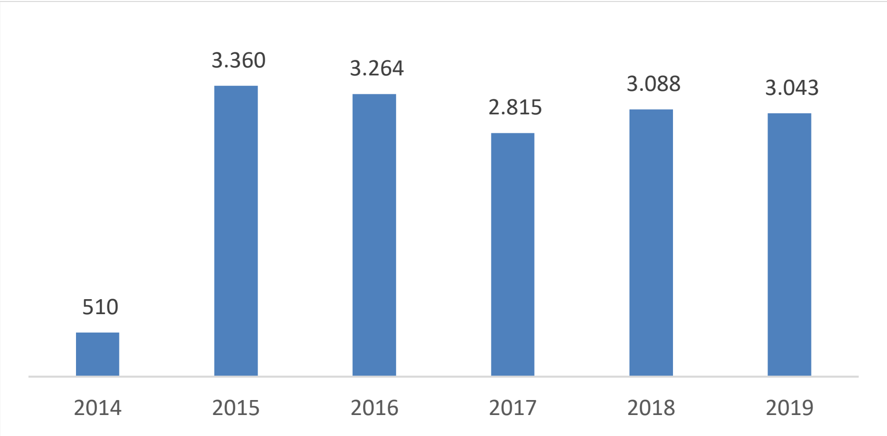
[300] UN (2019)," Pensions for IDPs and persons living in the areas not controlled by the Government in the east of Ukraine", (http://www.un.org.ua/images/documents/4719/Briefing%20Note%20on%20Pensions-eng.pdf).

[301] http://www.msp.gov.ua/news/13403.html

- 'Legal Aid',
- 'Coordination',
- 'Strategy',
- 'Resources',
- 'Psycho-social support',
- 'Compensation',
- 'Sharing Data',
- 'Health System',
- 'Means Testing',
- 'Accommodation' and 'Employment'

While legislative and administrative improvements related to the situation of IDPs are still ongoing, it is understood from ECFIN documentation as well as insights gathered from other stakeholders within the Commission that no major gap in the implementation of the recommendations have been identified. Notably, various envelopes dedicated to assistance to IDPs in 2017 were broadly maintained in the 2018 and 2019 budget or slightly increased (compared to the rather low envelope in 2017).

Figure 20. Budgetary allocations in favour of IDP programmes (UAH million)



Source: MoSP data

A milestone was also achieved when a strategy on integration of IDPs prepared by the Ministry of Temporarily Occupied Territories and IDPs, was adopted by the Cabinet of Ministers in November 2017 and signed in December 2017.

MFA IV conditions followed up on the implementation of the 2018-2020 IDP strategy by requesting the adoption of Action Plan (itself approved in November 2018). According to ECFIN MFA IV assessment[302], it triggered the preparation and/ or enactment of several measures, including some aiming at facilitating payments of social benefits to IDPs, compensation for damaged property, provision of affordable housing.

One exception to this rather positive assessment regarding the follow up on the recommendations formulated as part of the evaluation concerns the social benefits. More specifically, the evaluation had recommended to harmonise the requirements for IDPs

[302] European Commission (2020) Information Note to the European Parliament and to the Council. Available at: https://ec.europa.eu/info/sites/info/files/economy-finance/mfa_iv_ukraine_info_note_to_ep_and_council_2nd_tranche_may_2020.pdf

and non-IDPs to access social payments. Yet, IDPs are still subject to additional verification requirements, which are onerous especially for those actually living in the NGCA (see section A8.5.2).

Last but not least, another area of impact stems from the fact that the report in itself was widely shared with CSOs and international organisations like the UNHCR. It has subsequently been used to inform the delivery of humanitarian response by donors in Ukraine, as reported consistently during stakeholder interviews.

A8.5.2 Provision of social benefits and services to IDPs

The other IDP condition (#12, 2nd tranche) was focused on results (reading need to "ensure the effective provision of social benefits and services to internally displaced persons (IDPs) through adequate legislation and funding"). It was a useful reference incentivising the authorities and prompt reaction to the Ukrainian authorities' IDP programme in 2016 following its suspension. It is reasonable to assume that the process may have taken more time without the MFA condition and in itself, this is already an achievement, despite the limitations of this programme e.g. easing the pressure on the housing of the IDPs (see Figure 21).

Figure 21. Limitations of the programme to solve the housing problem

Over the medium to long term perspective, housing became one of the most acute problems for IDPs in Ukraine.

The very low level of financial support granted under the IDP programme – 884 hryvnias (approx. 27 euro) for people unable to work (with disabilities) and 442 hryvnias (approx.14 euro) for others are not aligned with the prices on Ukraine's housing market. Desk research indicated that prices for one-room apartments in 2017 ranged from 1,200 hryvnias or approx. 38 euro in the Sumy oblast in northeast Ukraine to 7,000 hryvnias or approx. 219 euro in the Kyiv oblast.

In addition, while this in theory should not be a problem, the need for IDPs to officially register for residence at their new address include risk of discrimination of IDPs, in a context where many flat owners still practice tax avoidance.

Source: *Bertelsmann Stiftung (2018) An uneasy reality - Donor support for IDPs in Ukraine*

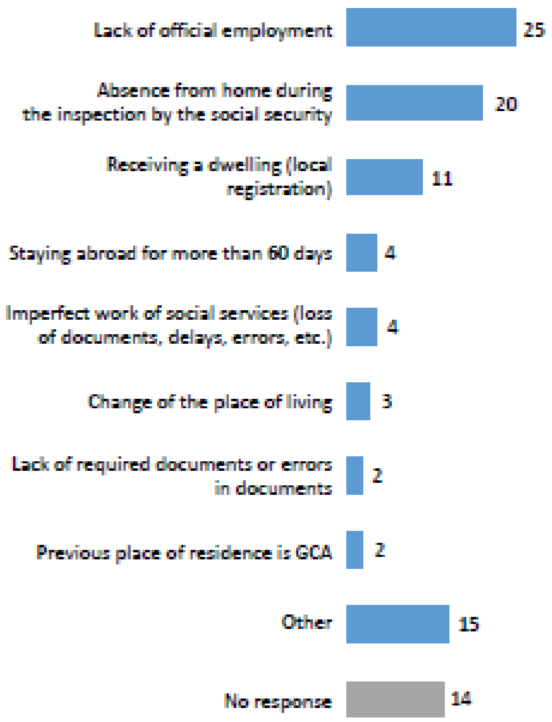
Over the course of MFA III implementation, it became clear that the condition formulation become subject to ambiguous interpretation. In its narrow sense, the purpose of the condition #12, 2nd tranche, agreed in May 2015, was to ensure that the time-limited IDP assistance programme would be renewed. At first, the condition was met: the programme was first renewed before being made permanent in November 2015. The implementation of the condition was, however, not smooth further down the line when the payments were suspended in February 2016, pending a verification process whose aim was allegedly linked to fraud related concerns, but in fact seemed to illustrate the authorities' actual intention to stop the payment of pensions to persons who actually reside in the NGCA.

When this happened, using the MFA III leverage, the EC focussed on the argument that payments did not need to be suspended during the verification process. Secondly, when procedures enabling IDPs concerned by the suspension to apply for the renewal of their IDP certificate and for the reinstatement of their social payments were put in place, the EC insisted also on the speedy processing of the applications, requiring weekly updates on the process (which were indeed provided). In the end, condition was essentially waived on the grounds that the verification process, by the end of 2016, had progressed well (90% of applications having been processed), and the second tranche of the MFA III was subsequently disbursed.

The effectiveness of the condition, from the EU perspective was, however, mixed: the processing of the applications did not mean that the provision of social benefits and services to IDPs was effective. For those who saw their application accepted, the payment of accumulated arrears is still an open issue, according to stakeholder interviews. Besides, a substantial share of applicants saw their applications rejected: 13.5% of the submitted applications as per MoSP figures for January 2020, or 369,055 IDP applications.

The interviews conducted as part of the national monitoring system report on the situation of IDPs shed some light on the reasons behind the suspensions of social payments. The two most frequent reasons to have the benefits suspended were the lack of employment (the assistance is meant to not exceed four months for the working age IDP population[303]) and the absence from home during the verification process. The third reason is obtaining residence registration in their new homes, which means that in the current set-up, IDPs face a trade-off and cannot continue to receive assistance and pension and secure other rights, such as the right to vote in local elections.

Figure 22. Reason behind the suspensions of social payments, % of respondents who had social payments suspended



Source: International Organization for Migration (IOM), Mission in Ukraine, National monitoring system report on the situation of IDPs, June 2019

Figure 23 recaps on the key protection concerns associated with the IDP programme and the verification process.

[303] According to the Government Resolution No. 505 On providing a monthly targeted assistance to IDPs to cover living expenses, including housing with utilities if a family receiving support consists of working age persons who have not been employed or do not actually work, within two months from the date of the monthly targeted assistance, the amount for able-bodied family members is reduced by 50% during the next two months, and the next period is terminated.

Figure 23. Key protection concerns

- The suspension of benefits prior to verification violated basic principles of procedural fairness and implied delays with payment ranging from 1 to 6 months. Benefits should only have been suspended if and when fraud had been detected.
- Among those IDPs who faced suspension of social assistance, only a minority received suspension notifications were aware of the reasons behind the suspension of social payments (25% and 37% respectively).
- Suspension of payments put IDPs at risk of eviction, homelessness, as well as inability to meet basic needs such as food and medicine. It may also have led to forced secondary displacement including return to NGCA.
- Only IDPs are subject to this periodic verification procedure, held every six months, which is discriminatory. Other Ukrainian citizens receiving the same benefits are not being subject to the same scrutiny. The evaluation of social service delivery to IDPs prompted by the MFA condition (condition #16, 3rd tranche) had recommended to harmonise the requirements for IDPs and non-IDPs.
- Older people have to queue for long hours at the Pension Fund to apply to have their pension reinstated.
- In itself the inspection process, which does not rely on any sort of prior notification, implies that IDPs need to be present at their registered address at all times – which restricts not only their mobility but also their employment opportunities.
- The process is also prone to corruption.

Source: *Protection Cluster Ukraine (2017) Update on IDP access to social benefits and pensions*

This issue of the suspension of payments was intertwined to the fact that since 2014, the Ukrainian legislation requires persons from NGCA to register as IDPs in the GCA in order to continue receiving their social payments (including their pensions). Many (among those who are not mobile and not able to leave the NGCA and travel to GCA) have been deprived of their rights as result – which was a first reason of concern for the EU/ UN. In addition, this policy distorted IDP statistics, as pensioners from the NGCAs, even if they were not internally displaced and did not intend to relocate to GCAs, had incentives to register as IDPs, if they wished to receive their pension. In that context, it is understood that many frequently crossed the contact line back and forth, to receive their social payments while maintaining their actual place of residence in the NGCA. At first the authorities, despite being aware of the situation, accepted it[304] but the suspension of payments and subsequent verification process suggest that the government seeks to restrict the access to pensions for persons who reside in non-government-controlled areas[305].

Even when those officially registered as IDPs but still living in the NGCA were de facto allowed to receive their payment, the frequent travel requirement represented a disproportionate burden for all those concerned. In that context (and to help the non-mobile ones who were already left out of the system), the EU and UN started to argue that since receiving a pension is a fundamental right protected by the Ukrainian Constitution, pension payments should not be dependent on obtaining the status of IDP (delinking).

[304] United Nations (2019) Pensions for IDPs and persons living in the areas not controlled by the Government in the east of Ukraine, Briefing Note//February 2019

[305] UN (2019)," Pensions for IDPs and persons living in the areas not controlled by the Government in the east of Ukraine", (http://www.un.org.ua/images/documents/4719/Briefing%20Note%20on%20Pensions-eng.pdf).

In the meantime, as long as delinking was not achieved, the CoE highlighted how important it would be to stop the inspections linked to the verification process - inspections which gave the grounds to exclude those actually living in NGCA from the IDP programme and deprive them from their rights[306].

The MFA condition thus did not suffice to prevent a deterioration of the situation for those effectively living in the non-government-controlled areas (NGCA) of Donetsk and Luhansk regions of Ukraine. More than an issue of support to IDPs, the matter is one of access to social payments for those living in the NGCA. These broader (social payments and pension) issues were discussed in ECFIN mission reports. The more flexible stance of the EU on the broader, intertwined, politically loaded issue of access to social payments from those living in the NGCA stems from (i) the progress made on the verification process and (ii) the fact that the MFA condition did not specifically mention the issue of the non-payment of pensions of those living in NGCA. It also illustrated the difficulties of pushing for particular actions from the outside when there is no shared understanding. There are considerable differences between Ukrainian authorities and international groups (e.g. UN, EU) regarding the way in which IDPs are viewed. For the EU, the provision of social security to IDPs is principally a humanitarian issue, whereas for the Ukrainian authorities it is more politically complex than that as citizens from the parts of the Donetsk and Luhansk regions in east of Ukraine which are currently not controlled by the government of Ukraine are no longer contributing to the pension system in Ukraine and residents in these areas typically receive a pension from the so-called "authorities" of these so-called "Republics", or from Russia for those who registered their residence in Russia and obtained Russian passports.

Bearing in mind the mixed results described above, 12 participants to the Delphi survey agreed that MFA III conditionality was successful in ensuring social services are delivered to the IDPs while 9 participants did not agree.

A8.6 Role and contribution of the MFA III

The MFA III leverage was seen as useful to put pressure on the authorities to extend their support programme and reinstate the social assistance once it had been suspended, despite the broader results which were more mixed. Over time, the IDP issue became linked to that of the eligibility for pensions. Individuals from the NGCA could receive their pensions only if they register as IDPs while according to the EU/UN, all people hold the legitimate right to receive a pension regardless of their IDP status. With the benefit of hindsight, the MFA III condition calling to "ensure the effective provision of social benefits and services to internally displaced persons (IDPs) through adequate legislation and funding" was perhaps not specific enough and too result-oriented to ensure a shared understanding of what was exactly intended.

Although the issue was debated, no condition on pensions specifically has been incorporated in the subsequent MFA operations. If a condition on such an issue was to be proposed as part of an MFA MoU, there would be a need to ensure that the condition is precise enough, and that there is a sufficient backing for it (coming from internationally agreed principles or from rulings in Ukraine e.g. the Supreme Court in Ukraine), and that the authorities are ready to endorse such a condition, which may well not be the case given the material differences in views on the question of access to social payments from the NGCA.

[306] Council of Europe (2019) Enhancing the Legal Framework of Ukraine on Protecting the Human Rights of IDPs

A8.7 Annex 1

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- Bertelsmann Stiftung (2018) An uneasy reality - Donor support for IDPs in Ukraine
- Council of Europe (2019) Enhancing the Legal Framework of Ukraine on Protecting the Human Rights of IDPs
- Greg McTaggart, Michael Stone (2016) Evaluation of the policy steps taken by the Ukrainian Government towards the delivery of social services to Internally Displaced Persons (IDPs) https://www.msp.gov.ua/news/13403.html
- International Organization for Migration (IOM), Mission in Ukraine, National monitoring system report on the situation of IDPs, June 2019
- Protection Cluster Ukraine (2017) Update on IDP access to social benefits and pensions
- United Nations (2019) Pensions for IDPs and persons living in the areas not controlled by the Government in the east of Ukraine, Briefing Note//February 2019

Annex 9 Case study on the use of the euro

A9.1 Introduction to the case study

In December 2018, the Commission ended 20 years of policy neutrality on the Union's single currency. A Communication (Towards a Stronger International Role of the Euro), as well as a Recommendation in the field of energy, were published by the European Commission, advocating an active policy to support the global role of the euro[307]. To this end, the Commission, *inter alia*, envisages diplomatic engagement with international partners to promote the use of the euro in payments and as a reserve currency.

Given the political and economic nature of the MFA instrument, it can potentially play a role in promoting the use of euro as an international currency among recipient countries through the following channels:

Direct role via the use of conditionality aimed at promoting the use of euro as an international trading, investment and reserve currency among recipient countries e.g. promoting reforms that enable the government, public authorities and/ or businesses in recipient countries to issue euro-denominated debt; or reforms that enable the recipient country to access infrastructure for euro trading and clearing.

Direct impact of MFA on the stock and currency composition of the beneficiary country's debt and foreign reserves.

Use of conditionality aimed at promoting bilateral trade, investment and economic ties between the EU and the recipient country, more broadly.

Using the economic assistance provided via MFA as an inducement/ leverage to encourage international use of euro among recipient countries. In other words, actively encouraging recipient countries to increase their use of euro in return for the financial assistance.

The MFA operations in Ukraine pre-date the European Commission's communication on a stronger international role of the euro and as such, these specific operations did not include any conditionalities or entail any specific diplomatic efforts aimed at promoting the use of euro. This case study therefore, focuses on channel 2. It is based on information collected via desk research and interviews.

A9.2 The use of euro in asset and debt management activities of the Ukrainian authorities

A9.2.1 Asset management – the use of euro in investment and foreign exchange reserves

The currency composition on the asset side of the NBU's balance sheet reflects the currency composition of its liabilities, to avoid a mismatch between the two. According to the NBU, it does not like to have open currency positions on its balance sheet.

As most obligations of the Ukrainian government are in dollars (see next section on debt management), the majority of the NBU's foreign assets are dollar denominated (about 75% in 2018). Ukraine also has large borrowings from the IMF in SDRs. On the asset side, the currency composition therefore, reflects the SDR basket currencies (the U.S. dollar, the euro, the Chinese renminbi, the Japanese yen, and the British pound sterling).

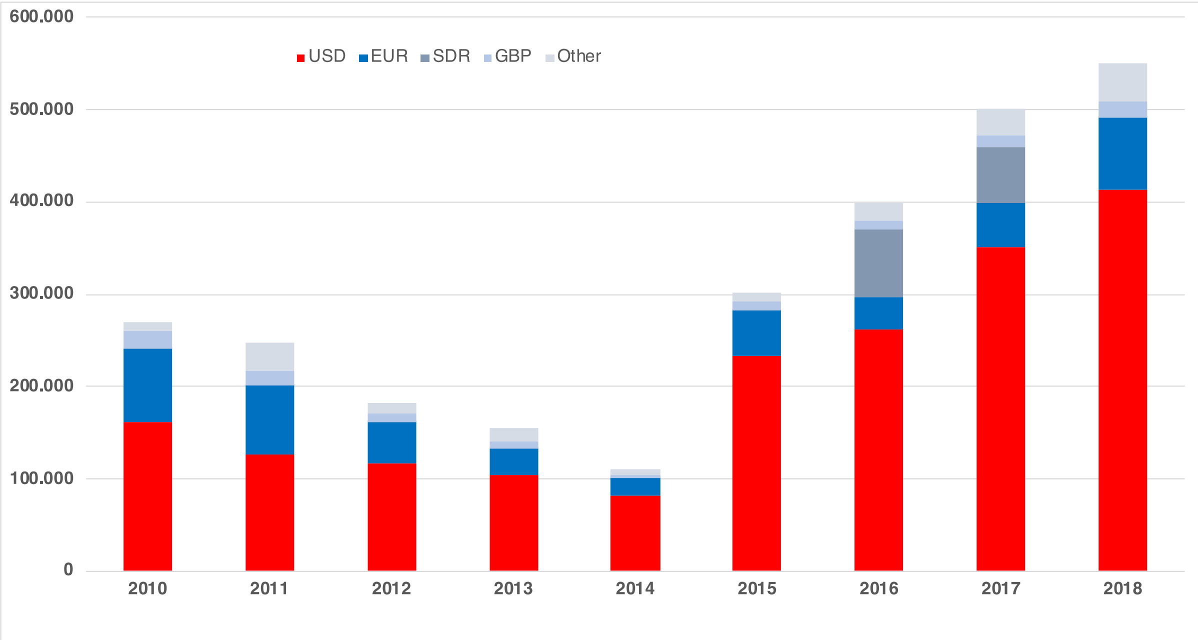
The share of euro in the NBU's reserves has declined both in absolute and relative terms between 2010 and 2018 – see Figures 1 and 2. In absolute terms, the amount of foreign assets held in euros declined from 79 UAH billions to 78 UAH billions, while the relative

[307] COM(2018) 796/4 - Towards stronger international role of the euro: Commission contribution to the European Council and Euro Summit. Brussels, 5 December 2018. Available at: https://ec.europa.eu/commission/publications/towards-stronger-international-role-euro-commission-contribution-european-council-13-14-december-2018_en

share of euro dropped from 29% to 14% over this period. About a third of the euro denominated assets were held in the form of cash and deposits at the end of 2018, while two-thirds were held in the form of securities. The amount of euros held in the form of cash and deposits has declined over time, while the amount of euros held in the form of securities has increased.

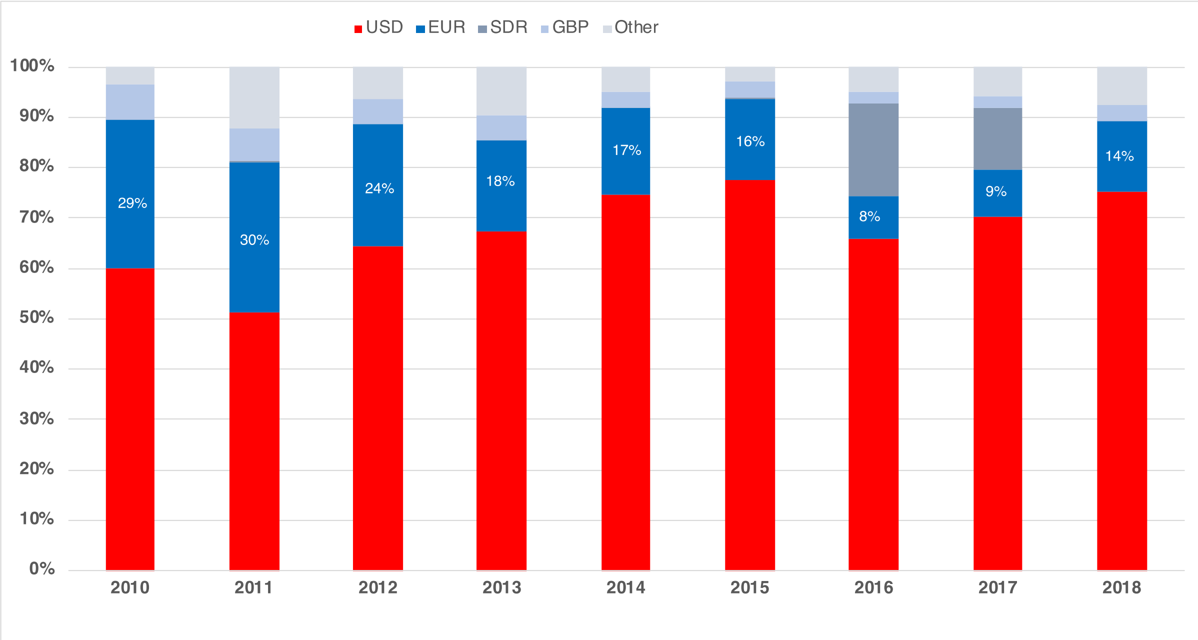
During 2010-2012, a push to diversify the reserve currency structure and increase returns, drove an increase in the NBU's euro holdings (and other exotic transactions such as buying up gold scrap directly from population and made amendments to NBU law to allow it to start gold mining in Ukraine and purchasing over a billion in Australian dollars in a bet that commodity boom would push them up). The picture changed following the drain on currency reserves that started after Russia's military intervention in Crimea.

Figure 24. NBU Foreign Assets in UAH millions



Source: NBU

Figure 25. NBU Foreign Assets, % share of currencies



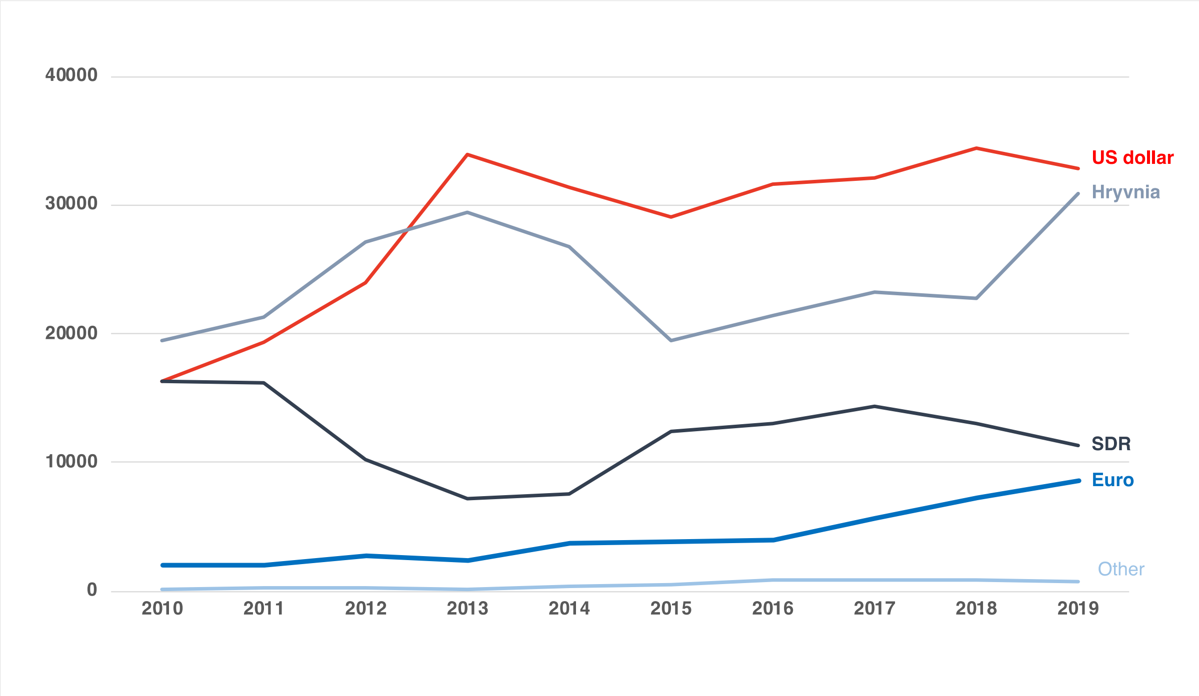
Source: NBU

According to the NBU, settlements in euros have increased significantly, but still the main interbank market activity is conducted in dollars and the official rate is still hryvnia-dollars. The rest of the rates are calculated based on the dollar (cross-rates based on dollar). So for example, if an importer needs euros, normally they buy dollars, then convert these dollars into euros. The dollar domination reflects an element of path dependency: Ukraine has historically been a very dollarized country.

A9.2.2 Debt management – the use of euro as a borrowing currency

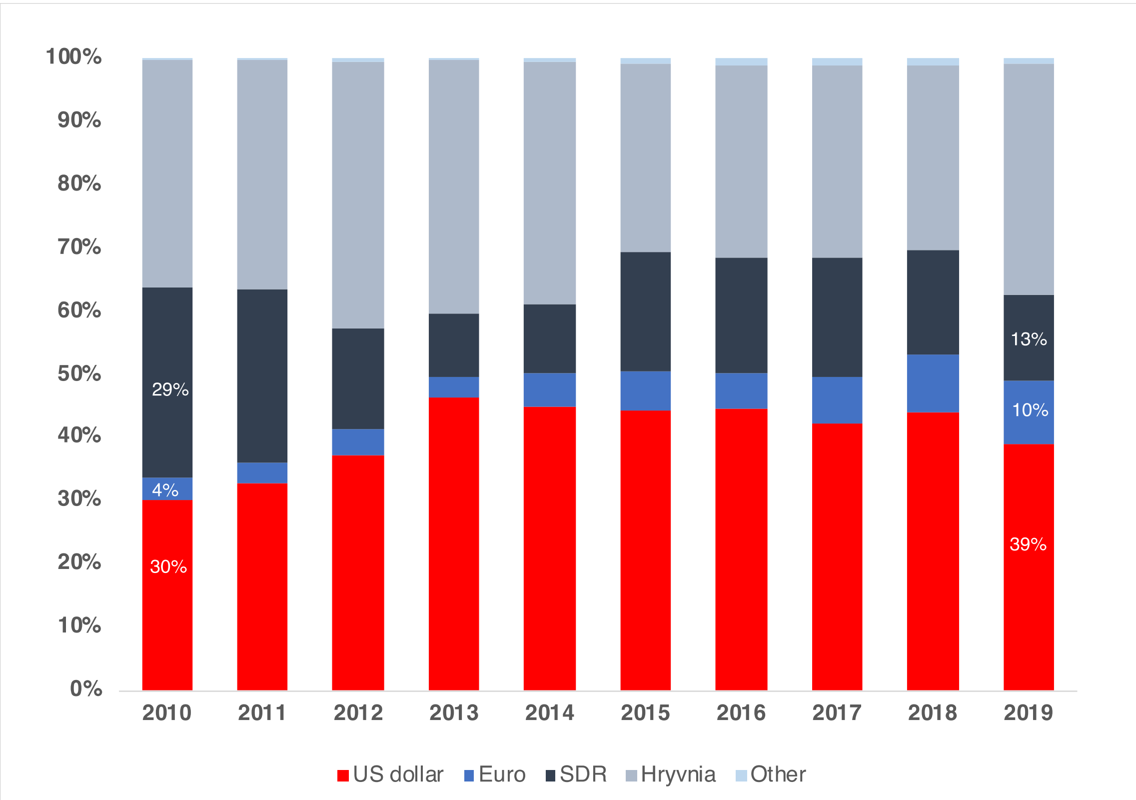
Ukraine's state debt is largely dominated by foreign currency denominated debt (63% of total debt as of end 2019). USD-denominated debt represents 39% of the total state debt and is predominantly composed of USD-denominated Eurobond series. The second largest category comprises SDR-denominated debt raised as part of financing within the IMF programs (10% of Ukraine's state debt at the end of 2019). EUR-denominated debt mainly raised as a part of the several EU's Macro-Financial Assistance programmes extended over 2014 – 2018 and accounted for 10% of the debt at the end of 2019. The EU MFAs thus, directly contributed to increasing the stock of EUR- denominated over the period 2015 - 2018. According to the MoF, this encouraged them to go the EUR Eurobond market.

Figure 26. State and state-guaranteed debt breakdown by currency, USD million



Source: Ministry of Finance

Figure 27. State and state-guaranteed debt breakdown by currency, % share



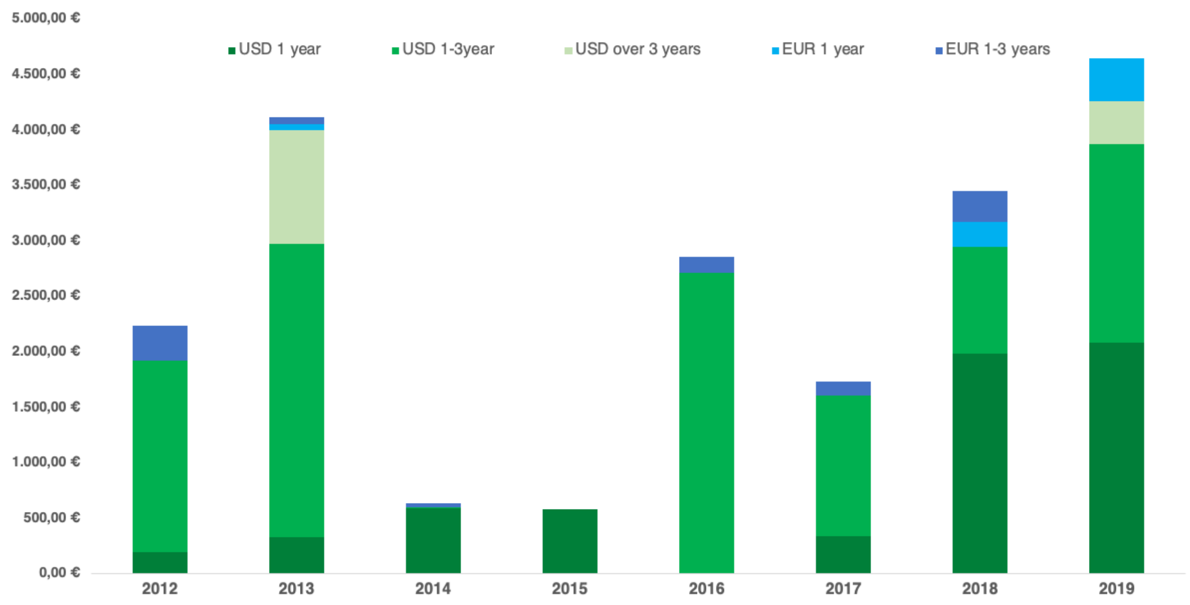
Source: Ministry of Finance

The Ukrainian MoF was initially borrowing from the markets only in USD , reflecting past legacy (and heavy dollarization of the economy). Moreover, US investors (particularly pension funds) were attracted to Ukrainian debt as it offered high return in line with the risky profile of the country. The European investors, which are traditionally more conservative, did not have much of an appetite for Ukrainian debt due to its sub-investment grade sovereign rating.

Recently, however, the MoF has taken several measures to enhance EUR- denominated debt exposure:

- Returning to EUR Eurobond market in 2019 after a gap of 15 years with a 7-year EUR 1bn issuance at the rate of 6.75% per annum. The issuance was successful in attracting European investors (37% from Continental Europe and 32% from the UK)[308]. Following this, the MoF went for a second issuance in January 2020. This 10-year EUR 1.25bn issuance was heavily oversubscribed (6x) and the authorities were successful in achieving a record low 4.375% yield. The Investors from the United Kingdom accounted for 42% of the issue; 34% of investors were from the United States (27% in 7 - year Eurobonds); and 19% of the issue was purchased by investors from the EU and Switzerland[309].
- Issuances of EUR-denominated domestic government bonds totalling EUR 387m in 2019;
- Continuing cooperation with the EU, EBRD, EIB.

Figure 28. Evolution of volume of euro denominated issuances, EUR million



Source: Ministry of Finance

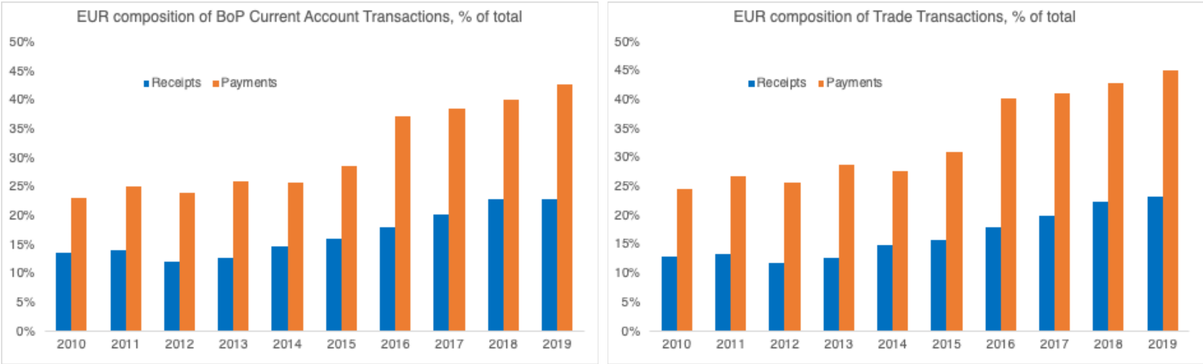
This shift partly reflects the increasing share of euro in trade turnover and current account flows[310] – see Figure 29.

308 https://www.mof.gov.ua/en/news/ukraina-povertaietsia-povertaietsia-na-rynok-ievro-iz-pershym-vypuskom-ievrobondiv-nominovanykh-v-ievro-vpershe-za-rokiv

309 https://www.mof.gov.ua/en/news/yuriy_butsa_building_a_yield_curve_in_euros_allows_us_to_expand_the_investor_base_and_create_a_benchmark_for_corporate_borrowers-2028

310 Which includes trade flows, income and direct transfers (such as remittances)

Figure 29. Share of euro is current account flows and trade turnover, %



Source: National Bank of Ukraine

Other reasons for increasing euro issuance include

- Rebalancing state debt currency mix and offsetting euro BoP outflows;
- Diversification of investor base (e.g. pension funds from Eurozone);
- Capitalising on lower funding costs (spread is more expensive, but headline coupon is lower as compared to USD);
- Construction of a benchmark yield curve – see box below.

In parallel, the search for yield has driven investors to Ukraine and also to other emerging markets from the region such as Serbia and Albania.

Figure 30. Ukraine's Medium-term state debt management strategy for 2019 - 2022

The overarching objective of the Strategy is as follows: *"to secure the required financing at the lowest possible cost, while containing risks."* To this end, the Strategy outlines the four specific objectives for state debt management:

Increase the share of state debt denominated in local currency to reduce FX exposure
Lengthen average debt maturity, and ensure a smooth state debt repayment profile.
Attract long-term concessional funding.
Continue developing strong investor relationships and further improve the state debt management policy framework.

FX risk and refinancing risk have been identified as key threats to state debt sustainability for the upcoming years. One of the tasks of this Strategy stands in the constant monitoring and mitigation of these risks.

Diversifying currency mix of the public debt structure is one of the goals of the Strategy, given the trend to increase the role of Euro in the Ukrainian economy as a result of integration into EU markets. The Strategy foresees construction of EUR-denominated Eurobond yield curve, to expand the investor base and create a benchmark for corporate borrowers interested in obtaining financing in euros. At the same time, it also envisages an increase in issuance of UAH-denominated domestic government bonds, deepening the local currency bond market (by enhancing the participation of international investors in the Ukrainian domestic market), as well as mitigating FX risks by reducing the share of USD in Ukraine's state debt portfolio through the issuance of Eurobonds in other currencies.

Source: Ministry of Finance of Ukraine

A9.3 Key messages

The MFA operations in Ukraine did not include any conditionalities or involve any specific diplomatic efforts aimed at promoting the use of euro. However, by increasing the stock of EUR-denominated debt, the MFA played a role in encouraging the Ukrainian authorities to go the EUR Eurobond market. The Medium-term state debt management strategy of the Ukrainian authorities envisages a diversification of the currency mix of their public debt and construction of EUR-denominated Eurobond yield curve. The use of MFA was thus aligned with the authorities' plans.

Annex 10 Social Impact Analysis (SIA)

A10.1 Introduction

The overarching aim of the Social Impact Analysis (SIA) is to use evidence from social indicators and primary data to assess the impact of Macro Financial Assistance (MFA) III on the social situation in Ukraine. The analysis considers both direct impacts transmitted through social safety nets (assisting vulnerable households and internally displaced persons[311]) and indirect impacts across a broad range of social indicators.

For the purpose of the analysis, direct effects are defined as impacts which stem from conditionalities outlined in the Memorandum of Understanding corresponding to the MFA. Indirect effects are defined as being those which stems more broadly from wider macroeconomic stability.

The approach of the analysis is, firstly, to describe how the social situation in Ukraine evolved before, during and after MFA interventions. Once this baseline is outlined, the analysis then contrasts these outcomes with several counterfactual scenarios[312] to form an assessment of what the social situation would have been in the absence of some or all of the MFA (and IMF) support.

With regard to the timing of the support, the implementation period of the MFA is defined as 2015-17[313].

The socio-economic context of Ukraine prior to and during MFA operations is discussed in Section 2.1. This provides a foundation for further analysis, especially with regard to policy challenges in the country. Direct effects are analysed in Section A10.2.1. The section seeks to understand – through data-driven analysis – the extent to which vulnerable households were protected from the effects of energy reform (as specified in the Memorandum of Understanding). The provision of social benefits and services for internally displaced persons (IDPs) is also addressed in this section. The analysis primarily focusses on four main policy aims:

- To ensure that compensation mechanisms designed to protect vulnerable households are fully functional (and take into account the anticipated increase in beneficiaries).
- To ensure the effective provision of social benefits and services to IDPs, through adequate legislation and funding.
- To cushion the effects of energy tariff increases while making progress towards consolidated and better targeted social assistance programmes.
- To evaluate the delivery of social services to IDPs and follow up effectively.

Evidence from stakeholder surveys is used in conjunction with available empirical data to form an assessment of progress made by the Ukrainian authorities. Challenges associated with implementing the main actions are discussed and, to the extent that it is possible, evidence of tangible impacts are consulted. The outcomes discussed in Section A10.2.1 can be considered to be the result of MFA operations. This is because the policies investigated are those which are specified in the Memorandum of Understanding associated with the MFA.

311 Internally displaced persons (IDPs) are people who have fled their home but have not crossed a border to find safety. Unlike refugees, IDPs stay within their own country and remain under the protection of its government (even if that government is the reason for their displacement).

312 These are hypothetical scenarios formed using a combination of stakeholder engagement, local expertise, macroeconomic theory and Delphi surveys.

313 The date of the council decision was April 2015, the first disbursement of funds was made in July 2015, and the second disbursement of funds was made in April 2017. The third disbursement was also scheduled for 2017 but was not disbursed.

Trends in variables relating to the macroeconomic situation (indirect effects) are also analysed in the report in Section A10.2.2. The aim of this content is to assess developments in socio-economic variables, such as wage growth and unemployment, prior to, and (where possible) during/after the MFA period. The section also discusses developments to nominal variables which impact the affordability of goods and services. Section A10.2.3 discusses impacts to key social outcome variables such as national poverty levels, living standards and household expenditure patterns.

The counterfactual analysis is provided in Section A10.3, which aims to establish what the social situation in Ukraine might have been in the absence of MFA first-tranche funding (Alternative 1), in the absence of MFA second-tranche funding (Alternative 2), with the addition of third-tranche MFA funding (Alternative 3) and in absence of all MFA and IMF funding (Alternative 4). The findings are summarised in Section 4.

A10.2 Social trends

Political instability, conflict and annexation

The context underpinning the social situation in Ukraine has been shaped by political instability and military conflict in the region. In February 2014, pro-Russian president Viktor Yanukovych was removed from power. This event was followed by armed conflict with the Russian Federation, culminating in the annexation of Crimea in 2014 and the war in Donbas in the Donetsk and Luhansk oblasts (military conflict is ongoing at the time of preparing this report).

Recent estimates from the UN High Commissioner for Human Rights[314] report that the armed conflict has resulted in 41,000-44,000 conflict-related casualties and 13,000-13,200 deaths. Another key result of these developments has been the internal displacement of approximately 1.5m residents affected by the conflict. According to the UN, Ukraine is the ninth largest country in the world in terms of internally displaced persons (IDPs) as a result[315]. The large and vulnerable group stemming from these developments poses challenges to the social situation of Ukraine.

In addition, as a result of the conflict, the political status of areas not under the control of the government in eastern Ukraine and Crimea has become increasingly complex. Referendums have been held regarding the legal status of Crimea, areas not under the control of the government in Donetsk Oblast and Luhansk Oblast, but Ukrainian authorities judged them as illegitimate due to their divergence from due process specified in the Ukrainian constitution[316]. Reinforcing this, the UN General Assembly voted in favour of the territorial integrity of Ukraine in 2014[317]. Nonetheless, as an interim measure, the Minsk protocol specifies that Ukraine must grant "special status to local self-government in certain areas of the Donetsk and Luhansk regions"[318].

[314] Office of the United Nations High Commissioner for Human Rights (2020), "Report on the human rights situation in Ukraine

16 November 2019 to 15 February 2020", (https://www.ohchr.org/Documents/Countries/UA/29thReportUkraine_EN.pdf).

[315] UN Refugee Agency, "Internally Displaced Persons – Ukraine", (https://www.unhcr.org/ua/en/internally-displaced-persons).

[316] The Verkhovna Rada of Ukraine (1996), "Constitution of Ukraine", (https://zakon.rada.gov.ua/laws/show/254%D0%BA/96-%D0%B2%D1%80/conv).

[317] UN General Assembly (2014), "Resolution adopted by the General Assembly on 27 March 2014", (https://www.un.org/en/ga/search/view_doc.asp?symbol=A/RES/68/262).

[318] https://peacemaker.un.org/sites/peacemaker.un.org/files/UA_140905_MinskCeasfire_en.pdf

The Ukrainian energy and utilities system – policy context

The structure of energy provision in Ukraine has changed considerably since 2010[319]. Historically, the energy model in Ukraine involved the provision of utilities to households at artificially low prices by quasi state-owned companies (incurring a loss which would be funded by the state). According to the Energy Subsidy Reform Facility (World Bank)[320], in 2013 the retail price of gas for the average Ukrainian household was just 20% of the import price of gas.

Although this model had the effect of lowering utility costs for households, it also had several significant shortfalls. Firstly, from a social perspective, due to the universality of the implied subsidy and due to differences in energy consumption patterns across income deciles, this policy was regressive. Only 13% of the implicit subsidies were being attributed to the poorest income quintile[321]. This means that, from the perspective of social transfers, the policy exacerbated income inequality in Ukraine. Secondly, the energy model considerably dampened incentives to improve energy efficiency and eliminate waste. Lastly, the policy was costly and created exceptional demands on public finances.

In light of these considerations, measures were taken to reform the energy market in Ukraine, gradually increasing the retail price of gas from UAH 1,089 in 2014 to UAH 6,958 in 2017. In order to compensate eligible households for rising tariffs, financial support was provided to households through various pre-existing utility subsidy schemes. The most important for the purpose of this analysis were the Housing and Utility Subsidies (HUS) scheme and the Housing and Utilities Privileges (PRIV) scheme. The former (and larger) scheme sought to cushion the effects of tariff increases for households most affected by energy reform (the evolution of this policy is considered throughout the SIA). The latter was established to grant certain categories of the population (e.g. war veterans, people disabled during hostilities in the east, Chernobyl victims) a discount on their energy bills irrespective of their income.

A10.2.1 Direct effects of MFA III

Conditionalities relating to the social safety net

Coupled with the budgetary support provided by MFA III, operations in Ukraine also include four key policy conditionalities (presented in Table 40). These conditionalities aimed to protect two key vulnerable groups in Ukraine: households who were affected by energy reform and IDPs.

Table 40. MFA III conditionalities relating to the social safety net

	Conditionality	Tranche
Households affected by energy reform	• With a view to protecting vulnerable households from the increase in energy tariffs, ensure that the compensation mechanisms are fully functional, taking into account the expected increase in the number of beneficiaries.	Second tranche
	• To cushion the effect of energy tariff increases, make substantial progress towards consolidating and better	Third tranche

[319] Principally change occurred since 2014. Prior to 2014, other Ukrainian authorities also made pledges to the IMF to phase out energy subsidies (e.g. the Tymoshenko government in 2008 and the Azarov government in 2010), but Naftogaz losses and implied energy subsidies were still very high in 2013.

[320] World Bank, ESMAP (2017), "Ukraine", (http://documents.worldbank.org/curated/en/884621506493335975/pdf/120076-26-9-2017-11-9-3-FINALESMAPCountryBriefUkraine.pdf).

[321] Ibid.

	targeting of relevant existing social assistance programmes[322].	
Internally displaced persons	• Ensure the effective provision of social benefits and services to internally displaced persons (IDPs) through adequate legislation and funding.	Second tranche
	• Prepare a first evaluation of social service delivery to IDPs and ensure effective follow up.	Third tranche

Source: European Commission (2014)[323].

Support for households affected by energy reform

The first key domain on which the conditionalities were focused was the strengthening of the social safety net to cushion the impacts of energy reform and improve its targeting[324]. This reinforced similar policy conditions present in IMF programme.

The second-tranche conditionalities required policy action to accommodate the increase in the number of beneficiaries and to ensure that compensation mechanisms were fully functional. This conditionality did not specify the efficiency with which vulnerable groups were targeted, but instead prioritised coverage in the first instance. This condition was considered as being fulfilled by the European Commission, albeit at a higher cost than was originally envisaged[325].

Ukrainian authorities launched an information campaign aimed at potential beneficiaries[326], including advertisements in national and local TV and radio programmes, the press, leaflets, and announcements made in supermarkets. This information campaign explained the policy change, as well as the necessity of energy price increases[327]. The Ukrainian authorities also simplified the application process, in order to reduce access barriers for vulnerable groups. The application forms were shortened to one page and income/expense declarations were also simplified[328]. As application volumes increased (starting around autumn 2015), administrative capacity to manage these applications was also reportedly increased[329]. By the end of 2016, approximately 7

[322] Examples of relevant programmes include: the privileged housing utilities programme, the means-tested transfers for housing utilities and the tariff compensation scheme.

[323] European Commission (2015) " Memorandum of Understanding between the European Union as Lender and Ukraine as Borrower".

[324] European Commission (2015) "Proposal for a Decision of the European Parliament and of the Council Providing Macro-Financial Assistance to Ukraine", (https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52015PC0005&from=EN).

[325] IMF (2020) Ex-post evaluation of exceptional access under the 2015 extended arrangement—press release and staff report (https://www.imf.org/en/Publications/CR/Issues/2020/06/16/Ukraine-Ex-Post-Evaluation-of-Exceptional-Access-Under-the-2015-Extended-Arrangement-Press-49518?cid=em-COM-123-41725)

[326] European Commission (2017) "Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III".

[327] IMF (2020) Ex-post evaluation of exceptional access under the 2015 extended arrangement—press release and staff report (https://www.imf.org/en/Publications/CR/Issues/2020/06/16/Ukraine-Ex-Post-Evaluation-of-Exceptional-Access-Under-the-2015-Extended-Arrangement-Press-49518?cid=em-COM-123-41725)

[328] Muzychenko Vitalii (2018), "Reform of the program of housing and utilities subsidies in conditions of increase energy prices", [in association with the Ministry of Social Policy of Ukraine, World Bank and Social Protection and Jobs Learning Forum] (http://pubdocs.worldbank.org/en/721741520534548015/SSLF18-Economic-Shocks-Ukraine.pdf).

[329] European Commission (2017) "Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Second Disbursement Under MFA III".

million households were benefitting from the subsidies scheme as tariffs increase outpaced the increase in disposable income[330].

The third-tranche conditionalities maintained the requirement of compensating vulnerable households, but additionally specified the need for consolidation across social assistance programmes and better targeting. The European Commission assessed this conditionality as being fulfilled by the Ukrainian authorities. The Ministry of Social Policy in Ukraine adjusted the benchmarks of the housing and utilities subsidies scheme to limit outlays, improve targeting and encourage energy efficiency. Specifically, this involved lowering the subsidised threshold for gas consumption from $7m^3$ gas per m^2 floorspace to 5.5 m^3 gas per m^2 floorspace. Additional measures involved tightening controls to prevent applicants underreporting their income, and the gradual phasing out of energy privilege programs (including PRIV)[331].

In the years following the tighter measures, the number of households receiving subsidies and the average payment of housing and utility services decreased as incomes start increasing faster than housing and utility bill. In the heating period 2018-2019, over 4 million households received subsidies and the average payment was about UAH 1700[332]. By early 2020, the number of households receiving subsidies decreased to 2.8 million and the average payment decreased to UAH 1200 also partially due to stricter eligibility criteria[333].

Evidence from stakeholder interviews did not highlight any significant issues with this conditionality. However, it did include discussion of the need to articulate the rationale for greater targeting in a clear and effective way. The concern was felt that, if miscommunicated, ambitions to improve the targeting of utility subsidies could be misinterpreted as a part of a programme of austerity or public sector cuts.

Internally displaced persons

The second key domain on which the conditionalities were focussed was the provision of social benefits and services to internally displaced persons (IDPs) within Ukraine. The bulk of the policy action was front-loaded onto the second-tranche conditionalities, with third-tranche conditionalities mainly relating to ex-post evaluation and follow up actions.

Success in this policy area was mixed. On the one hand, the initial objective of making permanent the initially temporary assistance programme for IDPs was achieved. The social protection programme which was adopted by the Ukrainian authorities in 2015 was initially judged by the European Commission as being sufficient to demonstrate the effective provision of social benefits, despite not being particularly generous[334].

On the other hand, from 2016 onwards there were major issues with the provision of social benefits and services. In February 2016, social payments (mainly pensions) were suspended for approximately 500,000 IDPs in five eastern regions, pending verification of their status[335]. According to the UN, these policy measures were principally aimed at restricting the access to pensions and other social payments for persons who reside in

[330] Ibid.

[331] Beneficiaries of energy privileges schemes are gradually being transferred to the housing and utilities subsidies scheme and (since 2016) benefits from the two schemes cannot be cumulated.

[332] Ministry of Social Policy (2020), *Interviews*.

[333] Ibid.

[334] European Commission (2017) “Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Third Disbursement Under MFA III”.

[335] Estimates vary. According to UN, suspensions of social benefits and services occurred to up to 600,000 IDPs. [UN News (2016), “UN expert calls on Ukraine to step up its efforts to protect the rights of the internally displaced” (https://news.un.org/en/story/2016/09/538772-un-expert-calls-ukraine-step-its-efforts-protect-rights-internally-displaced).

non-government-controlled areas[336]. Following pressure from the EU, the UN and Ukrainian NGOs, a resolution was adopted by Ukrainian authorities establishing procedures for the reinstatement of social payments to IDPs. This involved new applications (from IDPs who had social payments suspended) to have IDP certificates renewed. By July 2016, local authorities who were responsible for verifying these applications had only processed 9% of submissions and the vast majority of IDPs continued to lack access to social payments.

In the second half of 2016, notable progress was made towards the resumption of social protection for IDPs involving bilateral contact between EU and Ukrainian authorities. By February 2017, 95.8% of applications received had been processed (of which 77% received a positive decision). 98.9% of applications were processed by January 2020.

The European Commission judged the condition to not be fulfilled but waived this conditionality for the second tranche due to the progress made by Ukrainian authorities since July 2016.

Evidence from stakeholder interviews provide further context to the suspension of payments and the political situation regarding IDPs. There were reportedly considerable differences between Ukrainian authorities and international groups (e.g. UN, EU) regarding the way in which IDPs were viewed. The EU saw the provision of social security to IDPs principally as a humanitarian issue, whereas for the Ukrainian authorities it was more politically complex than that and this led to the temporary suspension of social payments to some IDPs.

There were also reportedly discussions regarding the definition of pensions. The conditionality relating to IDP support did not explicitly mention pensions and there was some debate as to whether pensions come under the heading of social benefits and services.

With regard to the third tranche, as per the requirement, Ukrainian authorities commissioned an evaluation of social service delivery to IDPs in 2016. The evaluation followed two separate approaches: a human-rights-based approach and an international-law-based approach[337]. The evaluation provided various recommendations[338], and follow-up actions have been reported by the Ministry of Social Policy.

Moreover, according to the European commission, by 2017 many of the policy recommendations were either achieved or were in the process of being implemented[339]. The implementation of the remaining policy recommendations rested principally on the allocation of an appropriate financial envelope and the development of a comprehensive strategy for prioritising ongoing initiatives. There were early signs of progress towards this, as the 2018 budget of the Ministry of Temporarily Occupied Territories and IDPs was increased relative to 2017 (this budget was roughly maintained in 2019).

Based on the progress outlined above, the European Commission assessed this conditionality as being broadly fulfilled.

Assessing the impact channels

In In light of the considerations above, the direct impacts via the conditionalities included in the MoU are likely to emerge through two main channels:

[336] UN (2019)," Pensions for IDPs and persons living in the areas not controlled by the Government in the east of Ukraine", (http://www.un.org.ua/images/documents/4719/Briefing%20Note%20on%20Pensions-eng.pdf).

[337] https://www.msp.gov.ua/news/13403.html

[338] Recommendations covered the following themes: 'Suspension of Payments', 'Voting', 'Birth, Marriage and Death Certificates', 'Elderly and Disabled Pensions', 'Database', 'Legal Aid', 'Coordination', 'Strategy', 'Resources', 'Psycho-social support', 'Compensation', 'Sharing Data', 'Health System', 'Means Testing', 'Accommodation' and 'Employment'.

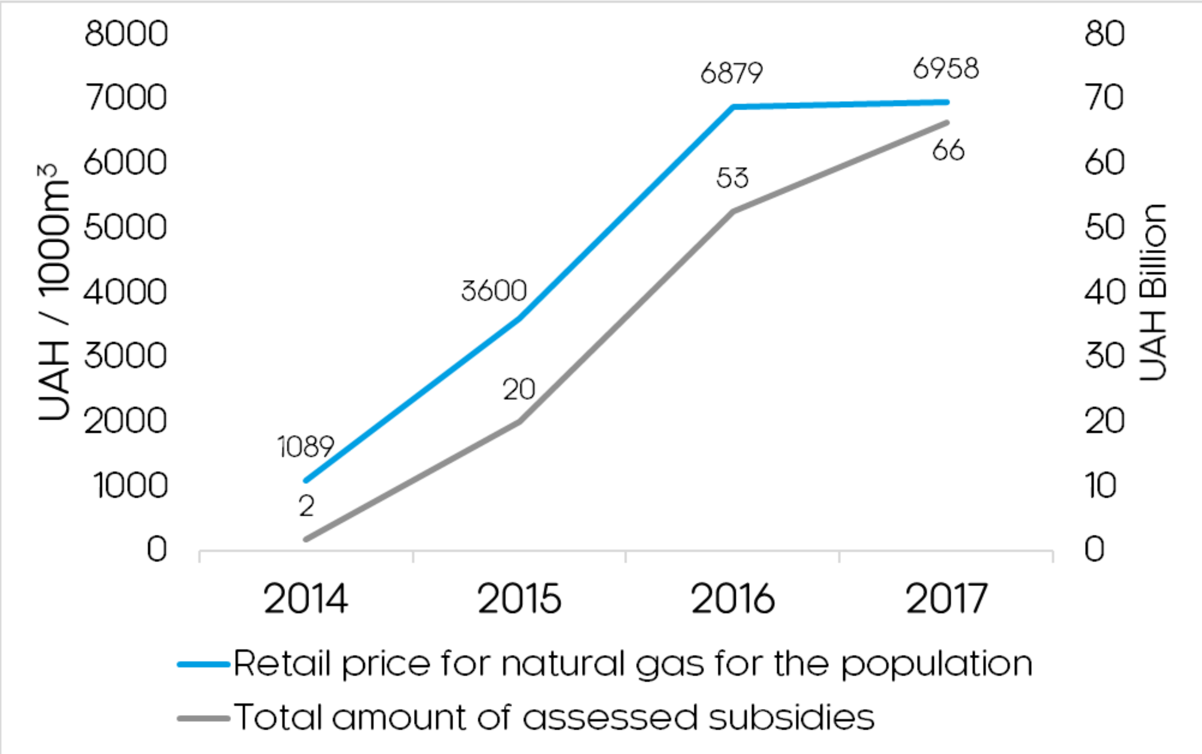
[339] European Commission (2017) "Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Third Disbursement Under MFA III".

- increased disbursements of social security schemes (existing or new),
- development of the administrative capacity necessary for: (I) targeted social security, and (II) provision of social benefits and services for IDPs.

Table 41 shows total assessed subsidies and the retail price for natural gas. Consistent with the reported findings in European Commission compliance statements and accompanying notes, increases in energy tariffs coincided with increases in the value of assessed subsidies. The total value of subsidies increased by approximately UAH 18 billion in 2015 and a further UAH 33 billion in 2016.

The growth in annual subsidies also considerably outstripped inflation over the period of MFA operations, implying a real increase in assessed subsidies of 173% per annum over 2014-17[340].

Table 41. Implied price of natural gas and total subsidies (2014-17)



Source: Ministry of Social Policy of Ukraine (2018)[341].

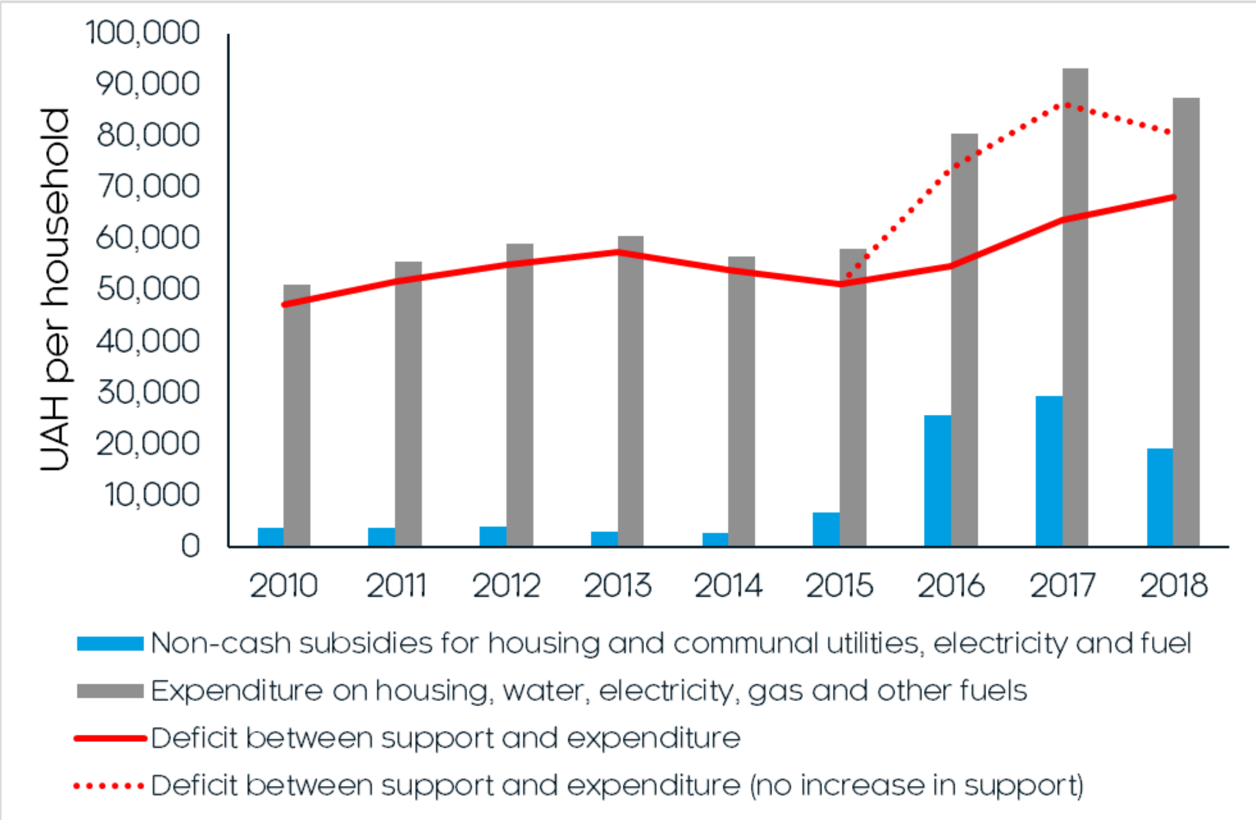
Insights into the extent to which housing and utilities subsidies cushioned the effects of energy reform can also be gathered by assessing the recorded breakdown of income and expenditure of households (this exercise is carried out in greater detail in Section A10.2.3). Table 42 shows average household expenditure on housing and utilities, contrasted with monetised non-cash subsidies provided by the state (for housing and utilities). The variation in these indicators is shown over 2010-18 and are adjusted to account for inflation.

[340] The corresponding nominal increase is 240%.

[341] Ministry of Social Policy of Ukraine (2018), "Reform of the program of housing and utilities subsidies in conditions of increase energy prices", (http://pubdocs.worldbank.org/en/721741520534548015/SSLF18-Economic-Shocks-Ukraine.pdf).

The analysis shows that increases in non-cash subsidies for housing and utilities is unable to fully offset the increases to average household expenditure in this category. It does however succeed in cushioning the impact of increased expenditure. If non-cash support remained at 2015 levels from 2015 onwards (and assuming unchanged expenditure patterns), then the deficit between expenditure and state support would have peaked at UAH 86,000 by 2017 (compared to a deficit of UAH 64,000 which was observed).

Table 42. Implied average household expenditure and subsidies for housing and utilities (adjusted for inflation)



Source: State Statistics Service of Ukraine[342] [343] [344].

While this analysis is a useful illustration of the extent to which compensation mechanisms succeeded in protecting households from the increase in energy tariffs, there are some notable limitations of the exercise. Firstly, the available data are only sufficient to describe changes experienced by the average household and is unable to provide inferences into conditions specifically relating to vulnerable households. Thus, it does not provide any information regarding the targeting of the social safety net.

Secondly, although energy reform is likely to be a key driver of changes to expenditure on housing and utilities, there could be other accompanying causes for changes to expenditure. The available statistics therefore include but do not fully isolate increased expenditure which resulted from energy reform.

[342] State Statistics Service of Ukraine, "Structure of household expenditure", Demographic and social statistics (http://www.ukrstat.gov.ua/)

[343] State Statistics Service of Ukraine, "Structure of household resources", Demographic and social statistics (http://www.ukrstat.gov.ua/)

[344] State Statistics Service of Ukraine, "Consumer price indices for goods and services in 2002-2019 (year to previous year)", Economic statistics (http://www.ukrstat.gov.ua/)

With regard to administrative capacity, evidence from compliance statements, Commission notes and stakeholder consultation (discussed earlier in this section) suggest that Ukrainian authorities were relatively successful in meeting the increasing administrative demands of utility subsidies. This is observed in the increased uptake of subsidies by households over 2014-17 (see Table 43).

Table 43. Share of Ukrainian households receiving housing and utility subsidies

	Share of households receiving housing and utility subsidies (%)
2014	7.3
2015	30.7
2016	43.7
2017	46.2

Source: Ministry of Social Policy of Ukraine (2018)[345].

Evidence of deepening administrative capacity in the domain of IDPs, however, presents a mixed picture. The aforementioned progress made towards the resumption of social protection for IDPs over 2016 and 2017 indicates a positive development in the use of state resources (technical and financial). Similarly, the increase in budget allocated to the Ministry of Temporarily Occupied Territories and IDPs (from 2017 to 2018, and roughly maintained in 2019) is a promising development.

Nonetheless, the decision to suspend pension payments to IDPs in early 2016 is likely to have exacerbated the social situation for IDPs. Many IDPs who eventually had social payments resumed needed to wait several months before their applications were processed. Moreover, a considerable minority of IDPs had their applications rejected (23%)[346].

A10.2.2 Indirect effects of MFA III – wider socio-economic climate

Labour market performance

Prior to the introduction of Macro Financial Assistance in 2015, Ukraine's experience had been a sharp deterioration in key labour market indicators (principally in 2014). Table 44 illustrates changes to unemployment rates over the period 2010-19. In 2014, the unemployment rate increased by 1.9pp from 7.8% to 9.7%. The increase in the unemployment rate was likely associated with the economic impacts of the broken supply chains and resulted drop in income due to the military conflict in the East of Ukraine and annexation of Crimea by Russia (described in Section A10.2**Error! Reference source not found.**).

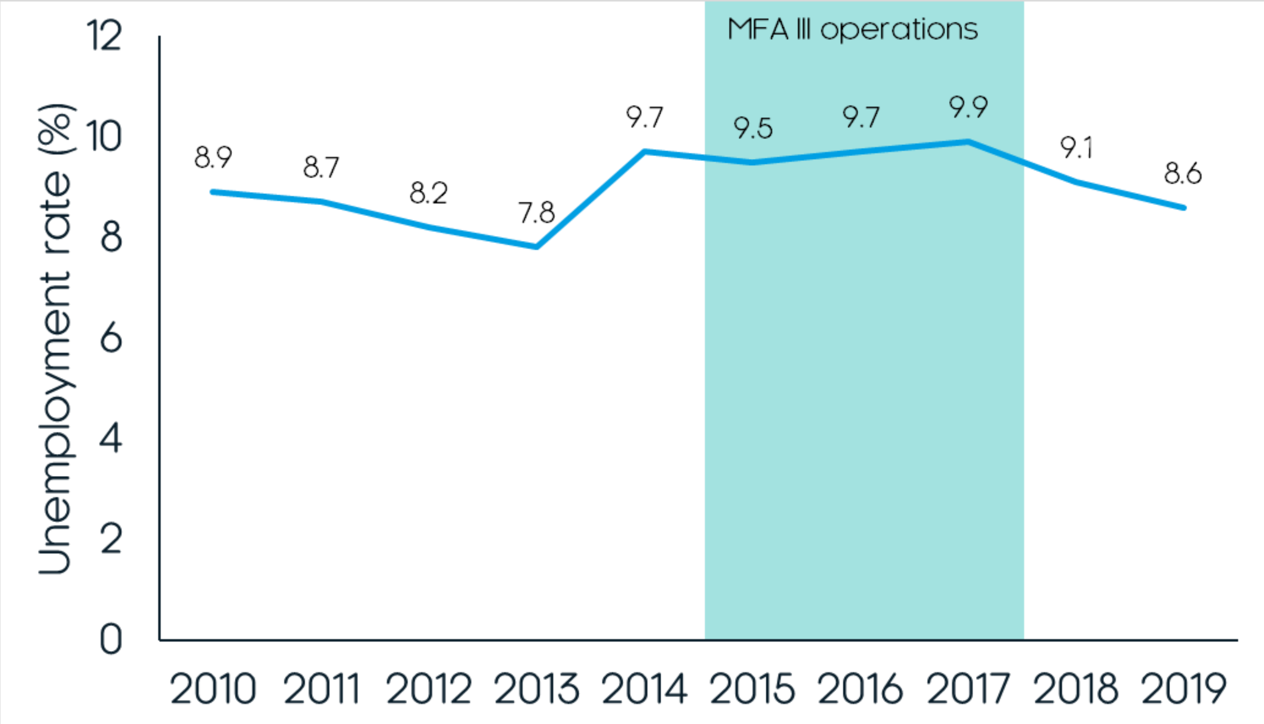
After stabilising in 2015, unemployment rates continued to marginally rise over the period of MFA operations (2015-17), as hostilities in eastern regions continued and in

[345] Ministry of Social Policy of Ukraine (2018), "Reform of the program of housing and utilities subsidies in conditions of increase energy prices" [http://pubdocs.worldbank.org/en/721741520534548015/SSLF18-Economic-Shocks-Ukraine.pdf]

[346] European Commission (2017) "Note to the European Parliament and the Council Macro-Financial Assistance to Ukraine: Third Disbursement Under MFA III"

relation to demographic changes. After 2017, the unemployment rate began to decline, falling from 9.9% in 2017 to 8.6% in 2019 (the most recent available year).

Table 44. ILO unemployment rate 2010-19



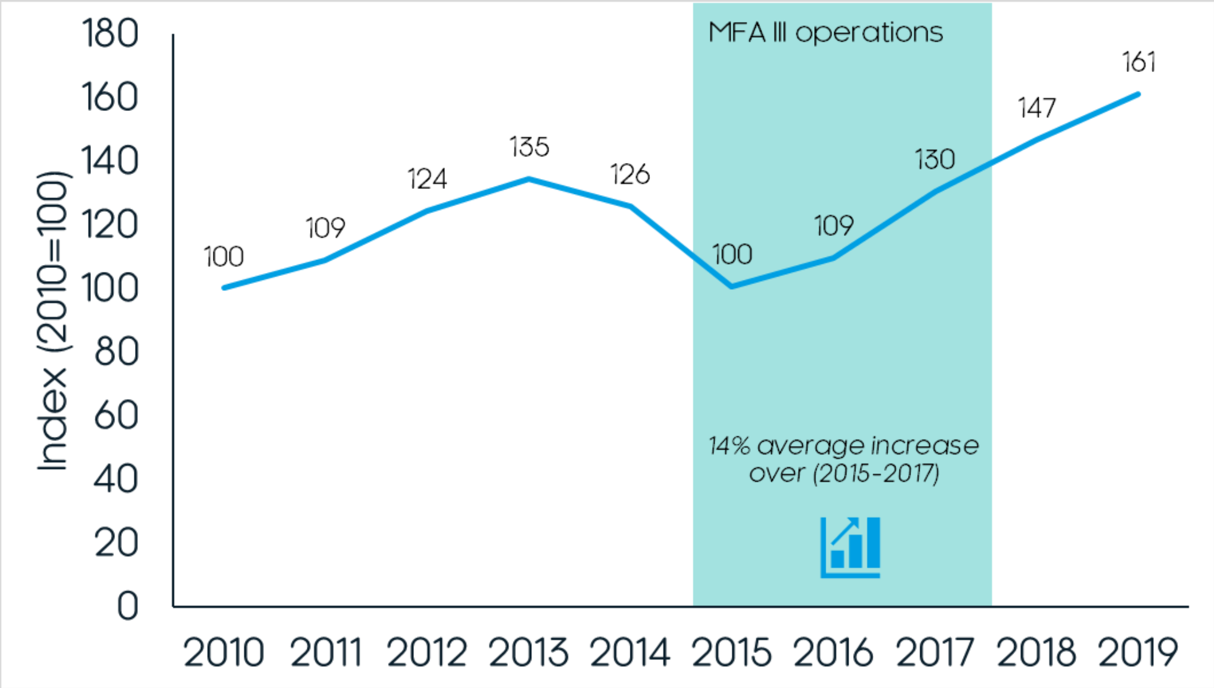
Source: State Statistics Service of Ukraine[347].

A similar deteriorating trend prior to MFA operations is observed for average real monthly wages. Table 45 shows the average real wage index over 2010-19 (indexed to the year 2010). Sharp decreases in real wages are observed over 2014 and 2015, as a result of the costs of living outpacing wage growth. Over the period of the MFA operations (2015-17), this trend reversed and robust increases in average real wages are observed (on average 14% per annum). This was because of strong nominal wage growth to compensate the high inflation, surge in minimum wage as well as tight labour market due to migration.

Real wages continued to grow strongly after MFA III operations, and were approximately 60% higher on average in 2019 than in 2015.

[347] State statistics service of Ukraine, "ILO employed", Demographic and social statistics, (http://www.ukrstat.gov.ua/).

Table 45. Real wage index 2010-19 (2010=100)



Source: State Statistics Service of Ukraine[348].

Nominal variables

Table 46 shows the consumer price index for 'housing and utilities' and for the aggregate basket of goods and services. The evidence suggests that inflation in Ukraine accelerated considerably over the period of MFA operations (2015-17). Over 2011-14 (prior to MFA operations), the average annual inflation rate was approximately 5%[349]. The rate of inflation increased considerably in 2015 such that average inflation over 2015-17 was 25%[350]. After the MFA period, inflation slowed to 9% (over 2018-19), a rate which is still above those observed in the pre-MFA period.

The accelerating increase in the cost of living over 2015-17 – as expressed by the aggregate price index – is largely attributed to the dramatic increase in the cost of housing and utilities as well as hryvnia depreciation. Over 2015-17, the price index for housing and utilities increased by 55% per annum, meaning that the (standardised) price of housing and utilities in 2017 was four times higher than that of 2014.

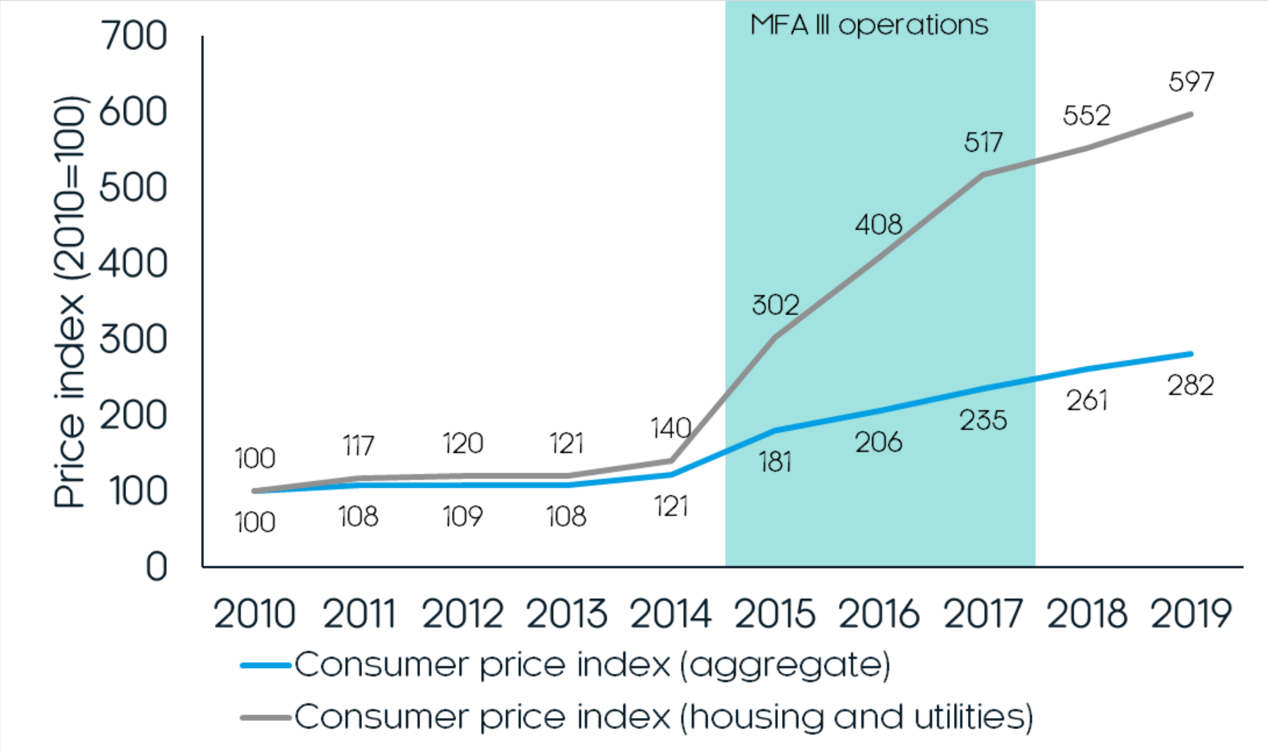
These observations, coupled with evidence discussed in Section A10.2.1, suggest that energy reform in Ukraine played a notable role in the rise in the cost of living experienced by Ukrainian households over 2015-2017 and confirm the need for social safety nets to protect vulnerable households.

[348] State statistics service of Ukraine, "Basic indicators on labor market (2010-2019)", Demographic and social statistics (http://www.ukrstat.gov.ua/).

[349] Cumulative annual growth rate of price index from 2010-2014 (i.e. rate of change considered from 2011-2014).

[350] Cumulative annual growth rate of price index from 2014-2017 (i.e. rate of change considered from 2015-2017).

Table 46. Consumer price index 2010-19 (2010=100)



Source: State Statistics Service of Ukraine[351].

A10.2.3 Key social outcomes – poverty and living standards

National poverty rates

Evidence regarding national poverty rates presents a mixed picture for Ukraine and the inferences are sensitive to the measures used to identify poverty.

The official measure of poverty (shown as the grey line in Table 47) suggests that poverty was reduced considerably (from 9% to 1%) over 2010-18. Poverty reduction under this measure stalls briefly around the time of the Euromaidan crisis (2014), but decreases considerably during and after MFA operations.

There are however, two issues with this measure. Firstly, although the legally established subsistence minimum increases over time, it often does not increase by the appropriate rate to fully reflect changes to the cost of living352. For example, in 2015 the subsistence minimum increased by 4.4% (to UAH 1227), yet aggregate inflation in 2015 is recorded to be much higher at 48.7%. Secondly, the legally established threshold for poverty is only one of many poverty criteria used in Ukraine and consistently below the 'actual' subsistence minimum, suggesting that the measure underestimates poverty in Ukraine353.

The poverty rate implied by the actual subsistence minimum is shown in Table 47 (black line), though data are only available as from 2014. According to this measure, poverty increased considerably in 2015 to 52%, in part as a result of the increasing minimum cost of subsistence. This result is echoed by the World Bank measure of poverty (shown as the blue line in Table 47). The sharp increase in poverty according to both these

351 State Statistics Service of Ukraine, "Consumer price indices for goods and services in 2002-2019 (year to previous year)", Economic statistics (http://www.ukrstat.gov.ua/).

352 It is adjusted in line with budget revenues.

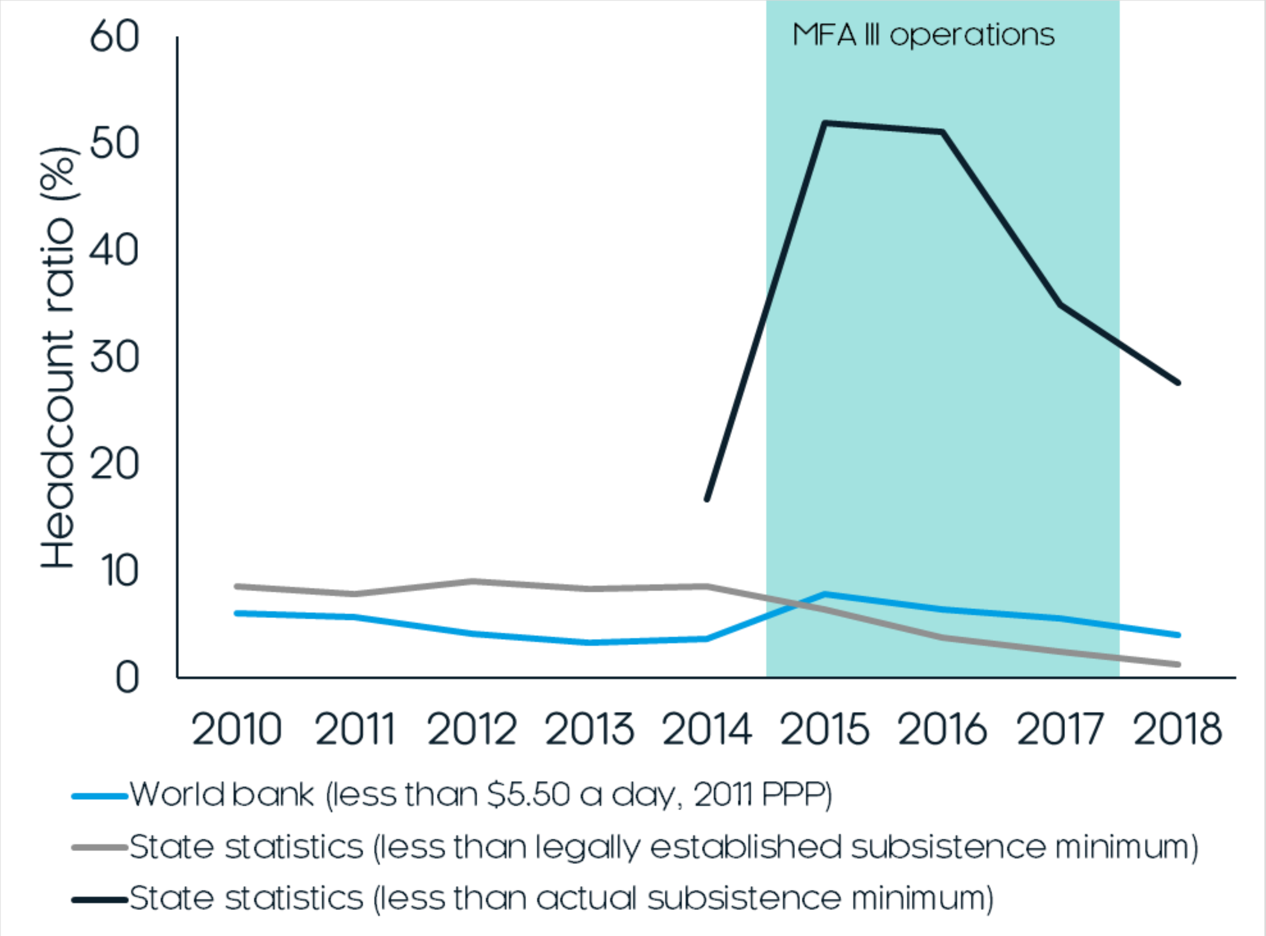
353 This is based on the presence of two poverty thresholds recorded in the State Statistics Service of Ukraine: the legal subsistence minimum and the actual subsistence minimum.

measures is a concerning result with regard to the social situation in Ukraine. A likely implication of this is that the combination of rising energy tariffs and economic instability had negative impacts on poverty (at least in the short term). This also reflects hryvnia depreciation.

However, according to all three measures, over 2015-19 poverty reduced considerably. 'Actual subsistence' poverty measure falls from 52% in 2015 to 28% in 2018 and 23% in 2019 (the most recent estimate). The notable improvement in this social outcome during and after the MFA operation is a promising sign, reflecting as well increase in wages and pensions.

Moreover, the reduction in poverty also coincides with progress in the provision of social benefits and services specified in the MFA conditionalities. 'Actual subsistence' poverty falls most sharply in 2017 (from 51% to 35%). As discussed in Section A10.2.1, the end of 2016 was a key milestone in the coverage of the housing and utilities social safety net (reaching 7 million households) and the majority of applications for the resumption of pensions for IDPs were processed from mid-2016 to early-2017.

Table 47. National poverty rates 2010-18



Source: State Statistics Service of Ukraine[354], World Bank[355].

[354] State Statistics Service of Ukraine, "Differentiation of household living standards", Demographic and social statistics (http://www.ukrstat.gov.ua/).

[355] World Bank Data, "Poverty headcount ratio at $5.50 a day (2011 PPP) (% of population)" (https://data.worldbank.org/indicator/SI.POV.UMIC).

Household expenditure

The composition of household consumption expenditure is shown in Table 48 for 2014-18. Analysis of the change in expenditure on housing, water, electricity, gas and other fuels is presented in Section A10.2.1. This section therefore focusses on the extent to which households substitute away from important items as a result of increasing energy and housing costs.

One concerning observation is the 5.6pp decrease in the share of spending allocated to food and non-alcoholic beverages which occurs over 2015-17. Coupled with the observation that inflation was also high for this spending category[356], this suggests that households may have been substituting away from food and non-alcoholic beverages to accommodate the higher housing and utility costs.

Table 48. Allocation of consumption expenditure 2014-18 (% of total consumption expenditure)

	2014	**2015**	**2016**	**2017**	**2018**
Food and non-alcoholic beverages	56.7	57.2	53.4	51.6	51.8
Alcoholic beverages and tobacco	3.7	3.6	3.1	3.3	3.7
Manufactured goods and services	39.6	39.3	43.5	45.1	44.5
Of which clothing and footwear	6.6	6.1	6.0	5.9	5.9
Of which housing, water, electricity, gas and other fuels	10.3	12.6	17.2	18.3	16.5
Of which furnishing, household equipment and routine maintenance of the house	2.5	2.2	1.8	2.2	2.3
Of which health	3.9	4.0	4.5	4.1	4.3
Of which transport	4.7	4.0	3.9	4.0	4.0
Of which communication	3.1	2.6	2.5	2.6	2.8
Of which recreation and culture	2.0	1.6	1.5	1.7	2.0

[356] Average annual inflation over 2014-2018 was 19%.

Of which education	1.2	1.2	1.1	1.2	1.1
Of which restaurants and hotels	2.5	2.2	2.4	2.5	2.6
Of which miscellaneous goods and services	2.9	2.9	2.7	2.7	2.9

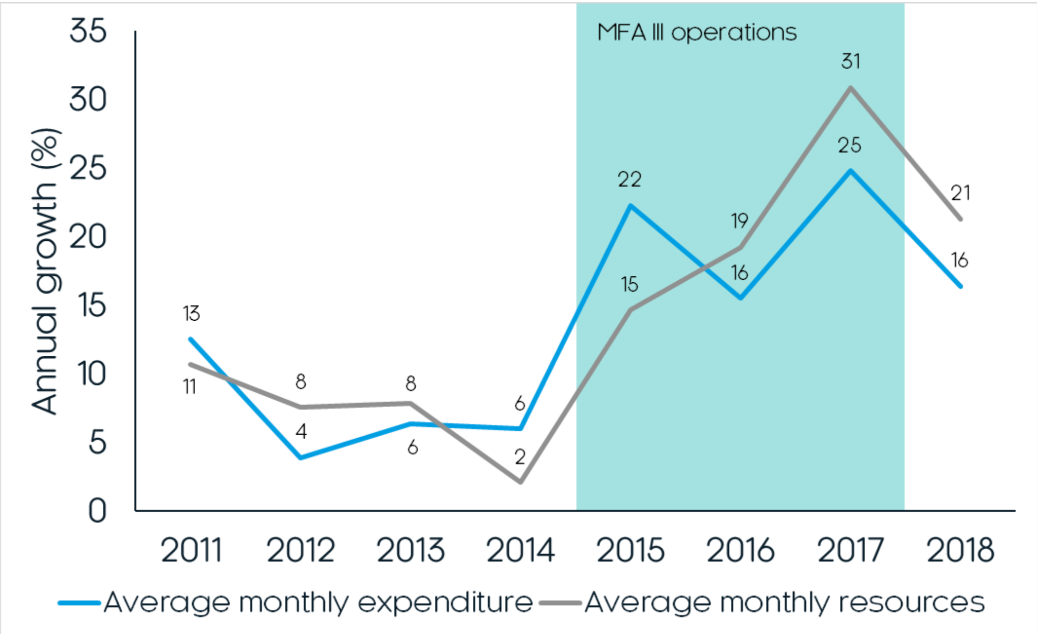
Source: State Statistics Service of Ukraine[357].

Aside from food consumption however, the share of spending on most other categories of household spending is fairly stable, and therefore not indicative of substitution.

Table 49 plots and contrasts growth in average household expenditure and average household resources (including non-cash subsidies). Growth in household expenditure outstripped that of household resources over 2013-15 indicating pressure on available household resources. From 2016 onwards, conditions change and the growth of average monthly resources accelerates (outpacing expenditure).

This is a promising sign for the social situation in Ukraine from 2016, however the caveats discussed earlier in this assessment regarding the conditions of average households versus vulnerable households apply here also.

Table 49. Growth in average household income and average household expenditure 2011-18 (%)



Source: State Statistics Service of Ukraine[358] [359].

[357] State Statistics Service of Ukraine, "Structure of household expenditure", Demographic and social statistics (http://www.ukrstat.gov.ua/).

[358] State Statistics Service of Ukraine, "Structure of household expenditure", Demographic and social statistics (http://www.ukrstat.gov.ua/).

A10.3 Counterfactual analysis

A10.3.1 Alternative 1: no MFA first-tranche scenario

Under the no first-tranche MFA scenario, Ukraine would not have had access to European Commission funds, but the IMF programme would still have been in place. To form a view regarding what would have happened in the absence of MFA operations, several key stakeholders were consulted who either were involved in the MFA/IMF operations or have specialist domain knowledge relating to Ukrainian governance.

In engaging with stakeholders who worked closely with Ukrainian financial rescue packages, this analysis seeks to provide insights into likely outcomes resulting from the absence of MFA.

Table 50. Assumptions for the no MFA first-tranche counterfactual scenario

Variable	Assumptions
Government revenue	Government revenues which are mainly taxes are not directly affected by the absence of MFA's first tranche[360].
Government expenditure	Government introduces cuts to spending in 2015 to the equivalent of EUR 600 million. Spending is reduced in the areas of: • cut to pensions (in real terms) • cuts to public procurement, including cuts to public services and cuts to any remaining capital expenditures such as infrastructure spending
Public debt	Ukraine does not obtain MFA III first-tranche financing. Public borrowing in 2015 is reduced by the equivalent of EUR 600 million (UAH 16 billion).
Gross financing needs	The gross financing need changes in line with the cuts to government expenditures.
GDP	GDP decreases due to cuts to public spending. The declines estimated using fiscal multiplier analysis are estimated at: • 2015: UAH 11.1 billion (2010 prices), equivalent to 1.2% of GDP • 2016: UAH 11.1 billion (2010 prices), equivalent to 1.1% of GDP
Inflation	Inflation remains unchanged.
Exchange rate	The UAH/USD exchange rate also remains unchanged based on the assumption that the presence of other donors in Ukraine, notably the IMF, cushions Hryvnia from the

[359] State Statistics Service of Ukraine, "Structure of household resources", Demographic and social statistics (http://www.ukrstat.gov.ua/).

[360] While government revenues could potentially decrease as a consequence of declining GDP, due to a lack of data, the potential impact on government revenues could not be reliably modelled. In any case, the impact would likely have been small in the case of this scenario.

	negative impact of not having received the first MFA tranche.

Table 50 outlines the key scenario assumptions associated with the "no MFA first-tranche" counterfactual scenario.

From the perspective of the social situation in Ukraine, a crucial element of this scenario profile is the changes to government spending expected to result from the absence of MFA. To a large extent, options for cuts to social spending were limited due to the legal safeguards imposed on certain categories of spending and due to political constraints of certain cuts.

However, the government response to the absence of MFA may have involved a delay to the unfreezing of public pension payments (decreasing the value of payments in real terms). Under the baseline, pension payments were unfrozen in September 2015 as a result of accelerating inflation. The absence of MFA funding may have necessitated a further delay to this, negatively affecting household resources from 2015.

The most likely channel of government cuts would have been capital spending and public procurement. Cuts in these areas would have had an impact on economic output and jobs, however, given the scale of the cuts relative to the size of economy, these are unlikely to have considerably destabilised Ukrainian labour markets.

Conditionalities were solely imposed on the second-tranche and third-tranche MFA disbursements and, for simplicity, their benefits will be considered in their respective scenarios. However, some of the benefits associated with these conditionalities should also be attributed to the first-tranche MFA. This is because the first tranche meant that Ukraine entered into the wider arrangement, and without which none of the conditionalities would have been in place.

A10.3.2 Alternative 2: no MFA second-tranche scenario

Under the no second-tranche MFA scenario, Ukraine would not have had access to the second-tranche of European Commission funds (disbursed in 2017) but the IMF programme would still have been in place.

Table 51. Assumptions for the no MFA second-tranche counterfactual scenario

Variable	Assumptions
Government revenue	Government revenues are not directly affected by the absence of MFA's second tranche
Government expenditure	Government expenditure is not affected by the absence of MFA's second tranche.
Public debt	The lack of MFA III second-tranche financing is initially offset by increased domestic borrowing to the full amount of EUR 600 million. The conditions underpinning domestic borrowing are similar to these obtained by Ukraine in December 2017 on its USD-denominated issuance: Maturity 1.5 years Interest rate: 4.0%
Gross financing needs	The gross financing needs remain nearly unchanged in the first 1.5 years.
GDP	No change to GDP.
Inflation	Inflation remains unchanged.
Exchange rate	The UAH/USD exchange rate also remains unchanged based on the assumption that the presence of other donors in Ukraine, notably the IMF, cushions Hryvnia from the negative impact of not having received the second MFA tranche.

Table 51 outlines the key scenario assumptions associated with the "no MFA second-tranche" counterfactual scenario.

From the perspective of the social situation in Ukraine, the absence of MFA funds would likely have been offset by increased financing from domestic markets, requiring no material changes to fiscal policy[361]. The impacts of the budgetary gap on the social situation would therefore be limited.

Considering the MFA operations as a whole (including conditionalities), Alternative 2 would have potentially undermined some of the progress made in policy areas such as utility subsidies and social benefits for internally displaced persons. According to the Delphi survey, 76% of respondents felt that reform in the area of social safety nets would have either been slower or not executed as fully without MFA conditionalities.

[361] This conclusion is supported by stakeholder consultations which typically suggest that economic conditions (and domestic funding options) were better at the time of the second-tranche disbursement (compared to the time of fist-tranche disbursement).

The timing and extent to which the social safety nets were operational would have affected the social situation for Ukrainian households. Section A10.2.1 found that the effects of increased utility prices were cushioned (partially) by the compensation mechanisms put in place by Ukrainian authorities. If these mechanisms had been delayed, if the coverage had been lower or if the schemes were less generous, then households would have been more severely affected by higher utility costs.

In a similar vein, further delays to the resumption of social benefits and services for IDPs would have likely led to a deterioration of social outcomes of this vulnerable group, especially for households relying on pension payments for subsistence.

A10.3.3 Alternative 3: MFA third-tranche scenario

Under the MFA third-tranche scenario, Ukraine would have had access to third-tranche European Commission funds in addition to other programmes which were in place.

Table 52. Assumptions for the MFA third-tranche counterfactual scenario

Variable	Assumptions
Government revenue	Government revenues are not directly affected by the availability of MFA third tranche.
Government expenditure	Government expenditure is not affected by the availability of MFA third tranche.
Public debt	The availability of third tranche initially reduces domestic borrowing by EUR 600 million. The conditions underpinning forgone domestic borrowing are similar to these obtained by Ukraine in December 2017 on its USD-denominated issuance: Maturity 1.5 years Interest rate: 4.0% The conditions underpinning the third tranche are the same as these offered by the second tranche: Maturity: 14 years Interest rate: 0.75%
Gross financing needs	The gross financing needs remain nearly unchanged in the first 1.5 years.
GDP	• No change to GDP.
Inflation	Inflation remains unchanged.
Exchange rate	The UAH/USD exchange rate also remains unchanged.

Table 52 outlines the key scenario assumptions associated with the "MFA third-tranche" counterfactual scenario.

Following the same reasoning as Alternative 2, the addition of third-tranche funding is unlikely to have resulted in any material differences in fiscal policy. Instead, the additional budgetary support would likely have meant slightly lower domestic financing, but limited policy impacts on social outcomes for households.

With regard to conditionalities, some stakeholders have expressed the view that the cancellation of the third tranche was important "from a credibility point of view". Thus, Alternative 3 might have resulted in a deterioration of the credibility of MFA conditionalities. The credibility impacts associated with this would only be felt in future MFA operations (beyond the scope of this analysis). However, the wider credibility impacts should be acknowledged.

Another consideration for Alternative 3 is the fulfilment of third-tranche MFA conditionalities. Specifically, if all MFA conditionalities are assumed to be fulfilled under Alternative 3 (as MFA funds are disbursed), there is a question of how this would have affected the social situation. On balance, it is unlikely that any material change in the social situation would have resulted from fulfilment of MFA conditionalities because the main conditions relating to the social situation of Ukraine (Social safety nets and IDPs) were already fulfilled.

A10.3.4 Alternative 4: no MFA, no IMF scenario

Under the no MFA, no IMF scenario Ukraine would not have received the rescue packages provided by the EU and the IMF. The total amount of funding provided by these two rescue packages over 2015-17 amounted to approximately EUR 8.9 billion. Due to political and legal constraints, cuts to public spending and increases in government revenues would either have been infeasible or insufficient to cover the gap in budgetary support[362]. It is also extremely unlikely that Ukraine would have been able to obtain sufficient financing from other bi-lateral/multi-lateral sources.

For these reasons, under this scenario, the expert view is that Ukraine would have defaulted on its debts. This is likely to have created a sovereign debt crisis, exacerbating the current instability stemming from the conflict in the east and destabilising the economy. Historically, sovereign debt crises are often associated with economic recession, increased rates of unemployment (sometimes sustained in the medium term), high levels of inflation and cuts to public services and wages[363]. These factors all typically have the effect of deteriorating the living conditions of households, living through the crisis.

However, while the impacts of sovereign default could plausibly have been negative and far-reaching, there are considerable identification issues[364] which limit the causal inferences which can be drawn from past cases of sovereign debt default. Namely, it is exceptionally difficult to untangle the economic crisis which caused the default from the economic crisis that results from it.

The effects of the crisis are also shaped considerably by the economic context of the country, the context of the time and the policy response of the country. For instance, sovereign debt default by the Russian Federation in 1998 differed considerably from the Greek experience of the Eurozone crisis. The Russian crisis involved high inflation (19% and 72% in 1998 and 1999) and a short sharp recession, whereas the Greek debt crisis

[362] According to experts, nearly all politically feasible options to tighten the budget have been exhausted during the 2015 consolidation, which included increases in excise and income tax rates, freezes to wages, surcharges on imports and cuts to state aid (including support for Naftogaz).

[363] This is based on the experiences of Mediterranean economies during the Eurozone debt crisis (2009-2012), Argentina during the debt crisis of 2001-2002, Ecuador following the default of the 2012 and 2030 Global Bonds (2008-2009) and the Russian debt default of 1998.

[364] Yeyati, Eduardo Levy, and Ugo Panizza. (2011) "The elusive costs of sovereign defaults." Journal of Development Economics.

involved only moderate inflation but was followed by sustained issues with unemployment and GDP growth.

Annex 11 Debt Sustainability Analysis (DSA)

A11.1 Introduction

The objective of this debt sustainability analysis (DSA) is to evaluate the contribution of the EU's macro-financial assistance (MFA) III operation (2015-17) towards the sustainability of Ukraine's public debt. DSA relies on modelling the key debt burden indicators and macroeconomic variables which affect the path of a country's debt and its capacity to manage its debt sustainably.

Technically, a government is solvent if its future primary balances when discounted to their present value are at least as large as its public debt stock. Therefore, analysing a country's ability to service its public debt offers us a starting point to determine whether its debt is sustainable.

The ability to service debt is reflected in the dynamics of debt-burden indicators which show a debtor's solvency and liquidity profile relative to data-based benchmarks. For Ukraine, the analysis is focused on two debt burden indicators:

- the debt-to-GDP ratio, and
- the gross financing need-to-GDP ratio.

According to the IMF and as a country with access to international financial markets, once Ukraine's debt burden breaches its pre-set benchmark, the risk to its debt sustainability increases with the level of indebtedness.

By comparing how these indicators responded to the MFA operation (the baseline case) against how they would have evolved under different scenarios, we can identify the effect of the MFA programme on the sustainability of Ukraine's debt.

MFA is provided as a general-purpose budgetary support, and therefore there is no precise information on how the funding was spent when disbursed, or how it would have been spent had it been granted. To this end, it can be argued that the MFA component that went towards government spending potentially improved Ukrainian debt sustainability by providing it with financing and liquidity in the first instance. In addition, MFA can also provide savings on the cost of borrowing as the interest rates underpinning MFA lending tend to be much lower compared to interest rates offered by international and domestic financial markets, thus limiting the accumulation of debt.

The increase in (or maintaining of) government spending through the MFA operation may also have contributed towards stabilising and growing the Ukrainian economy, which tends to have a positive impact on debt sustainability.

This analysis focusses on both of these issues and the broader performance of the Ukrainian economy as part of the review of the MFA's impact.

A11.2 The EU MFA and IMF programmes

Following the completion of MFA I and MFA II operations in early 2015, the MFA III package was agreed to help alleviate Ukraine's large external financing needs, as the economic situation of the country was deteriorating. The MFA III loan facility of EUR 1.8 billion was agreed in July 2015 and was composed of three tranches:

- first tranche of EUR 600 million disbursed in July 2015,
- second tranche of EUR 600 million disbursed in April 2017, and
- third tranche of EUR 600 million undisbursed and expired on the 13th of January 2018.

Concurrent to the MFA III operation, the IMF provided its own assistance under its four-year Extended Fund Facility (EFF) arrangement of approximately USD 8.5 bn disbursed between March 2015 and April 2017.

These rescue packages jointly provided budgetary support, likely as an alternative to other sources of finance or cuts to public spending. In addition, the EU's and the IMF's assistance signalled support and confidence in the Ukrainian government's ability to manage the crisis and conduct the economic reforms. This in turn improved investors' confidence in the economy. Due to the similarities between the EU and the IMF assistance to Ukraine, this analysis will reference the IMF rescue package while keeping the focus on the EU's MFA operation.

A11.3 Final assessment of the debt sustainability

Our approach to assess the contribution of the EU's MFA III towards the sustainability of Ukraine's public debt relies on counterfactual analysis where the possible paths of the debt-burden indicators listed above are evaluated and compared across different scenarios, designed to show:

- what happened (the baseline scenario),
- what would have happened without the MFA III first tranche but with the IMF assistance in place (Alternative 1: no MFA first-tranche scenario), and
- what would have happened without the MFA III second tranche but with the IMF assistance in place (Alternative 2: no MFA second-tranche scenario), and
- what would have happened had MFA III third tranche been disbursed, with the IMF assistance in place (Alternative 3: MFA third-tranche scenario), and
- what would have happened in the absence of MFA III and without the IMF assistance (Alternative 4: No MFA, no IMF scenario).

Comparing debt sustainability indicators across these scenarios allows us to consider the impact of each tranche of MFA funding on the sustainability of Ukraine's public debt, as well as the joint impact of the MFA and IMF assistance.

A11.4 What happened under the baseline scenario

The baseline scenario is the actual state and can be informed by observable data. However, in instances where data are missing, the analysis relies on approximations and projections.

Whenever possible these approximations draw on data from official and recognised sources such as the IMF and the World Bank, as well as from Ukraine's National Bank and Ukraine's Ministry of Finance.

Table 53presents the key macroeconomic indicators describing Ukraine's economy over 2004-2017.

Key developments over 2004-2017 include the rapid economic contraction in 2014 and 2015, with real GDP in these years declining by 6.6% and 9.8%, respectively. GDP growth recovered to around 2.5% per annum in 2016 and 2017, a touch slower than the average rate of growth over 2004-12.

In response to the conflict and the abandoning of the peg between the Hryvnia and the Dollar, the Hryvnia lost nearly 70% of its value between 2013 and 2017, falling steadily from 8 UAH to the Dollar in 2013 to nearly 27 UAH to the Dollar in 2017.

Inflation increased from 4.3% in 2013 to 15.9% in 2014 and peaked at 38.9% in 2015. Inflation moderated to 17.1% in 2016 before picking up again to 22.0% in 2017.

Table 53. Assumptions for the baseline scenario - macroeconomic variables

	2004 - 2012 [1]	2013	2014	2015	2016	2017
Real GDP growth (in percent)	3.1	0.0	-6.6	-9.8	2.4	2.5
Inflation (GDP deflator, in percent)	17.2	4.3	15.9	38.9	17.1	22.0
Nominal exchange rate (Ukrainian Hryvnia per US dollar)	6.4	8.0	11.9	21.8	25.6	26.6

Notes: 2004-2012 values represent average for the period.
Sources: IMF World Economic Outlook database and IMF International Financial Statistics.

These developments weighed on the values of debt sustainability indicators presented in Table 54. Debt indicators are presented for the average over 2004-2012, 2013 and 2014. For 2015, 2016 and 2017 the presented values are projections modelled using the approximate data on Ukraine's debt profile and sources of finance over that period. The debt profile reported in the analysis is based on a calculation of old debt minus principal payments and new debt converted to Ukraine Hryvnia as part of the DSA framework. As a result of these approximations and the way that the debt indicator is derived, the projected values for indicators in 2015, 2016 and 2017 may depart from the historical values reported in statistical publications.

The nominal gross public debt increased from 40.8% of the GDP in 2013 to 70.5% in 2014, largely as a result of the depreciation of the Ukrainian Hryvnia. The projections for years 2015 and 2016 show the ratio increasing to 79.8% and 81.9% respectively. In 2017 the ratio was projected to decline to 72.8% as a result of primary surplus and growth in Ukraine's GDP. According to the IMF guidelines[365], a debt-to-GDP ratio of above 50% for emerging markets like Ukraine implies heightened risk and warrants higher levels of scrutiny to assess debt sustainability.

Similarly, public gross financing needs-to-GDP ratio increased rapidly as a result of an increased cost of servicing public debt. Public gross financing needs stood at 6.0% (of GDP) in 2014. In the baseline scenario projections show gross financing needs-to-GDP ratio increasing to 12.5% in 2015. Despite debt restructuring in 2015[366], the ratio subsequently increased to 13.3% in 2016 due to UAH 121 billion financing required for recapitalisation of banks. Subsequently, in 2017 gross financing needs decreased to 9.4% in 2017.

In the years prior to 2015, the Ukrainian government ran small primary deficits. Restructuring of public finances and cuts to expenditures over 2015-2017 resulted in substantial primary surpluses, estimated at 3.0% of GDP in 2015, 1.9% in 2016 and 1.6% in 2017.

[365] IMF, 2013. Staff Guidance Note for Public Debt Sustainability Analysis in Market Access Countries. Available at: https://www.imf.org/external/np/pp/eng/2013/050913.pdf

[366] IMF, "IMF Country Report No. 16/319", (https://www.imf.org/external/pubs/ft/scr/2016/cr16319.pdf)

Table 54. Assumptions for the baseline scenario – debt indicators

	Actual			Projections		
	2004 - 2012	2013	2014	2015	2016	2017
Nominal gross public debt (percent of GDP)	27.2	40.8	70.5	79.8	81.9	72.8
Public gross financing needs (percent of GDP)	4.1	6.7	6.0	12.5	12.9	9.4
Primary deficit (percent of GDP)	0.3	0.7	0.3	-3.0	-1.9	-1.6

Notes: Debt indicators are based on the general government definition. 2004-2012 values represent average for the period.
Sources: IMF and CE projections based on IMF data and other sources.

A11.5 Alternative 1: no MFA first tranche scenario

Under the Alternative 1 scenario Ukraine would not have received the first MFA tranche of EUR 600 million in July 2015. Our assumptions on what would have happened in the absence of the first tranche are based on insights obtained through stakeholder consultations, desk research and insights shared by local economic experts.

Consultations included experts from institutions such as the National Bank of Ukraine (NBU), the Ministry of Finance, the Ministry of Economy, the IMF, the World Bank and the European Bank for Reconstruction and Development. As some of these experts were directly involved in negotiation and implementation of the support packages provided to Ukraine, their account of the situation in Ukraine and the choices faced by the government provide an insight of what would likely have happened in the absence of the MFA first tranche.

As the MFA III first tranche was disbursed in 2015, the analysis also relies on evidence gathered during the evaluation of the MFA I and MFA II packages, which focused on years 2014-2017.

The available evidence suggests that if the first tranche had not been disbursed the government's response would likely have involved cuts to government expenditure in the areas of:

- Cuts to pension payments (in real terms) to the amount equivalent to EUR 150 million;
- Cuts to public procurement of approximately EUR 450 million. These could include cuts to public services and cuts to any capital expenditures such as investments in infrastructure.

Section 6.2 provides more details on the rationale behind the selection of these two types of cuts (instead of other hypothetical responses by the government).

The assumptions of impacts on the key variables under no MFA first-tranche scenario are outlined in Table 55.

Table 55. Assumptions for the no MFA first-tranche scenario

Variable	Assumptions
Government revenue	Government revenues which are mainly taxes are not directly affected by the absence of MFA's first tranche[367].
Government expenditure	Government introduces cuts to spending in 2015 to the equivalent of EUR 600 m. Spending is reduced in the areas of: • EUR 150 million cut to pensions (in real terms) • EUR 450 million cuts to public procurement, including cuts to public services and cuts to any remaining capital expenditures such as infrastructure spending
Public debt	Ukraine does not obtain MFA III first tranche financing. Public borrowing in 2015 is reduced by the equivalent of EUR 600 m (UAH 16 bn).
Gross financing needs	The gross financing need changes in line with the cuts to government expenditures.
GDP	GDP decreases due to cuts to public spending. The declines estimated using fiscal multiplier analysis are estimated at: • 2015: UAH 11.1 bn (2010 prices), equivalent to 1.2% of GDP • 2016: UAH 11.1 bn (2010 prices), equivalent to 1.1% of GDP
Inflation	Inflation remains unchanged.
Exchange rate	The UAH/USD exchange rate also remains unchanged based on the assumption that the presence of other donors in Ukraine, notably the IMF, cushions Hryvnia from the negative impact of not having received the first MFA tranche.

Declines in public spending would have resulted in a dip in aggregate demand and further spillover effects throughout the Ukrainian economy. Based on fiscal multiplier analysis[368], these public spending cuts would have resulted in a decline in Ukrainian GDP by EUR 860 million in 2015 (UAH 11.1 billion, 2010 prices) and a further EUR 860 million in 2016[369], giving the cumulative impact of approximately EUR 1.7 billion over these two years.

It is unlikely that at that time Ukraine would have been able to issue new foreign and domestic debt due to its precarious circumstances and weakened banking sector after the

[367] While government revenues could potentially decrease as a consequence of declining GDP, due to a lack of data, the potential impact on government revenues could not be reliably modelled. Most likely the impact would have been relatively small and unlikely to significantly affect debt indicators.

[368] Fiscal multipliers were obtained from the IMF study 'Fiscal Multipliers in Ukraine', March 2015, (https://www.imf.org/en/Publications/WP/Issues/2016/12/31/Fiscal-Multipliers-in-Ukraine-42815)

[369] Roughly equivalent to just over 1% of GDP at constant prices in 2015 and 2016.

2014 crisis and series of bankruptcies of local credit institutions (for more details see Section 6.2). Consequently, we estimate debt-burden indicators that would have resulted from this decline in GDP, assuming the absence of MFA III first-tranche funds leaves unchanged other factors such as the exchange rates, inflation and government revenues, variables which can impact debt dynamics and debt sustainability.

A11.6 Alternative 2: no MFA second-tranche scenario

Under the Alternative 2 scenario Ukraine would not have received the second MFA tranche of EUR 600 million in April 2017. Based on cross examination of the evidence obtained through desk research, stakeholder interviews, the Delphi survey and views shared by local economic experts the absence of the second tranche would have resulted in additional domestic borrowing to fill the financing gap in absence of the second tranche. Table 56 describes in detail the key assumptions of the counterfactual.

Table 56. Assumptions for the no MFA second-tranche scenario

Variable	Assumptions
Government revenue	Government revenues are not affected by the absence of MFA's second tranche
Government expenditure	• Government expenditure is not affected by the absence of MFA's second tranche.
Public debt	The lack of MFA III second-tranche financing is initially offset by increased domestic borrowing to the full amount of EUR 600 million. The conditions underpinning domestic borrowing are similar to these obtained by Ukraine in December 2017 on its USD-denominated issuance: Maturity 1.5 years Interest rate: 4.0%
Gross financing needs	The gross financing needs remain nearly unchanged in the first 1.5 years.
GDP	• No change to GDP.
Inflation	Inflation remains unchanged.
Exchange rate	The UAH/USD exchange rate also remains unchanged based on the assumption that the presence of other donors in Ukraine, notably the IMF, cushions Hryvnia from the negative impact of not having received the second MFA tranche.

At the time when the second tranche was disbursed Ukraine was able to access domestic financial markets. However, the terms of lending would likely have been different to those offered by the MFA second tranche. The interest rate on short-term borrowing to fill the gap is assumed at 4% - the rate on Ukraine's USD-denominated domestic issuance in December 2017. This rate reflects a much higher cost of borrowing compared to the baseline scenario, as the second MFA tranche was offered at a 0.75% interest rate (irrespective of the longer maturity of the MFA loan).

The financing gap due to the lack of the second tranche would likely have been covered initially by short-term borrowing, which for the counterfactual scenario is assumed to mature at 1.5 years – the same term obtained in the December 2017 domestic debt issuance. Therefore, the financing needs would have remained nearly unchanged during the MFA III operation apart from the difference in interest payments (discussed in detail in Section A11.12).

As the Ukrainian economy was comparatively more stable in 2017 than in 2014, it is unlikely that the lack of the second tranche would have impacted other macro-economic variables such as the GDP, inflation rate or exchange rate.

A11.7 Alternative 3: MFA third-tranche scenario

Under the Alternative 3 scenario Ukraine would have received the third MFA tranche of EUR 600 million in the second half of 2017. The Alternative 3 scenario is therefore different to the other counterfactual scenarios in that it assumes presence of additional MFA financing, rather than its absence. The examined evidence discussed in detail under section 6.2 suggests that had the third tranche been available, Ukraine would have decreased its domestic financing by the full amount of EUR 600 million that the MFA third tranche would have provided. Table 57 describes in detail the key assumptions of the counterfactual.

Table 57. Assumptions for the MFA third-tranche scenario

Variable	Assumptions
Government revenue	Government revenues are not affected by the availability of MFA third tranche.
Government expenditure	• Government expenditure is not affected by the availability of the MFA third tranche.
Public debt	The availability of the third tranche initially reduces domestic borrowing by EUR 600 million. The conditions underpinning forgone domestic borrowing are similar to these obtained by Ukraine in December 2017 on its USD-denominated issuance: Maturity 1.5 years Interest rate: 4.0% The conditions underpinning the third tranche are the same as those offered by the second tranche: Maturity: 14 years Interest rate: 0.75%
Gross financing needs	The gross financing needs remain nearly unchanged in the first 1.5 years.

GDP	• No change to GDP.
Inflation	Inflation remains unchanged.
Exchange rate	The UAH/USD exchange rate also remains unchanged.

The evidence indicates that Ukraine obtained financing from domestic markets as a direct replacement of the third MFA tranche. Had the third tranche been disbursed, Ukraine would likely have reduced its domestic borrowing. Therefore, the assumptions underpinning the Alternative 3 scenario are effectively the opposite of these described for the Alternative 2 scenario.

The third tranche would have likely replaced the December 2017 domestic issuance. The hypothetical terms underpinning the MFA third tranche are assumed to be the same as for the second tranche, at 0.75% interest rate and 14 year maturity.

Similar to the Alternative 2 scenario, the gross financing needs would remain nearly unchanged in the first 1.5 years, with only a small difference occurring due to the difference in interest payments, which are further discussed in Section A11.13.

As in the Alternative 2 scenario, no other macro-economic impacts are assumed on other key variables such as GDP, inflation or the exchange rate.

A11.8 Alternative 4: no MFA, no IMF funding scenario

Under the no MFA, no IMF scenario Ukraine would not have received the rescue packages provided by the EU and the IMF. The total amount of funding provided by these two rescue packages in years 2015 to 2017 amounted to approximately EUR 8.9 billion.

However, it is assessed that the lack of support from the EU and the IMF could have had additional effects:

- Joint support of the EU and the IMF served as a signal and boosted investor confidence in Ukraine's ability to fulfil its obligations to creditors. Expert interviews suggest that September 2017 Eurobonds issuance of USD 3 billion would not have been possible if the EU's and the IMF's support did not boost investors' confidence. It is likely that further funds from sources such as the World Bank and the European Bank for Reconstruction and Development (EBRD) as well as bilateral assistance from individual countries were crowded-in thanks to the support provided by the EU and the IMF. So, with no support from the EU and the IMF funds from these other sources would not have been available.
- Similarly, the support from the EU and the IMF provided backing to the government as it attempted to introduce reforms aimed at restoring Ukraine's financial soundness. As a number of these reforms were linked to conditionalities associated with the financial packages, it is likely that some of these reforms would not have been achieved under the no MFA, no IMF scenario. This would have had a negative impact on Ukraine's finances, likely increasing its debt burden.

At the same time, very limited cuts to public spending would have been politically feasible but unlikely to compensate for the full amount of lost funding from the EU, the IMF, as well as what was crowded-in. Similarly, it would not have been politically feasible to increase government revenues. According to experts, nearly all politically feasible options to tighten the budget had been exhausted during the 2015 consolidation, which included increases in excise and income tax rates, freezes to wages, surcharges on imports and cuts to state aid (including reduced support for Naftogaz) – most as part of the consolidation effort prescribed in the IMF program back in the time

These considerations form the key assumption of the counterfactual. Under these assumptions, the expert view, in conjunction with analysis of published data, suggest that Ukraine would have defaulted on its debts. It is extremely unlikely that Ukraine would have been able to obtain financing from other sources that was close to the amount provided jointly by the EU and the IMF to meet its obligations to creditors, resulting in a default in 2015 or in early 2016.

Sovereign default is the ultimate result of unsustainable debt. Further evaluation of the impacts of the default on Ukraine's economy would be purely speculative due to the level of uncertainty. Therefore, the scenario has not been analysed using the DSA framework further.

A11.9 Methodology and data underpinning debt sustainability analysis

To analyse the sustainability of Ukraine's public debt, we use a debt sustainability analysis tool for countries that can access international financial markets. This tool was developed by the IMF and the World Bank and is among the benchmark tools for DSAs.

The DSA tool was used to generate short-term and medium-term projections of the dynamics for debt sustainability indicators (the debt-to-GDP ratio and the gross financing need-to-GDP ratio) for years 2015-2017.

The DSA tool takes as inputs historical data on key macroeconomic and financial variables which impact debt dynamics, such as GDP, government debt, government gross financing needs, government spending, government revenues, exchange rates, and inflation. From these variables, forecasts are generated for debt stock and financing needs which are then used to calculate debt sustainability indicators. Comparing the tool's outputs across the different scenarios helps to determine the MFA's effect on debt sustainability.

Inputs to the DSA tool for the baseline scenario are based on past observations of variables from sources such as the IMF, the National Bank of Ukraine, Ukraine's Ministry of Finance, and others. In certain cases where data are not available, approximate values were derived using multiple imputation methods.

Inputs to the DSA tool for the counterfactual scenarios are constructed in line with the assumptions listed above which are based on a combination of economic theory and logic, financial market data, IMF reports on Ukraine and insights from stakeholder interviews and feedback provided by the local economic experts.

Determining the path of these variables under these alternative scenarios is not straightforward, in part because of the limited information available on the most likely counterfactuals. The analysis focuses on movements in key variables such as GDP, inflation, exchange rates, government revenues and expenditures, and risk premia near the time when the MFA and IMF funding were approved or disbursed. For example, assuming financial markets would price in the approval of a large financial rescue package, a fall (or slowdown in the rate of increase) of government bond yields would reflect (part of) the MFA's impact on government debt sustainability.

Data

We have tried as much as possible to use IMF data for consistency, but in some cases, we have drawn on other sources where more detail was required, or the data were not published by the IMF. In the case of IMF data, the main sources were the World Economic Outlook (WEO), International Financial Statistics (IFS), Government Finance

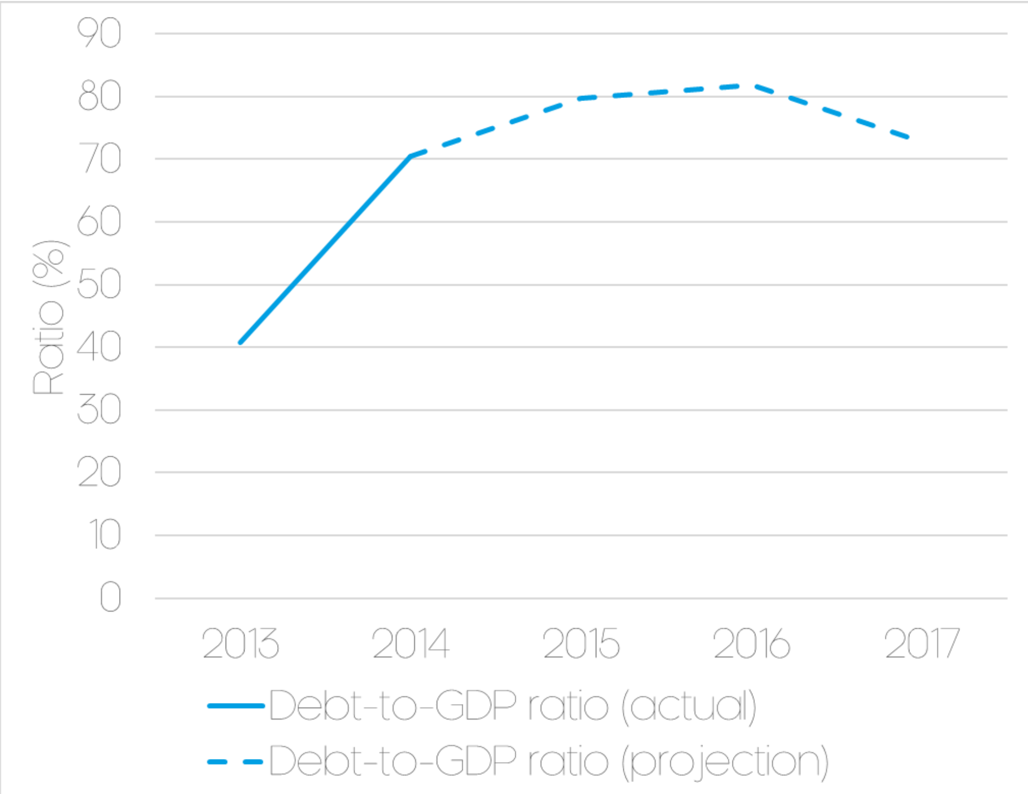
Statistics (GFS) data as well as IMF reports on Ukraine. We have also used data from the National Bank of Ukraine (NBU) and from the Ukrainian Ministry of Finance.

A11.10 Debt sustainability in the baseline scenario

Against the economic backdrop described in Section A11.4, public sector debt expressed as a percentage of GDP (debt-to-GDP ratio) increased rapidly between 2013 and 2015, as shown in Figure 31. The ratio stood at 40.8% in 2013 and subsequently increased to 70.5% in 2014. The projections based on Ukraine's financing needs, historical debt profile and financing obtained in years 2015 onwards estimate an increase in the debt-to-GDP ratio to 79.8% in 2015 and 81.9% in 2016, before a subsequent decline in 2017 to 72.8%.

Such a rapid increase in the debt-to-GDP ratio was in particular driven by the depreciation of the Hryvnia, as approximately 62% of Ukraine's public debt was denominated in foreign currencies in 2014. As the Hryvnia depreciated against the Dollar by 33% in 2014 and by a further 46% in 2015, the relative size of the foreign-currency denominated liabilities to Ukraine's shrinking GDP increased.

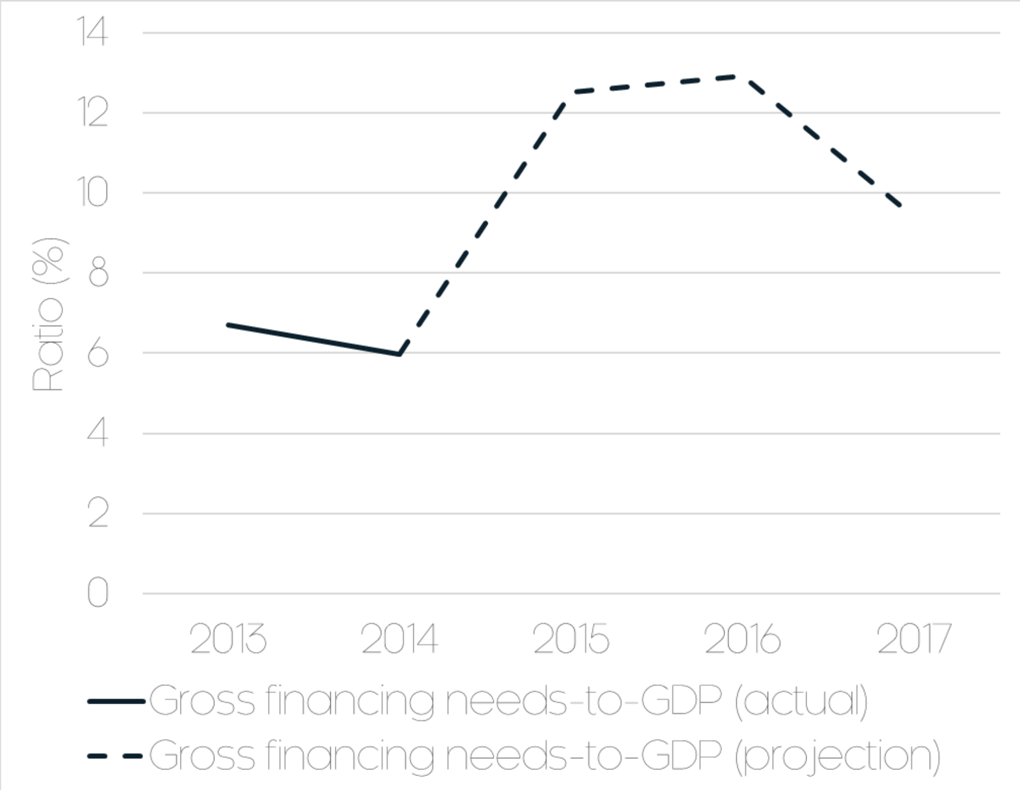
Figure 31. Debt-to-GDP ratio in the baseline scenario



Sources: IMF data and CE projections based on IMF data and other sources.

The public gross financing needs relative to GDP were also impacted in 2015-2017, as shown in Figure 32. Public gross financing needs-to-GDP ratio stood at 6.7% in 2013 and 6.0% in 2014. The projections show that in the baseline scenario the gross financing needs-to-GDP ratio increased to 12.5% in 2015, primarily as a result of depreciation of the Hryvnia. The ratio subsequently increased further to 12.9% in 2016 as a result of increased financing needs related to resolutions and recapitalisations in the banking sector. By 2017, the financing needs declined to 9.4% of the GDP.

Figure 32. Gross financing needs-to-GDP ratio in the baseline scenario



Sources: IMF data and CE projections based on IMF data and other sources.

While Ukraine's debt surpassed the higher scrutiny benchmark for the debt-to-GDP ratio (50%) and its financing needs nearly doubled compared to its GDP over 2015-2017, Ukraine was able to fulfil its obligations to creditors. The risk likely peaked in 2015 and 2016, coinciding also with the most severe stages of the conflict in East Ukraine.

During that period, the ability of Ukraine to access financial markets in an event of any additional shock was severely impaired. Following a series of credit downgrades, the yields on credit default swaps linked to Ukraine's debt peaked in February 2016[370]. This reflects the market's perception of a high risk of Ukraine defaulting during that period. Also, the crisis in the domestic banking sector between 2013 and 2016 limited the ability to absorb additional public debt by the domestic banks, and indeed, 2015 and 2016 saw multiple unsuccessful domestic debt issuances[371].

However, in 2017 the risk to debt sustainability moderated thanks to over improvement of the economy and the stabilisation of the situation in the East. Thanks to the USD 3 billion issuance in September 2017 at 7.4 percent interest, Ukraine was able to restructure part of its external debt and cover its financing needs. As the September 2017 issuance was reported to be oversubscribed[372], this suggests potentially sufficient appetite among international investors for more debt issued by Ukraine had Treasury

[370] World Government Bonds, "Ukraine 5 Years CDS - Historical Data". (http://www.worldgovernmentbonds.com/cds-historical-data/ukraine/5-years/)

[371] World Bank, "Ukraine: Building the domestic debt market for local currency issuances". (https://www.worldbank.org/en/news/feature/2019/11/04/ukraine-building-the-domestic-debt-market-for-local-currency-issuances)

[372] Financial Times, "Ukraine prices USD 3 bln bond deal at 7.375%". (https://www.ft.com/content/d227d1b0-49c2-361a-8279-9c66c62e1783)

decided to do so. It is therefore likely that Ukraine would have been able to raise additional financing in 2017 to accommodate any potential negative shocks.

The debt trajectory therefore appears sustainable, with the debt-to-GDP and the gross financing needs-to-GDP ratios declining in 2017. While the gross financing needs ratio was the highest in 2016, at 12.9%, its value did not surpass the IMF's 15% threshold, a threshold which would have implied high risk and signalled the need for greater scrutiny (although the debt-to-GDP ratio of over 50% signalled the need for greater scrutiny regardless).

A11.11 Debt sustainability in the absence of the MFA first tranche (Alternative 1)

This section provides the analysis of Ukraine's debt sustainability in the Alternative 1 scenario described in more detail in Section A11.5. According to the scenario assumptions, EUR 600 million of financing provided by MFA first tranche is assumed unavailable and in response the government introduces cuts to public spending of an equivalent amount in the areas of public procurement and pensions.

The wider economic impacts of cuts to public spending on Ukraine's GDP are modelled using fiscal multipliers[373]. The impact of these declines on GDP growth rates is presented in Table 58. According to the analysis, the GDP would have declined by the equivalent of EUR 860 million in 2015 (approx. UAH 11.1 billion, 2010 prices), and by the same amount in 2016. This is equivalent to an aggregate decline in Ukrainian GDP of approximately 1% in both 2015 and 2016.

Table 58. Real GDP and GDP growth in the Baseline and Alternative 1 scenarios

	Actual		Projections		
	2013	2014	2015	2016	2017
Real GDP - Baseline (UAH billions, 2010 prices)	1,140.8	1,066.0	961.8	985.3	1,010.2
Real GDP - Alternative 1 (UAH billions, 2010 prices)	1,140.8	1,066.0	950.8	974.2	1,010.2
Real GDP growth - Baseline (in percent)	0.0	-6.6	-9.8	2.4	2.5
Real GDP growth - Alternative 1 (in percent)	0.0	-6.6	-10.8	2.5	3.7

Sources: IMF and CE projections based on IMF data and other sources.

Table 59 presents the comparison of the key debt indicators for the Baseline scenario and the Alternative 1 scenario. In line with the government cuts assumed in Alternative 1, the primary surplus increases to 3.9% in 2015, compared to 3.0% in the Baseline.

[373] Fiscal multipliers were obtained from the IMF study "Fiscal Multipliers in Ukraine". (https://www.imf.org/en/Publications/WP/Issues/2016/12/31/Fiscal-Multipliers-in-Ukraine-42815)

The trajectory of the debt-to-GDP ratio under Alternative 1 scenario is slightly different compared to the Baseline. While in 2015 and 2016, the debt-to-GDP ratio is projected to be 0.1 pp higher in the Alternative 1 scenario against the Baseline, it is projected to be lower in 2017 (by 0.7 pp). This trajectory stems from the combined effect of lower GDP in 2015 and 2016 and lower financing needs in 2015 under Alternative 1 scenario.

Due to the cuts to government spending, gross financing needs in 2015 under Alternative 1 are projected to be lower, at 11.8% (of GDP), compared to 12.5% projected under the Baseline (equivalent to EUR 600 million covered by the MFA first tranche). As no cuts to spending are assumed in 2016 and 2017, financing needs remain virtually unchanged for these two years, with the difference close to 0.1 pp.

Table 59. Debt sustainability indicators in the Baseline and Alternative 1 scenarios

	Actual		Projections		
	2013	2014	2015	2016	2017
Primary deficit - Baseline (percent of GDP)	0.7	0.3	-3.0	-1.9	-1.6
Primary deficit - Alternative 1 (percent of GDP)	0.7	0.3	-3.9	-1.9	-1.6
Nominal gross public debt - Baseline (percent of GDP)	40.8	70.5	79.8	81.9	72.8
Nominal gross public debt - Alternative 1 (percent of GDP)	40.8	70.5	79.9	82.0	72.1
Public gross financing needs - Baseline (percent of GDP)	6.7	6.0	12.5	12.9	9.4
Public gross financing needs - Alternative 1 (percent of GDP)	6.7	6.0	11.8	13.0	9.3

Sources: IMF and CE projections based on IMF data and other sources.

Overall, the comparison of the key debt sustainability indicators suggests that had Ukraine not received the MFA first tranche, the risk to debt sustainability would have remained relatively unchanged compared to the baseline scenario. Public spending cuts would have been possible to compensate for lack of the MFA first tranche. The impact of such cuts would have had a small positive effect on Ukraine's debt sustainability indicators in 2017 compared to the Baseline. It is important to note, however, that these cuts would have been politically very difficult, and the scope for any further cuts would have been very limited.

In addition, fiscal multiplier analysis only considers a limited set of channels through which Ukraine's GDP is being affected by cuts to public spending, and over a short time frame. A lack of public spending (on infrastructure investment for example) could negatively affect productivity in the long run, leading to an even greater negative impact on GDP and sustainability indicators. At the same time lower GDP is likely to result in lower tax receipts, decreasing the government's primary balance and increasing financing needs. The impacts of these channels could not be modelled due to their longer term nature and/or a lack of data and uncertainty over where precisely cuts to public spending would have been made under the Alternative 1 scenario.

A11.12 Debt sustainability in the absence of the MFA second tranche (Alternative 2)

This section provides the analysis of Ukraine's debt sustainability in the Alternative 2 scenario described in more detail in Section A11.6. According to the scenario assumptions, the financing gap due to absence of the MFA III second tranche is initially covered by short-term USD-denominated domestic financing.

The calculations presented in Table 60 show how the difference in the interest rates between the MFA III second tranche (0.75% p.a.) and the assumed alternative domestic financing interest rate (4.00% p.a.) would have led to approximately EUR 29.3 million greater interest payments over the 1.5 years in the Alternative 2 scenario.

Table 60. Comparison of borrowing terms - MFA III second tranche (baseline) and alternative domestic financing

	Interest Rate	Amount (EUR millions)	Approximate cost of interest payments over 1.5 years (EUR millions)[1]
Baseline: MFA III second tranche	0.75%	600.0	6.8
Alternative 2: domestic financing	4.00%	600.0	36.0
Difference: Alternative 2 less baseline	3.25pp	0.0	29.3

Notes: Calculations exclude the compounding cost of interest payments.
Sources: CE calculations.

In line with these calculations, it is assessed that the key debt sustainability indicators would have remained nearly unchanged in the period of the MFA III operation up to 2018. The increased interest payments would have a limited impact on the key debt sustainability indicators. For example, the gross financing needs in 2017 stood at approximately EUR 9 billion, while the total debt amounted to EUR 69 billion. Therefore, given the difference in the interest payments of EUR 29.3 million, the debt-to-GDP and the gross financing needs ratios would remain nearly identical to these outlined in the baseline scenario, and overall the sustainability of Ukrainian debt would have been unaffected.

However, given that the second tranche was issued with a maturity of 14 years, Ukraine would likely need to seek alternative long-term financing to roll over the short-term domestic issuance upon its maturity after 1.5 years. This would not have impacted Ukraine's debt sustainability, as at the time Ukraine was able to access international capital markets, with successful issuances in 2018[374] and 2019[375]. However, the long-term debt issuance would likely be priced at a higher interest rate compared to that offered by the second tranche. Therefore, the potential cost of additional interest

[374] 'Ukraine: New Eurobonds issue', ICU 2018 (https://icu.ua/download/2870/ICUDebtInsight-20181030-Eng.pdf)

[375] 'Ukraine successfully sells 1 billion euros worth of Eurobonds', Kyiv Post, 14th of June 2019. (https://www.kyivpost.com/business-focus/ukraine-successfully-sold-1-billion-euros-worth-of-eurobonds.html#:~:text=Ukraine%20has%20issued%201%20billion,a%20seven%2Dyear%20maturity%20period)

payments would have been much higher over the entire 14 year period covered by the MFA second tranche.

For example, if Ukraine obtained alternative long-term financing on terms similar to those obtained during the September 2017 Eurobonds issuance[376], the amount of additional interest payments in the Alternative 2 scenario over the entire 14 year term would be approximately EUR 524 million higher compared to the baseline (inclusive of the EUR 29.3 million increase in interest in the first 1.5 years)[377].

A11.13 Debt sustainability in the presence of the MFA third tranche (Alternative 3)

As described in Section A11.7, the MFA third-tranche scenario differs from other counterfactual scenarios in that it assumes presence of additional MFA funding compared to the baseline, rather than its absence.

According to feedback from the interviews collected during the evaluation, the financing gap was filled through domestic issuance in December 2017 as it became evident that the third tranche will not be available. Therefore, the Alternative 3 scenario would have likely the opposite effect to that assumed for Alternative 2 scenario, with Ukraine reducing its domestic borrowing in 2017 by the equivalent of EUR 600 million.

Table 61 presents the difference in the terms of borrowing between domestic financing obtained in December 2017 (baseline scenario) and the likely terms offered by the third MFA tranche (Alternative 3 scenario). The difference in the interest rate, at -3.25 percentage points would have resulted in lower interest payments had the third tranche been available. Over the term for which domestic financing was obtained as a direct replacement of the third tranche (1.5 years), the interest payments would have been lower by EUR 29.3 million under the Alternative 3 scenario compared to the baseline scenario.

Table 61. Comparison of borrowing terms - domestic financing (baseline) and alternative MFA third tranche

	Interest Rate	Amount (EUR millions)	Approximate cost of interest payments over 1.5 years (EUR millions)[1]
Baseline: domestic financing	4.00%	600.0	36.0
Alternative 3: MFA III third tranche	0.75%	600.0	6.8
Difference: Alternative less baseline	-3.25pp	0.0	-29.3

Notes: Calculations exclude the compounding cost of interest payments.

Sources: CE calculations.

The decline in the interest payments of EUR 29.3 million over the 1.5 year period would not had a material impact on Ukraine's debt sustainability indicators. Therefore, it is

[376] Issued at 7.4% interest rate.

[377] Calculation excludes the compounding cost of interest payments.

assessed that the availability of the third tranche would not have impacted on Ukraine's debt sustainability in 2017 and 2018 during the MFA III operation.

However, the term of borrowing for third tranche would likely have been much longer than the initial term of 1.5 years covered by domestic financing in the baseline scenario in the absence of the third tranche. Therefore, the third tranche could also have served as a replacement to long term-issuances. For example, assuming that the third tranche would have been issued with maturity of 14 years and would have served as a replacement for long-term borrowing on terms similar to these obtained for the September 2017 Eurobonds issuance[378], the total interest savings over the 14 year period in the Alternative 3 scenario could have reached EUR 524 million compared to the baseline (inclusive of the EUR 29.3 million saving in the first 1.5 years)[379].

Annex 12 List of references

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[378] Issued at 7.4% interest rate.

[379] Calculation excludes the compounding cost of interest payments.

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Annex 13 Evaluation framework

Table 62. Framework for answering Evaluation Question 1: To what extent was the MFA III operation design (including adequateness of financing envelope, focus of conditionality) appropriate in relation to the outputs to be produced and objectives to be achieved?

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information
• The size of the financial assistance was adequate in relation to Ukraine's financing needs and given the constraints of the Genval criteria • Form and terms of support was appropriate given Ukraine's debt position and income status • MFA conditionalities were consistent with and relevant to Ukrainian needs and EU's and other donors' programmes and realistic given the short-term nature of the instrument • The MFA package was generally regarded as relevant to Ukraine's needs by	• Analysis of financing needs in 2015- 2017 (as done by IMF) and the role of MFA III in meeting these needs • Comparison between projected and actual financing needs – reasons for deviations and relevance and appropriateness of MFA III in light of any changes • Analysis of Ukraine's debt position and GDP data to examine if loan form was appropriate	• Degree of consensus among key stakeholders/ key informants regarding the relevance and importance of the MFA III (in absolute and relative terms) • Stakeholders and local economists' assessment of the use of a loan and focus of the conditionality; • Examination of whether the focus of MFA III conditionality was relevant and appropriate in Ukrainian context bearing also in mind the characteristics of the MFA instrument. In particular, the relevance focused on: (i) adequacy of the size of the financial assistance, (ii) appropriateness of the form and terms of financial assistance, and (iii) design and focus of conditionality	Desk review: - Ex-ante evaluation of MFA III to Ukraine; - The Memorandum of Understanding (MoU) and Loan Agreements - Reports and supporting documentation submitted by the Ukrainian authorities to the European Commission on the fulfilment of the structural reform criteria; - Commission's assessment of compliance with conditionality requirements (i.e. after mission reviews); - IMF research including Country Reports; - Other reports i.e. on the progress of PFM reforms accompanied with performance indicators/metrics. Semi-structured interviews: - EC officials: DG ECFIN, DG NEAR and SGUA - IMF/ WB/ EBRD officials; - Other bilateral/ multilateral donors supporting given reforms in Ukraine (i.e. USAID, GIZ); - Ukrainian authorities including also Ministry of Finance and Central Bank of Ukraine; - EU Delegation in Ukraine. Focus group with non-government stakeholders Stakeholder Workshop

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information
the key institutional stakeholders, local economists, civil society, media etc.		• Analysis of synergies with the IMF SBA/EFF programmes, WB (F)DPLs / other EU programmes	

Table 63. Framework for the evaluation of answering Evaluation Question 2: To what extent have the objectives of the MFA operation been achieved*?*

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information
• Macroeconomic impact • There has been an improvement in Ukraine's macroeconomic situation including external financial sustainability • The role and contribution of MFA III can be identified • MFA III had a positive social impact • The evidence suggests that Ukraine would have been worst off in absence of the MFA • Structural reforms • There is evidence of reform e.g. enhancement of the cash transfer program supporting	• Analysis of trends in key indicators (National accounts, Balance of payments statistics, Government finance statistics, Monetary statistics, External sustainability before, during and after MFA III • Analysis of data on lending conditions available for Ukraine (focusing on financing available from bilateral / multilateral donors and to some extent from national and international capital markets) • Debt Sustainability Analysis • Social Impact Analysis – evolution of key indicators relating to unemployment,	• Counterfactual analysis • Stakeholders and local economists' views on the specific contribution of MFA III to short-term macroeconomic stabilization of Ukraine; • Stakeholders and local economists' assessment of the contribution of MFA III including structural reforms; • Assessment of alternatives available to fill the financing gap if MFA	• Document and data review: • Macroeconomic data sourced from IMF/WB and national sources; • MFA documentation; • IMF reviews and country reports/ WB completion reports; • Credit rating agency reports (i.e. Moody's) • Academic and grey literature on Ukrainian economy; • Data on public borrowing (scale/ maturity/ costs) and prevailing market conditions at the time of

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information
households/ effectiveness of IDPs support service • There is evidence to suggest that MFA accelerated, reinforced or promoted reform in certain areas e.g. PFM • There is general consensus among stakeholders that the MFA contributed positively to macroeconomic stabilisation and Ukraine reform effort	poverty, support service to o-income households, IDPs etc,	III (and IMF) resources had not been provided; • Stakeholders' perceptions on other impacts.	MFA/IMF programs. • Semi-structured interviews: • EC officials: DG ECFIN, DG NEAR and SGUA • IMF/ WB (and EBRD) officials • Ukrainian authorities, in particular Ministry of Finance and Central Bank • EU Delegation in Kyiv. • Inputs from local experts • Delphi Survey • Focus Group

Table 64. Framework for answering Evaluation Question 3: Was the disbursement of the financial assistance appropriate in the context of the prevailing economic and financial conditions in the beneficiary country

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information
• MFA III disbursements were timely given Ukrainian financing needs	• Timing of disbursements in relation to key macroeconomic developments and Ukraine's financing needs	• Analysis of the timing of disbursements of both MFA III and IMF and factors affecting disbursements • Time taken between Ukrainian authorities request for MFA III assistance and approval/ disbursement of MFA III	Document and data review: - MFA documentation - IMF/ WB documentation Semi-structured interviews - EC officials: DG ECFIN, DG NEAR, SGUC - IMF/ WB officials - Ukrainian authorities - EU Delegation in Kyiv Delphi Survey results

Table 65. Framework for answering Evaluation Question 4: In what way has the design of the MFA assistance conditioned the performance of the operation in respect to its cost and its objectives?

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information
• There were favorable entry conditions for the MFA III operation e.g. political commitment; public buy-in, capacity to implement reform • The design of the MFA III operation was flexible, and it adjusted to changes in context and/or feedback mechanisms • There was effective dialogue between the European Commission and Ukrainian authorities • There was effective monitoring of the MFA III operation • Donors were well coordinated	Not applicable	• The extent of liaison between the European Commission and Ukrainian authorities; and between the European Commission and IMF/ other donors • The communication channels used and media treatment received • Whether there was effective monitoring of the MFA III operation • Stakeholders' feedback on what could have been done differently with the benefit of hindsight • Analysis of the choice of conditionality – see also relevance • Analysis of synergies with the IMF SBA/ EFF programs / other EU programs – see also relevance • Identification of good practice / lesson learned from the design and implementation of MFA III operation in Ukraine	Document and data review: Macroeconomic data sourced from IMF and national sources MFA documentation Semi-structured interviews: EC officials: DG ECFIN, DG NEAR, SGUA IMF/ WB officials Ukrainian authorities EU Delegation in Kyiv Delphi Survey Focus group

Table 66. Framework for answering Evaluation Question 5: What was the rationale for an intervention at EU level and to what extent did the MFA operation add value compared to other interventions by other international donors?

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information
• Financial added value over intervention at MS level • Evidence that MFA reinforced the Government's commitment to socio-economic reform • There is demonstrable evidence of signaling and confidence building effect of MFA operation – building investor and private sector confidence • EU had a discernible influence on the design and application of conditionalities • There is clear financial added value of EU support – national authorities would have struggled to meet their financing needs in absence of the EU MFA	Trends in confidence indicators and proxy indicators of confidence such as interest rates for T-bills and longer-term bonds denominated in local/ foreign currency and key indicators of the foreign exchange market/ announcements of credit rating agencies	• Qualitative assessment of links between wider fluctuations in confidence indicators and EU assistance • Mapping of conditionalities (see also relevance) • Stakeholders' views on the role and influence of EU in the design and application of support package	Document and data review: Macroeconomic data sourced from IMF and national sources; MFA documentation; IMF reviews and country reports; Academic and grey literature; Credit Rating Agencies reports; Financial markets data; Any relevant press monitoring reports Semi-structured interviews: EC officials: DG ECFIN, DG NEAR and SGUA; IMF/ WB officials; Other key bilateral/ multilateral donors; Ukrainian authorities; EU Delegation in Ukraine; Focus Group Delphi Survey Insights from study experts

Table 67. Framework for answering Evaluation Question 6: Were the measures of the MFA operation in line with key principles, objectives and measures taken in other EU external actions towards Ukraine?

Judgement criteria	Quantitative analysis	Qualitative analysis	Sources of information
• The MFA was fully in line with EU objectives and reinforced EU action deployed via other instruments	Not applicable	• Stakeholders assessment of the coherence of the MFA III with other EU external actions • Qualitative assessment of the adequacy of the conditionality, potential synergies/ overlapping with other EU instruments	Document and data review: - MFA documentation including ex-ante evaluations of MFA III to Ukraine; - Identification of relevant programs/ actions and review of their documentation; Semi-structured interviews: - EC officials: DG ECFIN, DG NEAR and SGUA; - EU Delegation in Kyiv; - Ukrainian authorities Focus Group Delphi Survey

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