



Macro-Financial Assistance for Ukraine
Loan Facility from the European Union of up to 1.8 billion EUR

MEMORANDUM OF UNDERSTANDING

between

THE EUROPEAN UNION
as Lender

and

UKRAINE
as Borrower

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and UKRAINE

1. On 15 April 2015, the European Parliament and the Council of the European Union adopted a decision to provide macro-financial assistance to Ukraine of up to EUR 1.8 billion in the form of a loan (Decision (EU) 2015/601). The objective of this assistance is to ease Ukraine's urgent external financing constraints, alleviate its balance of payments and budgetary needs and strengthen its foreign exchange reserve position. This assistance from the European Union is complementary to the resources provided to Ukraine by International Financial Institutions and bilateral donors in support of the authorities' economic stabilisation and reform programme.
2. The assistance will be disbursed in three instalments of EUR 600 million each. The disbursements will be conditional upon a satisfactory track record in the implementation of the Extended Fund Facility (EFF) agreed between Ukraine and the International Monetary Fund (hereafter referred to as "the IMF"). The first instalment will be disbursed upon entry into force of this Memorandum and the corresponding Loan Agreement, provided that Ukraine receives disbursements under the EFF agreed with the IMF. The disbursement of the second and third instalments shall not take place earlier than three months after the release of the previous instalment and will also be conditional upon a positive assessment by the European Commission (hereafter referred to as "the Commission") on behalf of the European Union, of progress made with respect to a set of macroeconomic and structural adjustment policy conditions specified hereinafter. These conditions are based on the economic stabilisation and reform programme developed by the Ukrainian authorities, and are consistent with the agreement reached by Ukraine with the IMF.
3. Prior to the release of the second and third instalments by the Commission, Ukraine's authorities shall provide the Commission with a Compliance Statement on the fulfilment of the conditionality attached to the instalment in question. Upon receipt of these compliance statements, the Commission will evaluate, in co-operation with the authorities of Ukraine, the progress made with respect to the fulfilment of the conditionality. The policy measures and frame of reference for this evaluation are laid down in Annex I. In case of a negative evaluation, the Commission may withhold the disbursement of the second and third instalments until Ukraine proves its compliance. If necessary, Annex I may be amended upon mutual agreement, following the completion of the respective approval processes of the EU and Ukraine.

The Commission will also continuously verify the financing needs of Ukraine and may reduce, suspend or cancel the assistance in case they have decreased fundamentally during the period of disbursement compared to the initial projections.

4. The effective payment of different instalments shall be subject to the signature of the corresponding Loan Agreement by the parties and its entry into force.

5. The Commission will make available the proceeds of the assistance to Ukraine through the National Bank of Ukraine (hereafter referred to as “the Agent”). Given the substantial budgetary financing needs faced by the country, the proceeds of the loan may be used to finance Ukraine's budget.

The authorities of Ukraine undertake to timely and fully service all financial obligations stemming from loans provided or guaranteed by the European Union.

6. During the implementation of the assistance, the authorities of Ukraine shall supply the Commission with all information that is relevant for the monitoring of its economic and financial situation and for the assessment of progress in the implementation of the policy measures agreed. In particular, the authorities will supply to the Commission on a timely basis the relevant information set out in Annex II.
7. With a view to preventing irregularities and fraud related to the use of the assistance and ensuring the protection of the EU's financial interests, the relevant provisions of the Loan Facility Agreement will apply, notably those regarding regular checks on the use of EU assistance, and checks and audits performed by the Commission and the Court of Auditors. Also, the provisions of the Loan Facility Agreement on early repayment will apply in case it has been established that Ukraine has engaged, in relation to the management of this assistance, in any act of fraud, corruption or any other illegal activity.
8. Throughout the duration of this MoU and for five years after the disbursement of the last instalment (*ex-post* period), the Commission, represented by its own agents or its duly mandated experts, shall have the right to carry out operational assessments of the administrative procedures and financial circuits of the government of Ukraine and of the Agent that relate to the management of EU macro-financial assistance.
9. An independent *ex-post* evaluation of the assistance may be carried out by the Commission or its duly authorised representatives. The authorities of Ukraine are committed to supply all necessary information to the Commission, represented by its own agents or its duly mandated experts, for the duration of this process. The evaluation report will be made available to the authorities of Ukraine for comments.
10. The authorities will ensure, as appropriate, close co-operation with the European Commission. Confidential information under this Memorandum shall be exchanged in accordance with the Agreement between Ukraine and the European Union on the security procedures for the exchange of classified information of 13 June 2005.
11. This assistance is implemented on the understanding that the authorities of Ukraine will continue to respect effective democratic mechanisms, including a multi-party parliamentary system, and the rule of law and to guarantee the respect for human rights.
12. The assistance will be made available for two and a half years starting from the day after the entry into force of this Memorandum of Understanding.
13. Annexes I and II are an integral part of this Memorandum.

14. All notices in relation with the present Memorandum shall validly be given if in writing and sent to:

For the European Union

European Commission
Directorate General for
Economic and Financial Affairs
Rue de la Loi, 170 - CHAR 11/248
B-1040 Brussels

For Ukraine

Ministry of Finance of Ukraine
12/2 Hrushevskiy Street, Kyiv
01008 Ukraine
For the attention of: Minister, Deputy Minister, and
Head of Debt and International Financial Policy
Department

With copy to:

National Bank of Ukraine
9 Instytutska Street, Kyiv
01601 Ukraine
For the attention of: Governor or Deputy Governor

15. The present Memorandum shall become effective following the signature by Ukraine and the European Union and following receipt by the European Union of written notification by Ukraine of fulfilment of internal procedures envisaged by the law of Ukraine.
16. This Memorandum may be amended upon mutual agreement of the parties in form of a written Addendum. The Addendum will be an integral part of this Memorandum and will enter into force according to the same procedure as the Memorandum.

This Memorandum of Understanding has been signed in four originals in the English language.

For the EUROPEAN UNION
as Lender
Represented by
the EUROPEAN COMMISSION

For UKRAINE
as Borrower
Represented by

Signed in Riga on 22 May 2015 by

Valdis Dombrovskis
Vice-President

Signed in Riga on 22 May 2015 by

Natalie Jaresko
Minister of Finance

Signed in Riga on 22 May 2015 by

Valeria Gontareva
Governor of the National Bank of Ukraine

Structural Reform Policy Measures

At the time of the Commission review that will precede the decision with respect to the disbursement of the second loan instalment, the authorities are committed to have fulfilled the following conditions:

Public Finance Management

External audit

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.

Public procurement

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.
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.

Fiscal governance

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.
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.

Governance and transparency

Anti-corruption

6. Establish a National Anti-Corruption Bureau, a specialised Anti-Corruption Prosecution Office and a National Agency for the Prevention of Corruption, ensuring that they are independent and operational, i.e. endowed with the financial resources, staff and equipment required to perform their functions.

Public administration

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.

State-owned enterprises

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.

Energy sector

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.
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.

Social safety nets

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

Business environment

Trade and Customs

13. Refrain from introducing new trade-restricting or trade-distorting measures, in line with Ukraine's WTO obligations.

Competition policy

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 publishing a document explaining the principles to be used in the setting of any pecuniary sanctions imposed for infringements of the competition laws.

Financial sector

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.

At the time of the Commission review that will precede the decision with respect to the disbursement of the third loan instalment, the authorities are committed to have fulfilled the following conditions:

Public Finance Management

External audit

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.

Public procurement

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.

Fiscal governance

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.
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.

Governance and transparency

Anti-corruption

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.
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.
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.

Public administration

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.
9. Adopt the by-laws relevant for the legislative package on the Civil Service.
10. Consistent with the new legal framework on the Civil Service, start running open competitions for the recruitment of civil servants.

Energy sector

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.
12. Amend the electricity market law in line with Ukraine's commitments under the Energy Community Treaty.
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.
14. Publish Ukraine's first Extractive Industries Transparency Initiative report.

Social safety nets

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-tested transfers for housing utilities and the tariff compensation scheme introduced in 2014.
16. Prepare a first evaluation of social service delivery to IDPs and ensure effective follow-up.

Business environment

Trade and Customs

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.
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.

Justice sector

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.

Deregulation

20. In order to streamline administrative procedures for carrying out business activity in Ukraine, reduce the number of permits and simplify permit and licensing procedures on the basis of a thorough analysis of their costs to businesses and benefits to society.

Financial sector

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.

Monitoring System

During the implementation of the European Union's assistance, the following indicators and reports shall be provided to the Commission by the relevant authorities on a regular basis in the English language. The monthly data shall be provided by the 25th of the following month, starting with June 2015 as the reporting period. The quarterly data shall be provided by the end of the second month of the quarter following the reporting period, starting with the first quarter of 2015 as the reporting period.

1. Level and composition of general government revenue and expenditure, including extra-budgetary public funds and state-owned enterprises (monthly)
2. General government and publicly guaranteed debt:
 - a) Stock of general government debt and publicly guaranteed debt (monthly)
 - b) Interest and principal payments made on general government debt and publicly guaranteed debt (quarterly)
 - c) Scheduled annual payments (interest and principal) on general government debt and publicly guaranteed debt with a quarterly breakdown for the years 2015-2018 (quarterly)
3. Gross external debt:
 - a) Stock of gross external debt (quarterly)
 - b) Interest and principal payments made on external debt per sector (quarterly)
 - c) Interest and principal payments on external debt falling due over the next 12 months (quarterly)
4. Energy sector:
 - a) Forecast annual balance, including a quarterly breakdown, of natural gas supply and distribution (monthly)
 - b) Financial indicators in the gas and heating sectors, including prices and volumes of domestically produced and imported (by sources of import) gas, sales, tariffs, arrears, payments to the budget, subsidies, and debt in the format agreed with the IMF (monthly)
 - c) Collection rates of Naftogaz by type of customer since January 2014 (monthly)
 - d) Information on the cash flows and the deficit of Naftogaz in the format agreed with the IMF (monthly)
 - e) Information on the financial liabilities of Naftogaz, including a schedule of interest and principal loan repayments (monthly)
 - f) Information on the quantity of heating energy meters installed at buildings, including as a ratio to the number of buildings (monthly)

5. Number and total financial value of public procurement procedures and breakdown into single-source and competitive procedures, including an appropriate span of historical data for comparison purposes, as well as a breakdown into: (i) utilities with a monopoly supplier; (ii) defence; and (iii) other sectors (quarterly)
6. General government arrears to public procurement contractors (monthly)
7. Data on VAT refunds in the format agreed with the IMF (monthly)
8. Data on tax arrears, including a breakdown into groups of taxpayers (monthly)
9. Financial sector:
 - a) Banking sector financial stability indicators, including the following ratios: Core Tier 1 capital adequacy ratio, non-performing loans (NPL) defined as loans more than 90 days past due, coverage of NPL with loan loss provisions, average return on equity and return on assets (quarterly)
 - b) Breakdown of aggregated loans to households including mortgage loans and consumer loans (monthly)
 - c) Data on the liquidity situation of the banking system, including information on liquidity support provided to banks, liquidity ratios used by NBU and aggregated information on deposit outflows with breakdown in local and foreign currency (monthly)
 - d) Data on banks put into resolution, including names of banks, total assets, type of procedure applied, payments to insured depositors and cash and other liquid reserves in the Deposit Guarantee Fund to pay insured depositors (monthly)
 - e) Data on public funds used for recapitalisation of banks, amounts of guarantees and other state aid instruments granted to banks and related budgetary costs (monthly)
10. Aggregated data on the financial performance of state-owned enterprises (quarterly)
11. Data on number of audits launched on state-owned enterprises (quarterly)
12. Information on clearance rates and disposition time of civil and administrative law cases including an appropriate span of historical data for comparison purposes (quarterly)
13. Results of planned user satisfaction surveys for court proceedings in civil and administrative matters (as they become available)
14. Anti-corruption:
 - a) Number of investigations undertaken/completed by the National Anti-Corruption Bureau (quarterly)
 - b) Number of cases prosecuted by the specialised Anti-Corruption Prosecution Office and number of indictments made (quarterly)
 - c) Number of asset declarations verified by the National Agency for Prevention of Corruption and their outcome, in particular number of suspicions of unjustified wealth identified based on these verifications and their follow-up (quarterly)
15. Average time lapsed between first notifications of intended mergers and decisions made by the Anti-Monopoly Committee of Ukraine (AMCU), and number of merger cases for which the AMCU decision has been pending for more than six months from the first notification by the companies concerned (quarterly)
16. Number of audits launched and, for audits concluded, number of reports published by the Accounting Chamber of Ukraine (quarterly)

17. Number of recruitment competitions launched and number of recruitment competitions completed under the new civil service law (quarterly)
18. Number of applications filed for the Household Utility Subsidy scheme, number of actual beneficiaries, and amounts disbursed to them under the scheme (monthly)
19. Number of registered Internally Displaced Persons and amounts of social benefits disbursed to them (monthly)
20. Monitoring report on the implementation of the Public Finance Management Strategy and Action Plan (quarterly; Ukrainian-language version is acceptable)
21. Inflation report published by the National Bank of Ukraine (quarterly)

In addition, the publication of macroeconomic data in a timely manner and in at least the same frequency and degree of detail as previously shall be maintained by the relevant authorities.