

**ROADMAP**  
FOR RESOURCE  
GOVERNANCE  
POLICY REFORM

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## SUMMARY

The resource governance reform requires implementation of simultaneous changes in many public administration aspects. Sound public policy relating to such governance should harmonize provisions of land and fiscal laws, financial and accounting reporting rules, environmental protection standards, format and extent of public data disclosure, including beneficial owners of extractive companies, and, more importantly, geological information.

In addition, such policy should comply with the general principle of subsidiarity that is being implemented in Ukraine within the framework of the decentralization reform. It is especially important in a view of a satisfactory score in the local impact subcomponent of the Resource Governance Index (RGI)<sup>1</sup>.

In other words, **aligning extractive industry governance standards in Ukraine with the best global practices is a challenging and comprehensive task.**

The latest RGI that analyzed resource governance quality for the period of 2015-16 provided the research team with a valuable general overview of the problem. While only governance standards in the oil and gas sector were assessed in Ukraine, it helped drag the researchers' attention to the key aspects to be improved. Following a discussion of the RGI results, this analysis focuses on reforming 11 aspects of public policy as broken down into 3 large groups, including **transparency and access to information, business deregulation tasks and involvement of local community interests.**

While occasional improvements cannot influence low RGI scores in the enabling environment component assessing general business environment, **this roadmap of priority activities sought to outline the path for Ukraine to substantially improve its current score in the next RGI.**

This study helped achieve one of the most valuable results — understanding that over the last few years significant efforts have been made in the appropriate direction in terms of development

<sup>1</sup> For more information about the RGI and Ukraine's scores see: <http://dixigroup.org/publications/shcho-take-indeks-upravlinnya-resursam/>

and, partly, adoption of amendments to the framework legislation. In particular, the Draft Laws No. 4646-д (implementation of modern accounting and financial reporting standards), No. 6229 (ensuring transparency in extractive industries), and deregulation Draft Law No. 3096-д were registered in the Verkhovna Rada, and the Laws No. 1793-VIII (partial rent decentralization) and No. 2059-VIII (environmental impact assessment) were passed.

Almost every aspect of reforms **requires significant coordinated efforts of different executive authorities** for further clarification and regulation of specific procedures for implementation of improved rules. There are no concerns as regards delays in implementation of such decisions in part where such regulatory activity coincides with other priorities of the Government, especially in terms of energy safety improvement. The rest of necessary activities as well as expanding relevant best practices beyond the oil and gas sector will require close attention and support from the civil society and international stakeholders.

However, the decisions and documents passed generally focus on occasional elimination of barriers or improvement of specific procedures within licensing, environmental or fiscal policies. Development of the **comprehensive policy which would establish strategic objectives for the whole sector reform will take place in future.** The new Subsoil Code of Ukraine should become the key document that must embody this idea and codify provisions scattered through different laws.

Judging by the experience of efficient development of the Concept for Development of Ukraine's Gas Production Industry<sup>2</sup>, the problem rather lies in the Government's vision of priorities that in the lack of capacity for such strategic activity. Therefore, it is very important to **give greater priority to improvement of resource governance standards in Ukraine on the Government's reform agenda.**

The analysis showed that, given such political commitment and the successful results achieved, implementation of priority activities aimed at improvement of the policy and conditions for subsoil users and other stakeholders might actually take 15 months. In addition, if this time period will be used for extensive work involving development and launch of future strategic reforms, **Ukraine can become one of the leaders of the future Resource Governance Index** by 2019.

<sup>2</sup> Approved by the CMU Ordinance of 28 December 2016 No. 1079-p (<http://www.kmu.gov.ua/control/uk/cardnpd?docid=249766439>)

## PART 1. TRANSPARENCY BY DEFAULT

Good governance is based on transparency across the whole value chain, reflected in detailed and disaggregated reporting. In extractive sector, the latter means disclosing information on what you pay (production and revenues), why you pay (contracts and permits), and who stands to benefit (beneficial ownership).

These became the new global standards in the extractive industry not just because transparency allows all stakeholders to observe actual trends and developments in the extractive industries, but most importantly to hold responsible decision makers and market players responsible to account for their conduct. Directive 2013/50/EU (new Transparency Directive) and Directive 2013/34/EU (new Financial Reporting Directive) require from oil and gas companies, mining companies and logging companies to report on their payments to governments at the project level. The same requirement can be found in the Extractive Industries Transparency Initiative (EITI) Standard, being implemented in more than 50 countries worldwide. Ukraine obtained the EITI candidate status in 2013. In the next year, the EU-Ukraine Association Agreement was signed with relevant commitments. At the same time, it is important to distinguish the EITI standard that provides a broad set of transparency requirements across the whole value chain of the extractive industries from the somewhat more specific and narrowed down EU accounting directives, which are a great complement to this broader vision, particularly around production and revenue collection.

Project level payment reporting provided for by these standards entails synergic benefits on numerous levels. Its approximation to the most detailed granularity enables all stakeholders to accurately determine whether the obligations that are usually determined at the project level are being met. In other words, it allows the government, companies and citizens to determine whether companies are compliant with their respective financial obligations. Not only does it bring considerable benefits for the citizens through allowing them to ensure that companies are paying their fair share, but it is also good for investment by means showing a non-discriminational treatment for all companies by the government.

Apart from payment reporting at the project level enabling investors to make informed decisions on attractiveness of specific field developments and communities to understand their benefits, these standards require disclosure of contracts. It means that any contracts granting the right to mineral resources development (exploration, extraction and exploitation) must be disclosed to the general public.

When people have no access to contracts, they cannot monitor the extractive company's performance of its investment and other obligations, which often leads to conflicts that block development of mineral resources and hinder economic development. In addition, disclosure of contracts results in deals that are more balanced; better able to stand up to public and commercial scrutiny and better drafted, so less likely to have legal issues associated with them.<sup>3</sup>, and thus has more chances to engage more responsible and transparent companies.

Despite successful disclosure of some data, e.g. disclosure of the Register of Special Permits for Subsoil Use and geological maps<sup>4</sup>, and disclosure of information on ultimate beneficial owners in the Unified State Register<sup>5</sup>, the data on specific fields and areas under development or prospective development is scattered through various agencies. There is an acute need for creation of the single data portal with free access.

We should also acknowledge that new reporting involves minimal expenses, including companies' expenses related to additional accounting and financial reporting activities, auditor's services as well as public expenditure on collection and processing of this information. However, due to extended access to extraction data, the Government and potential investors will have a clear vision of the situation and will be able to set rules of the game (including licensing system, tax and rent rates).

It is proved that greater transparency brings greater investments: the data analysis in 81 countries of the world showed that only accession to the EITI Standard resulted in increases of foreign direct investment to GDP of 2% on average<sup>6</sup>. One more survey related to Directives 2013/50/EU and 2013/34/EU also showed that these

3 [https://www.open-contracting.org/wp-content/uploads/2016/02/OCPT2016\\_EITI\\_brief.pdf](https://www.open-contracting.org/wp-content/uploads/2016/02/OCPT2016_EITI_brief.pdf)

4 <http://geoinf.kiev.ua/wp/interaktyvni-karty-spetsdozvoliv.htm>

5 <https://usr.minjust.gov.ua/ua/freesearch>

6 See Schmaljohann, Maya (2013): Enhancing Foreign Direct Investment via Transparency? Evaluating the Effects of the EITI on FDI. Discussion Paper Series No. 538. [https://eiti.org/files/Schmaljohann\\_2013\\_dp538.pdf](https://eiti.org/files/Schmaljohann_2013_dp538.pdf)

standards are strongly supported by field-specific experts: 82% of financial analysts and institutional investors consider the periodic information published to be useful for investment purposes; and 69% do not consider increased audit costs to be too onerous<sup>7</sup>.

## Implementing reporting at the project level

### DECISIONS



- *Adoption of laws on data disclosure at the project level in accordance with the EITI Standard, EU Directives and best global practices.*
- *Adoption of secondary legislation, including the submission procedure, reporting forms etc.*
- *Launch of software environment for e-submission of reports by disclosing entities and display of received data.*

### OPPORTUNITIES AND THREATS



The requirement as regards disclosure of information about extractive companies' activities at the project level is a part of the EITI Standard and EU directives provisions relating to transparency and financial reporting which are binding on Ukraine<sup>8</sup>. The EITI International Secretariat is likely to publish detailed guidance on the implementation of project-level reporting by the end of 2017, and this could be a key reference document.

A project is defined as an extractive company's operational activities in the specific subsoil area *"that are governed by a single contract, license, lease, concession or similar legal agreements and form the basis for payment liabilities to a government"*<sup>9</sup>. However, the definition provided in Directive 2013/34/EU also states that if multiple such agreements are substantially operationally and geographically interconnected, they should be considered one project.

<sup>7</sup> DeMarginy, Fabrice & Christophe Clerc (2010): Transparency Directive Assessment Report. Executive summary and possible improvements. [http://ec.europa.eu/finance/securities/docs/transparency/report-application\\_summary\\_en.pdf](http://ec.europa.eu/finance/securities/docs/transparency/report-application_summary_en.pdf)

<sup>8</sup> [https://eiti.org/sites/default/files/documents/eiti\\_progress\\_report\\_2017.pdf](https://eiti.org/sites/default/files/documents/eiti_progress_report_2017.pdf); <https://eiti.org/BD/2017-14;> \_

<sup>9</sup> <http://old.minjust.gov.ua/file/48858.docx>

In practice, such approach may be used for artificial integration of unrelated projects for the purpose of aggregate reporting so it needs detailed regulation. It is also important to maintain the principle that what constitutes a project is linked to the forms of legal agreement(s) governing extractive activities between the government and companies.

The Draft Law No. 4646-д<sup>10</sup> on financial reporting and the targeted Draft Law No. 6229<sup>11</sup> on reporting system for extractive companies are being considered by the Parliament. While the former does not provide for the definition of a project and the list of data to be disclosed, the latter sets detailed requirements and the procedure for data disclosure at the project level.

It also stipulates that the payment significance threshold, i.e. the value below which the data should not be included in reports, shall be determined separately for each type of mineral resources by the Multistakeholder Group at the Ministry of Energy and Coal Industry of Ukraine (MECI), involving the Government, the business and the public. In addition, while extractive companies must report on their payments to public authorities, the latter should also disclose the amounts credited to relevant budgets. In other words, the best practice should involve imposing on both parties an obligation to comply with the requirements through publication of the information on payments for each project.

Such balance of interests will allow for approval of new rules and will take fiscal transparency in Ukraine to a new level. As for sanctions for non-compliance with these reporting rules, a compromise was achieved as regards shortening the list of grounds, moderate fines, a possibility of quick elimination of violations, and transitional period during which the sanctions will not be imposed.

One should understand that optimal implementation of the new reporting procedure is possible only in case of automation of processes, administrative simplification and potential additional costs. For this purpose, it is important to develop, create and operate an e-system for submission of reports, their automated analysis and data publication for all reporting entities, including companies and payment recipients. The same principle is applied by Companies House<sup>12</sup> in the UK and by the ESTMA<sup>13</sup> in Canada, but the nearest analogue is the Tax Report Processing System<sup>14</sup> in Kazakhstan. Such

10 [http://w1.c1.rada.gov.ua/pls/zweb2/webproc4\\_1?pf3511=62044](http://w1.c1.rada.gov.ua/pls/zweb2/webproc4_1?pf3511=62044)

11 [http://w1.c1.rada.gov.ua/pls/zweb2/webproc4\\_1?pf3511=61409](http://w1.c1.rada.gov.ua/pls/zweb2/webproc4_1?pf3511=61409)

12 <https://extractives.companieshouse.gov.uk/>

13 <http://www.nrcan.gc.ca/mining-materials/estma/18198>

14 <http://kgd.gov.kz/ru/section/sono>

approach will require cooperation between the MECI responsible for the EITI implementation and the Ministry of Finance responsible for the accounting and financial reporting policy.



## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD

- *Adoption of the Draft Laws No. 4646-δ “On Introducing Amendments to the Law of Ukraine “On Accounting and Financial Reporting in Ukraine” (As Regards Improvement of Some Provisions)” and No. 6229 “On Ensuring Transparency in Extractive Industries” — by the end of 2017;*
- *Entry of the Laws into force — since the beginning of 2018;*
- *Development and approval by the Cabinet of Ministers of the Procedure for disclosure of information by economic entities operating in extractive industries and the Procedure for handling cases involving disclosure of information in extractive industries by the central executive authority in charge of implementation of public policy in the energy sector and coal industry— Q1 2018;*
- *Development and approval by the Cabinet of Ministries of forms of the production and payment report, consolidated production and payment report, report on payments received — by June 2018;*
- *Determination by the Multilateral Group on the EITI Implementation in Ukraine of the reporting threshold (minimum payment to be included in reports) for each extractive industry — by June 2018;*
- *Development and testing of the software environment for e-submission of reports by disclosing entities, open data formatting and display of received data — by 1 September 2018;*
- *Launch (including state certification) of the software environment — by 2019; and*
- *Enforcing submission of relevant reports — on annual basis, not later than the 1st of September.*

## RESPONSIBLE ENTITIES

- *Verkhovna Rada of Ukraine*
- *Cabinet of Ministers of Ukraine*
- *MECI (Multilateral Group on the EITI Implementation in Ukraine)*
- *State Fiscal Service*
- *Ministry of Finance*



## Creating the single portal with data on mineral resources

### DECISIONS

*Creation and efficient administration of the single government portal as a display and source of data on mineral resources of Ukraine and their potential.*



### OPPORTUNITIES AND THREATS

The Resource Governance Index (RGI) concluded that data disclosure in the extractive industry is weaker than disclosure of information generally available to public authorities. It is especially true for Ukraine where the single open data portal was created (<http://data.gov.ua/>) together with the Single Web Portal for the Use of Public Funds (<https://spending.gov.ua/>) where the information is published in accordance with the Law of Ukraine “On Openness of Use of Public Funds”. In addition, in Ukraine operates the globally recognized ProZorro system<sup>15</sup>, in which the world’s first blockchain auction took place, whereby it is impossible to change data in the system<sup>16</sup>.



However, there is no system for dissemination and access to information about mineral reserves, extraction and export. Some datasets are published by the Ministry of Energy and Coal Industry. The

<sup>15</sup> <https://ti-ukraine.org/news/prozorro-dlia-bankov-kakov-rezultat-prodazh-aktyvov-bankov-bankrotov-povnovomu/>

<sup>16</sup> <https://economics.unian.net/other/2119494-gospredpriyatye-setam-provelo-pervyyiy-v-mire-auksion-natehnologii-blokcheyn.html>

State Service for Geology and Mineral Resources of Ukraine (Derzhgeonadra) also administers a database on special permits for subsoil use through State Research and Development Enterprise “Derzhgeoinform”.

As early as 2015, the Government approved the Regulation on Datasets to be Published in the Open Data Format. They include the data owned by the MECl, the Ministry of Ecology and Natural Resources (MENR) and the Derzhgeonadra<sup>17</sup>. However, these datasets do not cover all issues related to natural resources and do not contain the most valuable information at the project level. The Resolution of the Cabinet of Ministers is being updated to expand the scope of datasets to be disclosed<sup>18</sup>. Still, we consider that the extractive industry needs a separate approach to disclosure of geological information as relevant datasets may belong to different data owners and they should be disclosed more deeply and systemically than data in other sectors.

Creation of a modern and user-friendly open data portal on natural resources is impossible without improvement of regulatory policy, and strengthening the competence and institutional capacity of responsible public authorities. This is proved by the examples of Mexico and the USA. The former launched a production website (<https://portal.cnih.cnh.gob.mx/>) within the framework of the systemic reform in the oil and gas sector, the latter did the same (<https://useiti.doi.gov/explore/>) after its first EITI Report.

Thus, if Ukraine is to create such portal, it should be done under a more extensive subsoil use and resource governance reform or as a part of the e-submission system (see above). Given the need for simultaneous creation of geological information database to be implemented by the Derzhgeonadra, we propose designating the MECl (as an entity responsible for the EITI implementation) or the MENR (as an entity responsible for resource governance) as responsible for creation of such portal. As the portal will also include the information for investors, it is recommended to engage the Ministry of Economic Development and Trade in this process.

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<sup>17</sup> <http://www.kmu.gov.ua/control/uk/cardnpd?docid=248573101>

<sup>18</sup> <https://www.slideshare.net/uaenergy/report-antikor-march2017revii>

## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD



- *Introduction of amendments to the CMU Resolution of 21.10.2015 No. 835 (updating the list of datasets to be disclosed) — by December 2017;*
- *Designation of the Authorized Agency for the portal administration — Q4 2017;*
- *Development of the Terms of Reference for the single portal of databases of central executive authorities in the area of subsoil use, fundraising activity for the project — by June 2018; and*
- *Implementation of the ToR and filling the platform with content.*

## RESPONSIBLE ENTITIES

- *Cabinet of Ministers of Ukraine*
- *MECI*
- *MENR*
- *State Agency for E-Governance*



## Disclosure of contracts or their elements



### DECISIONS

*Introduction of the system for disclosure of essential terms and conditions of contracts (optionally – also full text disclosure for new contracts) in accordance with the EITI Standard recommendations and best global practices.*



### OPPORTUNITIES AND THREATS

In Ukraine, there are no requirements as regards publication of contracts which grant the right to development of mineral resources, including subsoil use agreements, production sharing agreements, joint activity agreements and other agreements. Moreover, there are no obligations as regards disclosure of annexes or amendments to such documents. All such provisions are deemed confidential, unless all of the parties agree to disclose them.

However, the EITI Standard, which has been implemented in Ukraine since 2013 and resulted in 2 very informative reports on production of gas, oil, coal, iron ore, black iron ore and titanite ore, encourages contract disclosure.

39 countries worldwide disclose all or a part of contracts and 27 countries have relevant laws, including Constitution<sup>19</sup>. Some governments set it as a standard for any resource investments to be allowed to enter their markets through introduction of relevant amendments to the legislation. Such practice is highly recommended by the IMF<sup>20</sup>, the UN<sup>21</sup>, and is one of the requirements for sector companies related to obtaining the IFC (World Bank Group)<sup>22</sup> and the EBRD<sup>23</sup> loans etc.

19 From the NRG expert Rob Pitman's presentation within the framework of the Round Table "Resource Governance Index 2017: "Home Work" for Ukraine" (Verkhovna Rada Committee on Fuel and Energy Complex, Nuclear Policy and Nuclear Safety, 12.07.2017). See also [http://repository.openoil.net/wiki/Main\\_Page](http://repository.openoil.net/wiki/Main_Page)  
20 IMF (2007), Guide on Resource Revenue Transparency, <https://www.imf.org/external/np/pp/2007/eng/051507g.pdf>

21 UN (2015), Principles for responsible contracts, [http://www.ohchr.org/Documents/Publications/Principles\\_ResponsibleContracts\\_HR\\_PUB\\_15\\_1\\_EN.pdf](http://www.ohchr.org/Documents/Publications/Principles_ResponsibleContracts_HR_PUB_15_1_EN.pdf)

22 International Finance Corporation (2012), Policy on Environmental and Social Sustainability, [http://www.ohchr.org/Documents/Publications/Principles\\_ResponsibleContracts\\_HR\\_PUB\\_15\\_1\\_EN.pdf](http://www.ohchr.org/Documents/Publications/Principles_ResponsibleContracts_HR_PUB_15_1_EN.pdf)

23 European Bank for Reconstruction and Development (2013), Energy Sector Strategy, <http://www.ebrd.com/what-we-do/sectors-and-topics/ebrd-energy-strategy-transparency.html>

It will be good for transparency to publish the full text of a contract, licence or permit as well as related documents (annexes, studies, amendments and addenda), i.e. all sources that contain terms and conditions in the public interest or modify them. According to the NREGI, publication of contracts has become a new international rule applied by both governments and big multinational companies<sup>24</sup>.

Despite a difficult situation with the judiciary reform, protection of ownership and other factors leading to a high level of the private sector's distrust of the government and other market participants, certain progress may be observed in Ukraine. In 2015, the database of special permits for subsoil use was opened; this register<sup>25</sup> contains data on special terms of each licences. These provisions constitute an integral part of a subsoil use agreement, but agreements are not published. The special permit database is not convenient, and automated processing of their texts is impossible.

The Draft Law "On Ensuring Transparency in Extractive Industries" (No. 6229<sup>26</sup>) that was introduced by a group of MPs and is being considered by the Parliament, incorporates the EITI Standard and global reporting practices. In particular, it provides for the disclosure of data on essential terms and conditions of agreements, including subject-matter, dates of entry into force and duration, names of the parties, rights and obligations of the parties, terms for collection of charges, operational obligations, environmental, health and safety obligations, other social obligations. However, these requirements are not applicable to commercial contracts with counterparties, service contracts and other agreements.

Also, a recommended option would be to introduce best practice, i.e. full text disclosure for all new contracts (including annexes and amendments) to be included in future. It shall be considered to implement the EITI Standard section 2.4(a) recommendations.

Why do we need such bold moves? They are necessary for communities that complain of social and economic problems pertaining to extractive companies' activities in their settlements to understand the rules and conditions the latter must comply with. Appropriate monitoring of contract performance can give an impetus to solving the problem of sleeping licences and encourage the parties to negotiate better contractual terms and conditions and adopt best global

<sup>24</sup> <https://resourcegovernance.org/analysis-tools/publications/past-tipping-point>

<sup>25</sup> <http://geoinf.kiev.ua/wp/interaktyvna-karta-rodovyschch-korysnykh-kopalyn.htm>, <http://geoinf.kiev.ua/wp/spedozvoli-rep.php>

<sup>26</sup> [http://w1.c1.rada.gov.ua/pls/zweb2/webproc4\\_1?pf3511=61409](http://w1.c1.rada.gov.ua/pls/zweb2/webproc4_1?pf3511=61409)

practices. Companies are interested in obtaining a so called “social licence” for their activities from communities and building a social dialogue without unreasonable blaming. In addition, knowing that the new contracts would become public, parties of the respective agreements would be to draft them in accordance to higher standards thus making deals more responsible.

When implementing requirements relating to disclosure of essential terms and conditions of contracts and new types of reporting, one should consider a transitional period or a pilot period, during which a refusal to publish data or their partial publication will result rather in admonition than in fines in order to expand the practice on a voluntary basis.

The contract database should become an element of the single web platform (see above). Documents must be publicly available free of charge in a format allowing for their automated processing using electronic means, i.e. in a format enabling navigation and search in accordance with the Open Contracting Principles<sup>27</sup>. However, it is important to understand that publication of contracts is a final stage of the chain, including appropriate planning, holding auctions/contests, award and administration of special permits for subsoil use, production sharing agreements and other contracts to which the State is a party.

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<sup>27</sup> <https://www.open-contracting.org/get-started/global-principles/>

## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD



- *Adoption of the Draft Law No. 6229 “On Ensuring Transparency in Extractive Industries” — September — October 2017;*
- *Date of entry into force — from 1 January 2018;*
- *Development and approval by the CMU of the Procedure for data disclosure by economic entities operating in extractive industries — Q1 2018; and*
- *Creation of the database (register) of contracts on the single portal — by the end of 2018.*

## RESPONSIBLE ENTITIES

- *Verkhovna Rada*
- *MECI*



# Switching to international tax reporting and accounting practices

## DECISIONS



- *Introduction of amendments to the Law of Ukraine of 16.07.1999 No. 996-XIV “On Accounting and Financial Reporting in Ukraine” (switching to international financial reporting standards); and*
- *Finalization of the Tax Code of 02.12.2010 No. 2755-VI and the Order of the Ministry of Finance of 26.08.2008 No. 1090 “On approval of the Accounting Regulation (Standard) 33 “Expenditure on Exploration of Mineral Reserves” (as regards reflecting all costs invested in extraction on relevant accounts).*

## OPPORTUNITIES AND THREATS



According to the Resource Governance Index (RGI), extractive companies in Ukraine are not subject to special check of accounts other than ordinary audit. In accordance with the current Law of Ukraine “On Accounting and Financial Reporting in Ukraine”, application of the International Financial Reporting Standards (IFRS) is not mandatory. Here it goes about IFRS 6 — Exploration for and Evaluation of Mineral Resources<sup>28</sup>, FAS 19 — Financial Accounting and Reporting by Oil and Gas Producing Companies, and FAS 69 — Disclosures about Oil and Gas Producing Activities etc.

International standards are applied in most Western countries and by global exchanges, so their adoption will allow attracting investors which are able to appropriately assess project benefits and risks<sup>29</sup> as well as will facilitate access of Ukrainian companies to international markets (including capital markets). In addition, Ukraine undertook relevant commitments under the EU-Ukraine Association Agreement, including implementation of Directive 2013/34/EU on the annual financial statements, consolidated financial statements

<sup>28</sup> See annexes: [https://issuu.com/uaenergy/docs/web\\_global\\_standards\\_transparency\\_a](https://issuu.com/uaenergy/docs/web_global_standards_transparency_a)  
<sup>29</sup> For the same purpose, it is advisable to switch to the internationally accepted mineral resources accounting systems, i.e. CRIRSCO for solid minerals and SPE (PRMS) for hydrocarbons. For more information see <http://www.dkz.gov.ua/files/36/%D0%A2%D1%80%D0%B5%D1%82%D1%8F%20%D0%BD%D0%B0%D1%83%D0%BA%D0%BE%D0%B2%D0%BE-%D0%BF%D1%80%D0%B0%D0%BA%D1%82%D0%B8%D1%87%D0%BD%D0%B0%20%D0%BA%D0%BE%D0%BD%D1%84%D0%B5%D1%80%D0%B5%D0%BD>

and related reports of certain types of undertakings. The relevant Draft Law 4646-д<sup>30</sup> is being considered by the Verkhovna Rada and deals with mandatory application of international standards by large undertakings and simultaneous reduction in the number of reports for small businesses, transparency of extractive companies and public access to financial statements of undertakings.

The Draft Law, *inter alia*, introduces a report on payments to the State for enterprises engaged in extraction of mineral resources of national significance. The new Law improves the procedure for submission and publication of financial statements for such companies in electronic format as well as imposes the obligation to provide copies of their financial statements upon request for public data access.

The Draft Law No. 6229 “On Ensuring Transparency in Extractive Industries” is absolutely consistent with the above document. It incorporates integrated requirements of the EITI Standard and EU directives, and sets a detailed procedure for preparation of reports on payments and the EITI reports. Its adoption will ensure mandatory disclosure of detailed information about extractive companies’ activities at the project level (see above), including the results of the audit of financial statements for the accounting period.

It is not the general legal environment that is strongly criticized, but specific Accounting Rules (Standards) 33 relating to expenditure on exploration of mineral resources which, according to experts, have many unregulated issues. In particular, there are no detailed accounting procedure for drilling works, constituting a greater part of exploration works, and detailed rules for depreciation of exploration assets<sup>31</sup>. However, in accordance with the explanations of the State Fiscal Service, starting from 1 January 2015, book value of fixed tangible assets related to exploration of mineral reserves shall be subject to tax depreciation<sup>32</sup>.

In this context, some questions arise to the current CMU Resolution of 04.02.1998 No. 118 “On approval of the List of expenditure on exploration (additional exploration) and construction of any mineral reserves (fields) with relevant expenditure on their development included in a separate group of the taxpayer’s costs subject to depreciation”.

30 [http://w1.c1.rada.gov.ua/pls/zweb2/webproc4\\_1?pf3511=62044](http://w1.c1.rada.gov.ua/pls/zweb2/webproc4_1?pf3511=62044)

31 <http://molodyvcheny.in.ua/files/journal/2016/4/23.pdf>

32 <http://sfs.gov.ua/baneryi/podatkovyi-konsultatsii/konsultatsii-dlya-yuridichnih-osib/print-67642.html>,  
<http://officevp.sfs.gov.ua/baner/podatkovyi-konsultatsii/konsultatsii-dlya-yuridichnih-osib/print-68888.html>



## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD

- *Adoption of the Draft Laws No. 4646-δ “On Introducing Amendments to the Law of Ukraine “On Accounting and Financial Reporting in Ukraine” (As Regards Improvement of Some Provisions)” and No. 6229 “On Ensuring Transparency in Extractive Industries” — Q3 2017;*
- *Entry into force, start of preparation of statements in accordance with the IFRS — since the beginning of 2018; and*
- *Development of amendments to the Tax Code (Section III) and to the regulations — Accounting Rules (Standards) 33, the list of costs subject to depreciation — in terms of adjustment of accounts of all expenditure on exploration of mineral reserves — Q1 2018.*



## RESPONSIBLE ENTITIES

- *State Fiscal Service*
- *Ministry of Finance*
- *Verkhovna Rada of Ukraine*

## Improvement of the regime for disclosure of information about ultimate beneficiaries

### DECISIONS

- *Introduction of amendments to the Laws of 14.10.2014 No. 1701-VII and of 21.05.2015 No. 475-VIII (as regards elimination of possibilities for companies to avoid disclosing beneficiaries and strengthening of responsibility)*
- *Introduction of amendments to the Law of 14.10.2014 No. 1702-VII (as regards lowering the participation threshold)*
- *Introduction of amendments to the Law of 14.09.1999 No. 1039-XIV (as regards expanding the requirements relating to disclosure of beneficiaries to production sharing agreements)*
- *Improvement of operation of the Unified State Register (distinction between owners and beneficiaries, search)*



### OPPORTUNITIES AND THREATS

Ukraine is one of the first world's countries to establish a legal framework for disclosure of beneficiaries of business entities. Such disclosure took place in 2014 when relevant data was added to the Unified State Register of Legal Entities, Sole Traders and Civic Formations (USR)<sup>33</sup>. In August 2017, publication of information about beneficiaries in an open data format and joining the Global Beneficial Ownership Register were declared<sup>34</sup>. The passport and relevant dataset in the open data format were published on the portal at [www.data.gov.ua](http://www.data.gov.ua)<sup>35</sup>.



However, since the very beginning the Register has not been operating in an appropriate way. First, the data on beneficial owners and founders of relevant companies is displayed as one entry, which creates confusion and a room for manipulations. Due to this, the "Beneficiaries" field often contains the data about legal entities, being founders, rather than about natural persons, especially when a company is registered in offshore jurisdictions<sup>36</sup>. In addition, there

33 <https://usr.minjust.gov.ua/ua/freesearch>

34 <https://www.facebook.com/volodymyrgroysman/posts/589970561171862>

35 <http://data.gov.ua/passport/73cfe78e-89ef-4f06-b3ab-eb5f16aea237>

36 [http://texty.org.ua/pg/article/editorial/read/79183/Bez\\_JeDRPOU\\_jak\\_bez\\_ruk\\_U\\_rejestri](http://texty.org.ua/pg/article/editorial/read/79183/Bez_JeDRPOU_jak_bez_ruk_U_rejestri)

are no other identifiers for natural persons, apart from surname, name and patronymic, which leads to confusion in case when personal data coincide.

Second, it is necessary to eliminate all legal gaps which allow avoiding disclosure of beneficial owners (e.g. for trusts and venture funds) as well as to strengthen the liability for a failure to provide information or provision of partial information. At present, a fine for such violation amounts to 300–500 tax-free minimum incomes, i.e. UAH 5,100–8,500 (equivalent of USD 200–350). For some companies that wish to hide actual owners it is easier to pay a fine that's why it is necessary to raise its amount.

One more important change is lowering the minimum threshold for beneficiary's participation in the legal entity's authorized capital or voting rights. At present, this threshold is 25% allowing for artificial formation of shares at the level of 24.99% to hide the owners. It should be lowered to 10%, i.e. substantial shareholding as defined in the Law of Ukraine "On Prevention and Counteraction to Legalization (Laundering) of the Proceeds of Crime or Terrorist Financing"<sup>37</sup>, being the basis of the anti-corruption law of Ukraine.

In accordance with the CMU Resolution of 30 May 2011 No. 594, for the purpose of participation in auctions for allocation of special permits for subsoil use, candidates shall submit documents disclosing their ownership structure up to the ultimate beneficial owner (controller). However, in practice, this provision did not help avoid a scandal with Yuzgaz B. V. (Netherlands) that sought to develop the Yuzivska area.

This incident is remarkable because the ownership structure created just in a month before the competition was not publicly open and did not disclose ultimate owners, but due to a legal gap (disclosure of beneficiaries is not applicable to production sharing agreements), the company won the competition. The decision was later cancelled by the Cabinet of Ministers. Therefore, it is advisable to expand the requirements relating to disclosure of beneficiaries to companies that seek to develop mineral resources under all licensing procedures granting subsoil use rights, including competitions on and concluding of production sharing agreements.

This means that the decisions on granting the rights to use subsoil should include evaluation of any corruption risks and potential conflict of interests based on disclosure of beneficial ownership and po-

<sup>37</sup> <http://zakon2.rada.gov.ua/laws/show/1702-18>

litically exposed persons (as applicable by the anticorruption legislation).

In Ukraine, no public authority is designated as responsible for verification of beneficial owners, and there is no relevant verification mechanism. It is proposed to designate the Ministry of Justice and entrust it with development of relevant procedure.

## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD



- *Current technical improvement of the Unified State Register: more machine readable formats, distinction between founders and beneficiaries, search improvement, ability to search in case of beneficiary change, timely data updates, unified transliteration standards, additional identification of beneficiaries by TIN or similar identifier — by June 2018.*
- *Development of a comprehensive Draft Law on introducing amendments to legislative acts of Ukraine as regards administration of data on ultimate beneficial owners (controllers) of legal entities (participation threshold, eliminating gaps, production sharing agreements, fines, authorized agency) — by February 2018.*
- *Considering and passing the Draft Law — by June 2018.*
- *Development and approval of the procedure for verification of beneficial owners (by the Order of the Ministry of Justice or the CMU Resolution) — by December 2018.*
- *Updating the Unified State Register, verification with further imposition of new penalties — since 1 January 2019.*

## RESPONSIBLE ENTITIES

- *Ministry of Justice, State Agency for E-Governance*
- *Verkhovna Rada of Ukraine*



## PART 2. LICENSING AND RIGHTS OF SUBSOIL USERS

Despite relatively positive RGI scores, the Ukrainian system for granting land use permits for extraction of mineral resources remains obsolete and is not very well adapted to the market mechanisms. Excessive discretion at numerous stages of the process and red tape leading to systemic delays are among its major shortcomings. According to calculations of the industry-specific Association of Gas Producers of Ukraine uniting public and private companies that cover 88% of gas production in the country, obtaining necessary documents (about 40 from 16 various public bodies and institutions) for putting a new field into industrial operation takes 42 months. Doubling of numerous permits and approvals creates unjustified corruption risks, and cancellation of up to 4/5 of them most likely will not result in any substantial deterioration of environmental protection, lowering of labour standards or in financial losses for the budgets<sup>38</sup>.

An already obtained licence (special permit for subsoil use) does not always warrant a lasting and unconditional right to exercise those titles. For example, the State Service for Geology and Mineral Resources of Ukraine conducts scheduled and out-of-schedule checks and requires application of licence holders for reassessment of the mineral reserves every 5 years, irrespective of the production regime<sup>39</sup>. In 2015, the above agency, by its Order, instructed its functional subdivisions to conduct a national assessment in the form of evaluation of the National Balance of Mineral Reserves subject to a repeated state examination of geological and economic appraisals of the respective mineral deposits insofar as it concerned valid special permits for subsoil use, including those suspended. The text of that Order has not been published on the Derzhgeonadra's website<sup>40</sup>. Moreover, on some occasions, even scheduled checks of the body may be arranged several days before their commencement.

38 <http://agpu.org.ua/analytics/section-infographics/rekomendaci-deregulyaciya-dozvilno-sistemi-u-naftogazovidobuvniy-galuzi.htm>

39 <http://www.geo.gov.ua/novyna/shchodo-vykonannya-p-25-polozhennya-pro-poryadok-provedennya-derzhavnoyi-ekspertyzy-ta-ocinky>

40 <http://www.geo.gov.ua/storinka/nakazy-derzhgeonadr>

Discretionary nature of such control measures implies extraordinary corruption risks and substantially reduces confidence and trust of the investors. Thus, although inspections are a proper instrument for securing the industry being compliant with the rules and legislation, the lack of due process, insufficient predictability and exorbitant discretion of the responsible authorities are identified as pitfalls requiring specific attention.

Albeit the fact that the above problem is multifaceted, the current system's weakest point is a public authorisation agency remaining non-reformed, i.e. the State Service for Geology and Mineral Resources of Ukraine. Despite approval of a new regulation governing principles of its functioning in 2015,<sup>41</sup> the agency hasn't yet undergone any fundamental modernisation. From among major problems of that agency, it is worth mentioning the following ones:

- *obsolete approaches to regulation, which do not conform to modern challenges in the industry and the economic development targets;*
- *potential conflict of interests as a result of combining functions of an authorisation agency with those of a traditional (academic) geological survey;*
- *excessive staffing (in total, about 3,400 people, including related bodies and companies) going hand in hand with a lack of reliable technological infrastructure and qualified personnel, which results from chronic underfunding;*
- *outdated geological database recorded by means of obsolete methods and techniques and stored mainly in a non-digital form;*

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<sup>41</sup> <http://zakon2.rada.gov.ua/laws/show/1174-2015-%D0%BF>

- *a corporate structure which is unjustifiably complex and consisting of numerous industrial, research and expert subdivisions which often exercise excessive functions, not characteristic of them, that are extrinsic for a licensing and regulatory agency, including their duties on management of the state's participatory interests in 11 companies through NJSC "Nadra Ukrayny";*
- *assessment of the agency's activities demonstrates that despite numerous academic functions and goals, it particularly focuses on issuing permits for subsoil use;*
- *Derzhgeonadra and other central executive authorities, and particularly, the MECl (insofar as it concerns energy resources), or even state-owned companies like, for example, PJSC "Ukrgezvydobuvannia" which is indirectly subordinate to the MECl, having doubling powers in development of the public policy related to the development of the extractive industry.*

Moreover, what still remains questionable is the formal status of the agency and even its founding document, since the Decree of the President of 2011 approving the Regulation on the Derzhgeonadra<sup>42</sup> still remains in force despite a new Regulation as approved by the Cabinet of Ministers in 2015. However, in accordance with the both regulations, the level of the Derzhgeonadra's independence is extraordinary low, as that agency is subordinate to the Cabinet of Ministers represented by the Minister of Ecology and Natural Resources, that being one more major shortcoming of the system for issuing permits for subsoil use. In particular, a frequent change of management and regular scandals as a consequence<sup>43</sup>, resulting in a situation where the Derzhgeonadra haven't had adequate leadership for about a year, are related to such political dependency.

Along with that, not all functions relating to issuing licences for mineral resource development are in the hands of the Derzhgeonadra. For example, in 2015, the Central Commission for Development of Gas, Gas-Condensate and Oil Fields was established under the MECl,

42 <http://zakon3.rada.gov.ua/laws/show/391/2011>

43 As of now, there is a remaining uncertainty about the outcome of a public competition for the agency's management positions, as the public competition's results have been canceled by the court. However, it didn't prevent the Cabinet of Ministers from appointing two winners of one of the competition's rounds as the Acting Head and acting First Deputy Head.

*inter alia*, entrusted with the tasks of consideration of development plans, feasibility studies as regards the investment projects on field development as submitted by the users of oil and gas bearing subsoil resources; drawing up of proposals on approval of the development plans, and setting permissible rates of oil, gas and gas-condensate extraction during research and industrial field development<sup>44</sup>. The above Central Commission's most dubious feature is the procedure of forming of its composition that is led by the MECI, at its own discretion, and including, among the others, the representatives of oil and gas producing companies. It poses a serious threat to competitiveness of the entire industry and creates extraordinary corruption risks, producing no added value for improvement of regulation at the same time (when obtaining special permits for subsoil use, the applicants undergo similar procedures).

As for geological data, the access to it is available in principle but the major part of the data is still kept in hard copies in the archives of the State Enterprise "Geoinform of Ukraine". Publication of the data obtained by the State or state-owned companies is prohibited as the data is classified as Secret or For Official Use Only.

If an extractive company seeks to sell or transfer to its contractors own geological information, i.e. such it has collected/purchased at its own expense, it has to agree the issue with the Derzhgeonadra. In practical terms, the value and quality of the data the subsoil users or potential investors are forced to buy<sup>45</sup> falls short of what they need. As the data is scattered through different public institutions or private companies, it is difficult to analyze survey, exploration and extraction of mineral resources at the prospective sites<sup>46</sup>.

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44 <http://zakon2.rada.gov.ua/laws/show/ru/z0025-16#n17>

45 From the speech of O. Prokhorenko, the Chairman of the Board, PJSC "Ukrzavzvydobuvannia", at the Round Table "Resource Governance Index 2017: "Home Work" for Ukraine" (Verkhovna Rada Committee on Fuel and Energy Complex, Nuclear Policy and Nuclear Safety, 12.07.2017)

46 [http://www.chamber.ua/Content/Documents/-58349842Gas\\_Oil\\_WhitePaper\\_UA\\_WEB.pdf](http://www.chamber.ua/Content/Documents/-58349842Gas_Oil_WhitePaper_UA_WEB.pdf)

## Liberalisation of the arrangements governing use and disclosure of geological information



### DECISIONS

- *Introduction of amendments to the CMU Resolutions No. 423 of 13 June 1995, No. 594 and 615 of 31 May 2011 as regards the procedure of access to geological information;*
- *Introduction of amendments to the CMU Resolution No. 1075 of 10 December 2008 as regards reviewing approaches to geological information value assessment; and*
- *Digitization of the data, establishment of “data room” of the State Research and Development Enterprise (SRDE) “Geoinform of Ukraine” for the subsoil users.*



### OPPORTUNITIES AND THREATS

Collection, storage, servicing and effective use of geological information resources has to serve public interest and the interests of the subsoil users. It requires cancellation of prohibitions and restrictions relating to the use of geological information, its declassification and making it non-confidential.

Amendments to the Resolutions Nos. 423, 594 and 615 are to open access to all secondary geological information. Exploration reports, well data sheets, well-logging records, reserves evaluation protocols etc. are to be available online.

Along with that, the businesses also advocate review of the approaches to geological information value assessment through amendments to the CMU Resolution No. 1075 of 10 December 2008<sup>47</sup>. They argue that the geological data of the Soviet era, which is sold by the State, do not meet modern challenges and needs, their value is rated against inflation and has no objective criteria for assessment, that is why those data are overpriced.

<sup>47</sup> <http://agpu.org.ua/analytics/section-infographics/rekomendaci-dereguljaciya-dozvilno-sistemi-naftogazovidobuvnij-galuzi.htm>

This is about information owned by the State (collected or purchased through the State Budget funds); the data collected by private companies in course of their activities is deemed to be their property and may be purchased by the interested parties, including investors. It is also useful to establish a unified register of the primary geological information with the contact details of its administrators.

Available geological information whose amount is estimated as 170 thousand volumes<sup>48</sup> is to be digitalised and a data room for work with it is to be created. This data is to be processed and published in an open data format, which makes it possible to process it by scanning devices. It is also worth considering its placement on data.gov.ua platform (by amending the CMU Resolution No. 835 of 21 October 2015 or on a voluntary basis).

It is reasonable if State Research and Development Enterprise “Geo-Inform of Ukraine” keeps the functions of administering such a register and servicing the portal. It is worth pointing out that rise in the quality of the services provided, as well as their format, will require relevant funding of that institution. At the same time, bringing payments for the secondary geological information in line with the economically feasible levels will aggravate a problem with the current assets even more. According to the Derzhgeonadra, the value of the geological information sold during 2016 amounted only to UAH 17 million, and for the first six months of 2017 — to UAH 14 million<sup>49</sup>.

The Derzhgeonadra has already started work on collection, systematisation and digitalisation of the geological information with the support of the Natural Resources Canada and Alberta Energy Regulator<sup>50</sup>. It goes about a project for creation of interactive maps with the scale of 1:200,000 and 1: 50,000. However, the existing amount of the international support and resources is insufficient for processing the entire body of data, which may linger for years to come.

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48 According to the Derzhgeonadra, one volume consists, on average, of 3 to 4 books, each containing hundreds of pages and tens of pages with diagrams in the annexes.

49 From the speech of the Acting Head of the Derzhgeonadra O. Kyryliuk at the Round Table “Resource Governance Index 2017: “Home Work” for Ukraine” (Verkhovna Rada Committee on Fuel and Energy Complex, Nuclear Policy and Nuclear Safety, 12.07.2017)

50 [http://geoinf.kiev.ua/wp/wp-content/uploads/2017/04/01\\_Boiarkin.pdf](http://geoinf.kiev.ua/wp/wp-content/uploads/2017/04/01_Boiarkin.pdf), <http://www.geo.gov.ua/novyna/derzhgeonadra-spilno-iz-mizhnarodnymy-ekspertamy-pidsumuvaly-pershyy-etap-proektu-geomap-200>



## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD

- *Development of a plan, negotiations with the donors and international organisations on funding, registration of the international aid project — Q3 2017;*
- *Creation of the Centre for Data Processing and Digitalisation — by the beginning of 2018;*
- *Amending the CMU Resolutions — Q1 2018;*
- *Digitalisation, processing, placement of the geological data — by 2020–2022; and*
- *Education, trainings for the Derzhgeonadra and “GeoInform of Ukraine” on the advanced techniques of the digitalised data processing and evaluation — on a permanent basis.*



## RESPONSIBLE ENTITIES:

- *Cabinet of Ministers of Ukraine*
- *Ministry of Ecology and Natural Resources*
- *Derzhgeonadra*
- *Ministry of Economic Development and Trade*

### DECISIONS



- *Simplified procedure for transition from the research to the industrial regime of the land property use to warrant such a transition for a responsible investor.*
- *Cancellation of the additional permits for full-fledged use of the sites provided, including unhindered shaving off the ground surface; liquidation of the overlapping documents and approvals, and particularly, patented mining claims.*
- *Enhancing the possibility for execution of a land servitude to oil and gas projects, solving the issue of enforceability and amount of the compensation on the part of the subsoil users for the damage caused during their operations.*
- *Development of the similar approaches to identification and settlement of the problems with the related extractive industries other than oil and gas sector whose problems are assessed with sufficient quality.*

### OPPORTUNITIES AND THREATS



Taking off the burden of over-regulation when formalising extraction of oil and gas resources has been among the priorities of the reform agenda for over a year. Among the latest real achievements, it is worth mentioning adoption of the Rules of Oil And Gas Fields Development<sup>51</sup>, which take into account modern best practices in regulation of that sphere and specifically set the rules of development of shale and other non-traditional hydrocarbon deposits. Abolishing of the necessity to obtain redundant doubling permits will substantially reduce corruption risks along the numerous stages of the process of obtaining land plots for the usage, and make it simpler and more transparent for the investors. As a result of removal of the restrictions relating to the agricultural category of lands having substantial deposits of mineral resources, a value realisation of the subsoils will substantially increase.

<sup>51</sup> <http://zakon2.rada.gov.ua/laws/show/ru/z0025-16#n17>

These efforts are, however, directed at a rapid increase in the extraction rates, especially in natural gas extraction, in pursuance of the Concept for Development of Ukraine's Gas Production Industry<sup>52</sup> (including the programme of PJSC "Ukrgezvydobuvannia" also known as the "Concept 20/20") rather than at bringing management of the extractive industries in line with the international standards. While these areas of the Government activities are formally different, at this stage, the priorities in the industry mainly coincide, which casts the necessity of scaling up and further improvement in regulation aside.

The approach of detailed but narrow settlement of the problems relating to oil and gas extraction, has both shortcomings and advantages. The major shortcoming, apparently, is ignoring specific problems of the extraction industry outside the oil and gas sector (mainly, it specifically concerns gas extraction). The example of that shortcoming is minor changes as proposed by the Draft Law No. 3096-д introducing special simplified rules specifically for the companies extracting oil and gas, by way of removing them from under general regulation instead of reformation of that regime for the entire industry. At the same time, the procedure for consideration and approval of a new version of the Subsoil Code of Ukraine aiming at resolving major part of the problems in a comprehensive and overall manner, was suspended, and a full-scale reform of the land market still remains a hostage of the complicated political environment.

Synergy of the related priorities within the reforms is an advantage, as warranting energy security, if not independence, is the Government's objective goal. This makes it possible to count on rapid results to be then developed and applied for the rest of the extractive industries provided that similar regulatory activities take place.

The potential threat to the deregulation process, an particularly, to successful adoption of the Draft Law 3096-д, is the fact that Ukraine, until now, has kept in place the moratorium imposed on the land market, and, in particular, the issue of the property right to land, and especially, in the context of the commercial activities of the private sector, primarily, the foreign private sector, is an extraordinarily sensitive from the political point of view<sup>53</sup>. Even on a condition of the changes in the political environment, it will take no less than 3 years to streamline legal provisions and create the preconditions for the structural reform related to the launch of the land market in Ukraine<sup>54</sup>.

52 <http://zakon2.rada.gov.ua/laws/show/1174-2015-%D0%BF>

53 <http://www.kse.org.ua/uk/research-policy/land/analytical/?newsid=2082>

54 <http://www.worldbank.org/uk/news/opinion/2016/10/17/26-years-of-land-reform-the-glass-is-half-empty-or-half-full>

The severity of that risk is not very high, as the moratorium and land deregulation insofar as it concerns subsoil use do not intersect directly — only insofar as it concerns a possibility of the use and purchasing land titles, for the purpose of extraction, to those land plots which fall into a category of agricultural land. However, some additional explanation of the benefits from these parallel processes may help in supporting the critical Draft Law 3096-д.

To make positive changes come true fast, the key factor is adoption of the Draft Law 3096-д as a whole and signing thereof by the President of Ukraine. In accordance with the transitional provisions of the Draft Law, after its entering into force, on the day following its publication, the Government will be bound to ensure, within 3 months, conformity of its regulatory acts and bylaws of the other Central executive authorities with legislation.

While resolving, by using point solutions, pressing problems which, at the same time, will lead to certain improvement in quality of the mineral resources management and make it possible to increase the extraction, one should not lose sight of a possibility of the comprehensive reform of this area of public policy. Development of an approach making possible settlement of more practical issues relating to a land plot with the potential wells or quarries, by way of obtaining a single unified document in a single body (with an account taken of the specific features of using land plots of various forms of ownership) would become the approximation to the international best practices. The best approach may involve comprehensive work on the adoption of a new version of the Subsoil Code of Ukraine and the Land Code of Ukraine (possibly, together with the wider activities on reforming the land relations outside the extractive industries).



## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD

- *Adoption of the Draft Law No. 3096-δ “On Amending Certain Legal Acts of Ukraine with the view of Simplification of Certain Aspects in the Oil and Gas Sector” — by the end of 2017.*
- *Entry of the Law into force — since 1 January 2018;*
- *Drafting new versions of the Land Code of Ukraine and the Subsoil Code of Ukraine — by mid 2018.*

## RESPONSIBLE ENTITIES:



- *Verkhovna Rada of Ukraine*
- *Verkhovna Rada Committee on Fuel and Energy Complex, Nuclear Policy and Nuclear Safety*
- *Verkhovna Rada Committee on Agrarian Policy and Land Relations*
- *President of Ukraine*
- *Cabinet of Ministers of Ukraine*

## Changes in the procedures of issuing special permits for subsoil use

### DECISIONS

- *Adoption of amendments to the laws of Ukraine with the view to establishing a single public licensing agency and divesting the line ministries of their regulatory and licensing powers.*
- *Modelling of a unified title deed comprising environmental, sanitary, licensing, engineering and — ideally — land titles necessary for the subsoil use, to be issued based on “one-stop shop” principle.*
- *Bringing the price of a special permit for subsoil use in line with the economically justified tariffs.*
- *Settlement of a procedure of appointing and carrying out of the scheduled and out-of-schedule checks.*



### OPPORTUNITIES AND THREATS

Deregulation and simplification of doing business is often declared as the priority task of the Government of Ukraine. Under the conditions, where warranting of energy security insofar as it concerns ensuring general demand for natural gas, gas-condensate and raw oil directly depends on such simplification, the above priority becomes an issue of the national interest. The most apparent way to accelerate its implementation is cutting time and more comprehensible stages of licensing procedures, which will substantially facilitate and accelerate the start of works at the new fields. Introduction of lesser and more effective regulation of the extractive industries is the only major precondition for a radical change in the investment rates in this sector, including foreign investments.



In particular, the comprehensive action on a modern reform of legislative acts and bylaws with the view to ensuring openness, transparency, cancellation of preferential treatment for certain categories of subsoil users, and providing access to geological information is

an essential part of the Concept for Development of Ukraine's Gas Production Industry as approved by the CMU Ordinance of 28 December 2016 No.1079-p<sup>55</sup>. With the view to the above, the Government commissioned the MECl, the MENR, the MEDT and the State Regulatory Service of Ukraine (SRS) with supporting the Draft Law "On Amending Certain Legal Acts of Ukraine with the view of Simplification of Certain Aspects in the Oil and Gas Sector" (No. 3096), as a matter of high priority. Drawing up and consideration by the CMU of a package of bylaws and codification of certain laws relating to extraction of hydrocarbons in Ukraine are among the strategic measures planned for 2017.

These priority measures on improvement of legal and regulatory framework, provided that implementation thereof starts immediately, will take 8 to 12 month. Deeper reform on consolidation of the functions of various supervisory and licensing agencies based on the principle of a "one-stop shop" will require a competent development of the respective concept and substantial time for it to be set out in the form of draft regulatory acts to be adopted. Creation of such a unified licensing structure may concentrate all the processes and procedures necessary for the launch of the research and industrial development of the mineral deposits, and divest the respective ministries of such powers, leaving to them only the functions of policy-making and implementation of public policy in the respective spheres.

Because the very increase in gas production is the strongest stimulus for introduction of more transparent, freer market environment with low tolerance to corruption, atrophy of that stimulus may put continuation of the ongoing reform in this sphere at risk. It is therefore worth mentioning non-systemic character of oil and gas production and its lack of sustainability as the dangers related to the approach to reformation of the extractive industry mainly focused on the rules of oil and gas production. Due to sufficiently efficient national programmes for gas substitution, energy saving and energy efficiency, entering the European natural gas market, such goal as increase in domestic production of gas as set by Ukraine for the purpose of enhancing energy security, is not very critical. In other words, it may be achieved by 2020 or 2021 through relatively unsubstantial improvements in the system of mineral resources management or even without them at all, account taken of the easiness of managing a single state enterprise covering almost 75% of gas production.

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55 <http://www.kmu.gov.ua/control/uk/cardnpd?docid=249766439>

## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD



- *Introduction of relevant amendments to the Mining Code and the Land Code and laws on the public regulatory policy, on oil and gas, on regulation of the urban development activities — by the end of 2018;*
- *Amending the Procedure of issuing special permits for subsoil use as approved by the CMU Resolution of 30 May 2011 No. 615, the Procedure for holding auctions for the sale of special permits for subsoil use as approved by the CMU Resolution of 30 May 2011 No. 594 — by mid 2018.*
- *Introducing amendments to the Methodology for setting the starting price at the auction for a special permit for subsoil use through amending the CMU Resolution of 15 October 2004 No. 1374 — Q3 2018;*
- *Amending the Regulation on the State Service for Geology and Mineral Resources of Ukraine as approved by the CMU Resolution of 30 December 2015 No. 1174 — by the end of 2018; and*
- *Development and approval of the concept of an umbrella-type licensing agency responsible for the comprehensive support of the investors in the sphere of extraction of mineral resources — up to mid 2019.*

## RESPONSIBLE ENTITIES:

- *Verkhovna Rada*
- *Verkhovna Rada Committee on Fuel and Energy Complex, Nuclear Policy and Nuclear Safety, the Parliamentary Committee on Industrial Policy and Entrepreneurship*
- *Verkhovna Rada Committee on Environmental Policy, Nature Resources Utilization and Elimination of the Consequences of Chernobyl Catastrophe*
- *Cabinet of Ministers of Ukraine*



## Structural reform of the State Service for Geology and Mineral Resources of Ukraine



### DECISIONS

- *Development of the concept of the Derzhgeonadra's structural reform with the view of cancellation of its redundant functions and powers and transformation of that Service into the informational and academic institution;*
- *Drawing up and approval of a unified regulation on the Derzhgeonadra's activities to be approved by the Cabinet of Ministers, as well as establishing or designation of an independent authorisation (licensing) agency (see above);*
- *Conferring an exclusive competence in development of the public policy on subsoil management, including as regards mineral and energy resources and extractable resources, with the single public regulatory and supervisory authority — up to the end of 2018.*



### OPPORTUNITIES AND THREATS

According to the report of the international experts being a part of the composite work group of the US and Canadian geological surveys and EuroGeoSurveys, *"the current structure [of SGSSU] is, in many ways, dysfunctional, fragmented, complicated, severely underfunded and lacks a clear mission"*<sup>56</sup>. Loss of powers and duties in respect of managing state-owned enterprises and winding up of respective corporate and functional subdivisions are to become the most important changes in functioning of the renewed Service. Similarly, the Service has to be divested of active powers in issuing permits for subsoil use, with that function to be transferred to an independent, possibly new, agency. The main goal of the renewed body in the extraction industry of the country should be informational support of the investors and service companies by way of collection, procession and provision of the geological and geophysical information, relevant mapping and scientific research.

<sup>56</sup> [http://geoinf.kiev.ua/wp-content/uploads/2016/06/SGSSU-Assessment\\_A4\\_UKR.pdf](http://geoinf.kiev.ua/wp-content/uploads/2016/06/SGSSU-Assessment_A4_UKR.pdf)

A full-fledged reform of the Derzhgeonadra will require profound work on modelling restructuring of separate directorates and subdivisions under the current organisational structure, with clear allocation of functions and resources into authorisation (licensing) and scientific and informational activities. Depending on the scope of foreign financial and technical aid, as well as on the political will of the people's deputies, relevant ministries and the CMU, development and approval of the related amendments may take up to 12 months.

Substantial strengthening of the Service's informational and consulting function owing to the loss of extrinsic licensing and regulatory powers may become the outcome of its reform. Analytical and recommendation products of the renewed Service will aim at methodological advice on balancing interests of various stakeholders in the process of mapping of the extraction activities, including the interests of the state, local communities and private investors. Good example of such an activity would be the Planning Practice Guidance for Onshore Oil and Gas drawn up by the Department of Energy & Climate Change (DECC), UK<sup>57</sup>.

Critical need for the Service's reform being as quick as possible is confirmed by the regular scandals relating to its ineffectiveness. For example, the head of the biggest gas producer, the state-owned company "Ukrgezvydobuvannia" blames the Service of sabotaging issuance and extension of the licences, absent which the company will be unable to implement an ambitious programme aiming at increase in production. According to him, none of the 55 packages of applications submitted during the last 18 months had been successful<sup>58</sup>.

Therefore, an acute phase of criticism and apparent ineffectiveness of that agency will facilitate the fast settlement of the problem with the Derzhgeonadra's ineffectiveness. Profound and systemic reformation of the Service instead of a mere job swap of its leadership is to be the goal of civic activists, international donors and the team of reformists. Such a risk is real because settlement of a conflict situation relating to an appointment of a new Service's head, dominates now the public discourse regarding the reform of the Derzhgeonadra.

The start of the Derzhgeonadra's collaboration with the energy regu-

57 [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/224238/Planning\\_practice\\_guidance\\_for\\_onshore\\_oil\\_and\\_gas.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/224238/Planning_practice_guidance_for_onshore_oil_and_gas.pdf)

58 <http://glavcom.ua/interviews/oleg-prohorenko-bagato-lyudey-vjetsyia-navkolo-ukrgazvydobuvannya-425581.html>

lator of the Canadian province of Alberta and the Geological Survey of Canada<sup>59</sup> demonstrates the available possibilities for the foreign support in the reform of the Service. It is apparent that in order to deliver a reform, preparatory work on development of the future model, powers and responsibilities of a renewed body, is necessary. At the same time, current situation in the Service without a full-blooded and legally capable leadership casts doubts about the probability of a launch of that process, and the line minister is also sure of that<sup>60</sup>.

At the same time, current situation, which is extremely complicated from the political point of view, may lose edge particularly due to the functional redirection of that body. In other words, standardisation of the Service's mission and priority redirected to the academic and informational activities will make it possible to substantially reduce corruption risks when new leadership is appointed. This is exactly direction of priority reforms recommended in 2016 by a dedicated commission consisting of the representatives of similar bodies of Canada, the USA and the EU, whose task was evaluation of the current effectiveness of Derzhgeonadra<sup>61</sup>.

A need for creation and ensuring independence and professionalism of a new public licensing agency inheriting functions of issuing licences for subsoil use will become the major challenge in that reformation of the Derzhgeonadra. The examples of a number of the countries analysed during the independent assessment of the Derzhgeonadra show that such separation of functions is a generally accepted international practice, and similar transformations once took place with the relevant bodies in Poland and Lithuania, in particular<sup>62</sup>.

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59 <http://www.geo.gov.ua/fotogalereya/derzhgeonadra-otrymaly-pidtrymku-vid-kanadskyh-ekspertiv-shchodo-reformuvannya>

60 [https://biz.censor.net.ua/resonance/3023029/ostap\\_semerak\\_nayiblishim\\_viklikom\\_dlya\\_mene\\_stalo\\_pomnyati\\_mdj\\_mnsterstva\\_yak\\_odnogo\\_z\\_nayiblish\\_korumpovanih](https://biz.censor.net.ua/resonance/3023029/ostap_semerak_nayiblishim_viklikom_dlya_mene_stalo_pomnyati_mdj_mnsterstva_yak_odnogo_z_nayiblish_korumpovanih)

61 [http://geoinf.kiev.ua/wp/wp-content/uploads/2016/06/SGSSU-Assessment\\_A4\\_UKR.pdf](http://geoinf.kiev.ua/wp/wp-content/uploads/2016/06/SGSSU-Assessment_A4_UKR.pdf)

62 <http://geoinf.kiev.ua/wp/wp-content/uploads/2016/04/Annex-D-Case-Studies.pdf>

## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD



- *Development and approval of the concept of the Derzhgeonadra's structural reform with the view of cancellation of its redundant functions and powers and transformation of that service into the informational and academic institution — up to mid 2018;*
- *Adoption of the new version of the Regulation on the State Service for Geology and Mineral Resources of Ukraine as approved by the CMU Resolution of 30 December 2015 No. 1174 — by the end of 2018.*
- *Drawing up and approval of the amendments to the Law of Ukraine "On the Cabinet of Ministers of Ukraine" and Regulations of MECl, MENR, MEDT — Q1 2019.*

### RESPONSIBLE ENTITIES:

- *Verkhovna Rada of Ukraine*
- *Cabinet of Ministers of Ukraine*
- *Ministry of Ecology and Natural Resources*



### PART 3. IMPACT OF ON-SITE DEVELOPMENT OF NATURAL RESOURCES

Insofar as it concerns implementation of a current policy on assessment of environmental impact of the extraction projects on local environments, Ukraine is driven by its direct and specific international obligations, and in particular, by the Convention on Environmental Impact Assessment in a Transboundary Context<sup>63</sup>, the Convention on Access to Information, Public Participation in Decision-Making and Access to Justice in Environmental Matters<sup>64</sup>, and EU-Ukraine Association Agreement (Article 363<sup>65</sup> and Annex XXX<sup>66</sup>), and by the Treaty establishing the Energy Community (Directive 2011/92/EU).

At the same time, process of approving of necessary legislation has not been accomplished yet (the Draft Law of Ukraine “On Strategic Environmental Assessment”<sup>67</sup> is still pending, and serious obstacles are expected in implementation of the adopted Law of Ukraine No. 2059-VIII “On Environmental Impact Assessment”). In particular, it is about the lack of agreement of a new SEA procedure with the actual practices and relevant legislation on design and construction of industrial and infrastructure (including extractive) facilities<sup>68</sup>, which has been a result of technical replacement of the state ecological assessment with the EIA procedure instead of the profound change of the approach to regulation of such design and construction, account naturally taken of carrying out environmental impact assessment. The adopted law’s weak point is also its certain internal inconsistency as regards holding public hearings and taking account of the stakeholders’ opinion when approving a final decision on carrying out planned activities. In particular, Article 7 of the Law doesn’t stipulate comprehensive and detailed procedure of holding such hearings and retains possibilities for certain groups to influence the outcomes of the public hearings or substantially ignore their conclusions, which may bring to naught the essence of the entire procedure and the corruption risks.

Taking interests of the local communities into account when devel-

63 [http://zakon2.rada.gov.ua/laws/show/995\\_272](http://zakon2.rada.gov.ua/laws/show/995_272)

64 [http://zakon2.rada.gov.ua/laws/show/994\\_015](http://zakon2.rada.gov.ua/laws/show/994_015)

65 [http://zakon3.rada.gov.ua/laws/show/984\\_011](http://zakon3.rada.gov.ua/laws/show/984_011)

66 [http://www.kmu.gov.ua/docs/EA/Annexes\\_title\\_V/30\\_Annex.pdf](http://www.kmu.gov.ua/docs/EA/Annexes_title_V/30_Annex.pdf)

67 [http://w1.c1.rada.gov.ua/pls/zweb2/webproc4\\_1?pf3511=61186](http://w1.c1.rada.gov.ua/pls/zweb2/webproc4_1?pf3511=61186)

68 <http://www.rac.org.ua/uploads/content/233/files/eiadraftlaw2009a.pdf>

oping deposits of extractable resources in Ukraine often fades into insignificance when necessary priority reforms are assessed in the extraction sector. Only a deep-rooted lack of trust to the businesses on the part of the local authorities and residents, resulting in delaying in providing necessary documentation has made that problem actual and has finally brought about partial decentralisation of the rent to be paid by the oil and gas producing companies<sup>69</sup>.

The fact that the framework law introducing decentralised rent is set out in extraordinarily general terms (in fact, it sets only a basic rule stipulating allocation of 2% of the amount of the rent to an oblast budget, 2% — to a raion budget, 1% — to the budgets of the communities where hydrocarbons are located/extracted) is a serious challenge. Such a brevity in law-making and oil and gas producing companies' imperfect system of accounting and reporting may create a whole series of problems in further implementation — from geographic, chemical and commercial accounting of the extracted resources from specific wells to uncertainty as regards the regime of the usage and purpose of appropriations to be allocated to the local budgets. Low, albeit gradually rising<sup>70</sup>, institutional capability of the local governments, including newfangled united territorial communities (UTCs), is not going to facilitate rapid getting of the effective system of accounting, receipt and use of the additional funds up and running either. There is no procedure in place for disclosure of information from the tax statements on the rent paid by the extracting companies to the benefit of the stakeholders like raion and oblast councils. Finally, as expected, the extracting companies themselves will have to develop culture of filling in the annexes to the tax returns on the respective rent payments bound to the village and settlement councils in whose territory hydrocarbons are extracted, which will imply execution of documents at a whole new level than before.

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69 <http://zakon2.rada.gov.ua/laws/show/1793-19> (enters into force on 01.01.2018)  
70 [http://www.niss.gov.ua/content/articles/files/terutor\\_gromad-86ead.pdf](http://www.niss.gov.ua/content/articles/files/terutor_gromad-86ead.pdf)

# Implementation of legislation on environmental impact assessment and disclosure of ecological information



## DECISIONS

- *Accomplishing adoption of the framework legislation on EIA, and particularly, the Draft Law No. 6106.*
- *Specifying and standardisation of an environmental impact assessment procedure, in pursuance of the Law No. 2059-VIII;*
- *Standardisation of the rules governing creation of the commissions for environmental impact assessment, including requirements to relevant experts; launch of the register listing such experts;*
- *Upon adoption of the draft law No. 6106, a procedure of the monitoring and the public hearings as provided therein, is to be drawn up and adopted;*
- *Development of a comprehensive support programme and educational programmes for the local communities and line associations, with the view to making EIA a real tool for protection of rights and interests.*



## OPPORTUNITIES AND THREATS

After a serious pressure from a wide coalition of foreign partners and local civil society<sup>71</sup> caused by an unexpected decision of the president of Ukraine to veto the adopted laws on EIA<sup>72</sup>, final adoption of the law on strategic environmental assessment looks inevitable. Nonetheless, the very history of adoption of that legislative package proves the importance of the public hearings and monitoring of the legislative process by public. Taking the President's proposals into account when revisiting the draft law will also facilitate its successful adoption, as well as substantial incorporation of the provisions laid down in the respective EU directives implemented by both laws.

<sup>71</sup> <http://epl.org.ua/en/announces/mizhnarodni-organy-odnogosno-zaklykayut-ukrayinu-pryjnyaty-zakon-pro-otsinku-vplyvu-vetovanyj-prezydentom-ukrayiny/>

<sup>72</sup> <http://en.interfax.com.ua/news/economic/380464.html>

Like the other initiatives, new to Ukraine, which both civic activists and “champions” in the powers that be have managed to bring to a stage of adoption as framework legislation, implementation and fleshing out, the EIA procedures mainly depend on the adoption of high quality, balanced secondary legislation capable of minimising risks emerging from a sufficiently general approach adopted in the framework legislation. In particular, the law No. 2059-VIII fails to regulate in quite clear and comprehensive manner the procedure of finalisation of a binding EIA report. Moreover, Article 7 stipulates that the expenditure related to the public hearings are to be borne by an economic operator (a potential investor), which may, under certain circumstances, have substantial impact on the outcomes of such hearings.

Insufficient institutional capacity of the Ministry of Ecology and Natural Resources and related central executive authorities may pose a threat to proper materialisation of the laws’ spirit and letter. Technical and advisory support of the foreign partners could accelerate this work and warrant high quality of the draft bylaws.

Such factors as protracted process of development of lower level technical regulatory framework or development of the provisions capable of letting certain parties to the process to delay some procedures in environmental impact assessment and emasculate its real goals, stand in the way of timely and full implementation of all provisions contained in new legislation. Under the worst scenario, instead of the effective instrument making it possible to take account of the public opinion and interests, Ukraine may get another burdensome bureaucratic obstacle which would, in particular, reduce attractiveness of the investments in extraction projects. Much higher institutional capacity of the leaders of the local communities which are the parties most interested in a new procedure, may help to prevent that problem from arising, and that, in its turn, may become the result of the MENR’s effective and proactive work on development and dissemination of information and training documents, holding educational workshops and carrying out other educational activities. Effectiveness of such measures may be scaled up massively provided that there is co-ordination with the public sector and specialised international organisations and foundations.

At the same time, it is important not to lose sight of all various stakeholders involved in a procedure of environmental impact assessment. Even under the conditions of correct and full taking into

account of the public authorities' and local residents' interests, disregard of the lawful rights and interests of the extractive companies is potent to substantially worsen perceptions of the above instrument by the investors and reduce mutual trust between the communities and investors even more. That risk may be minimised at the level of high quality modelling of a map and interests of all stakeholders.

Awareness raising and training activities should be held on the permanent basis, account taken of the fact that it is essential to come up with the effective approaches and introduce best practical techniques to EIA as early as at the initial stages.



## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD

- *Adoption and signing by the President of the finalised Draft Law on the strategic environmental assessment No. 6106 — by the beginning of 2018.*
- *Drawing up and adoption of the regulation on the unified register of strategic environmental assessment, a procedure of submission of the documentation for the EIA report, a procedure of funding of the environmental impact assessment, and a procedure of public hearings in the process of environmental impact assessment in the form of the Cabinet of Ministers' resolutions — Q1 2018;*
- *Following adoption of the Draft Law No. 6106, drawing up and adoption of the procedure of monitoring of the consequences of the environment state planning document's implementation, including for the public health; as well as of the procedure of public hearings of the urban development documents in the form of the Cabinet of Ministers' resolutions — Q1 2018;*
- *Drawing up and adoption of the regulations of the EIA expert commission and qualifying requirements to the experts, and of the procedure of keeping register of EIA experts, in the form of a resolution of the Ministry of Ecology and Natural Resources — Q2 2018.*

• *Drawing up and implementation by the Ministry, in co-operation with the local state administrations and NGOs, of a procedure and timetable of educational and training programmes with the view of enhancing quality of public hearings during EIA — by mid 2018.*

### **RESPONSIBLE ENTITIES:**

- *Verkhovna Rada of Ukraine;*
- *Verkhovna Rada Committee on Environmental Policy, Nature Resources Utilization and Elimination of the Consequences of Chernobyl Catastrophe;*
- *President of Ukraine;*
- *Cabinet of Ministers of Ukraine;*
- *Ministry of Ecology and Natural Resources;*
- *Local state administrations, other bodies of local self-government;*
- *Environmental NGOs and Ukraine's international partners*



## Efficient introduction of legislation on decentralisation of the rent



### DECISIONS

- *Development of a standard contract mechanism for implementation of the provisions of the Law No. 1793-VIII between an extractive company and an oblast council capable of warranting compliance with mutual rights and obligations of the parties throughout the validity of the permit;*
- *Development and adoption of the methodology for assessment of actual hydrocarbons extraction rates for each individual field and well;*
- *Amending the Tax Code and the Budget Code of Ukraine capable of: (a) warranting the right of the members of local governments to obtain information from individual rent statements by the related companies, and (ii) setting clear rules of reporting as to the tax obligations on payments of the rent for subsoil use not only to the State Budget but also to the budgets of individual oblasts and raions; and*
- *Development and adoption by the Ministry for Regional Development, Building and Housing and the Ministry of Finance of the recommendations on the receipt, accounting and use of the funds obtained by the local budgets within the framework of rent decentralisation, capable of ensuring exclusive use of the above resources in the sphere of social and economic development of the respective community in the producing area and/or as compensation for the damage caused to local environment.*

## OPPORTUNITIES AND THREATS



In a view of the fact that companies will begin first direct payments to oblast and raion budgets no sooner than as from January 2018, the issue of implementation of the legislation on decentralisation of the rent still retains a number of unclear moments. That very lack of mutual trust between the private sector and the local governments the reform aims to lift, may become an embarrassment in the way toward that goal because of the confrontation between those parties. However, a public position of the Association of Gas Producers of Ukraine, and actual *ad hoc* start of working out the mechanism to that end in Poltava Oblast<sup>73</sup>, show that there is a huge mutual interest of both sides to make sure that the initiative as to the rent decentralisation is implemented in the best possible way.

The problem of lack of incentives to issuing new permits for subsoil use by the local governments is most pressing in Poltava Oblast. Due to delay of real positive changes for the local communities following the adoption of the Law No. 1793-VIII, the Oblast Council is not in a hurry to restore productive collaboration with the companies. During the last year, the Oblast Council issued no such permits at all, and in order to obtain such documents now, the extractive companies are forced to negotiate with the local governments on the individual basis, conclude individual “social” agreements providing for additional payments to the local budgets<sup>74</sup>.

Greater confidence of the oblast and raion councils in actual receipt of additional funds in a transparent and foreseeable manner, and confidence of the local communities in securing the use of those additional funds for clearly defined purposes of development and social and economic support, capable of building up a long-lasting trust between the sides. That is because additional detailed but, nonetheless, simple and comprehensible rules of implementation of the Law No. 1793-VIII by the executive authority are vital for the resulting effectiveness of this reform. Moreover, in order to accelerate the drafting process and improve the quality of such rules, one should understand that further delaying of the agreement procedure in respect of extraction projects at the level of local governments will lead to especially negative outcomes for the investment attractiveness of the industry and for realisation of the government’s plans on substantial increase in domestic natural gas production.

73 <https://goo.gl/PjtCD6>

74 <https://tribuna.pl.ua/news/oblasna-rada-dala-dozvil-na-nadrokoristuvannya-privatnij-kompaniji/>

Finally, despite all various tiers of local self-government, the changes in the budgetary process in favour of the local authorities generally coincide with the vector towards decentralisation of powers, including on financial and budgetary issues, and that is why oblast and raion councils, if they desire so, may avail themselves of the techniques and experience of united territorial communities accumulated during all this time.



## EXPECTED OUTCOMES AND IMPLEMENTATION PERIOD

As practice shows, drawing up of regulatory documents capable of regulating new legal relations between the local governments and companies extracting natural resources, is already underway. Seizing an initiative from certain local councils and standardisation, unification of the process would draw nearer emergence of positive outcomes in the budget year 2018. Also, agreements should be transparent, as should payments so that citizens can monitor them and ensure that they make it into public spending. Preparation of the mechanisms of adequate accounting of resources extracted from individual wells, and, respectively, of the rates of the rent payments in favour of individual local budgets will make it possible to avoid conflicting data and will enhance general transparency of those new practices.

- *Development and adoption of a standard contract mechanism for implementation of the provisions of the Law No. 1793-VIII between an extractive company and an oblast council capable of warranting compliance with mutual rights and obligations of the parties throughout the validity of the permit in the form of the CMU Resolution — Q3 2018;*
- *Development of the methodology for assessment of actual hydrocarbons extraction rates for each individual field and well — by mid 2018;*
- *Drawing up and introduction of the amendments to the Tax Code and the Budget Code of Ukraine — by mid 2018.*
- *Development and adoption by the Ministry for Regional*

*Development, Building and Housing and the Ministry of Finance of the recommendations on the receipt, accounting and use of the funds obtained by the relevant local budgets within the framework of rent decentralisation — by the end of Q1 2018.*

### **RESPONSIBLE ENTITIES:**

- *Verkhovna Rada of Ukraine*
- *Cabinet of Ministers of Ukraine*
- *Ministry for Regional Development, Building and Housing of Ukraine*
- *Ministry of Finance*
- *State Fiscal Service of Ukraine*



# 2017

quarters

## III-IV

- Passing the Draft Laws No. 4646-д and No. 6229
- Introducing amendments to the Resolution No. 835 (2011)
- Designating the Authorized Agency in charge of the single portal
- Development of a project for large-scale digitalization of geological data
- Passing the Draft Law No. 3096-д
- Passing the Draft Law No. 6106-д

# 2018

## I

- Entry of the Laws into force
- Start of preparation of statements in accordance with the IFRS
- Approval of the Information Disclosure Procedure and the Procedure for Handling Cases Involving Violations
- Development of amendments to the Tax Code and Accounting Rules (Standards) as regards expenditure accounting
- Establishment of the data digitalization centre under the Derzhgeonadra
- Drawing up and adoption of the regulation on the unified register of strategic environmental assessment, procedures for submission of documents, funding and holding public hearings in the process of environmental impact assessment
- Drawing up and adoption of the procedure for monitoring of the consequences of the environment state planning document's implementation as well as of the procedure for public hearings as regards draft urban development documents
- Development and adoption of the recommendations on the receipt, accounting and use of the funds obtained by the relevant local budgets within the framework of rent decentralisation

## II

- Approval of the form of the consolidated production and payment report
- Setting reporting thresholds
- Development of the Terms of Reference for the single portal
- Completion of technical improvement of the Unified State Register (data on beneficiaries)
- Development of amendments to the Laws No. 1701-VII, 1702-VII, 475-VIII, 1039-XIV (beneficial ownership)
- Introducing amendments to the CMU Resolutions No. 423 (1995), 1075 (2008), 594 (2011), 615 (2011) relating to geological information and licensing procedures
- Development of draft laws introducing amendments to the Mining Code and the Land Code and laws on the public regulatory policy, on oil and gas, on regulation of the urban development activities
- Drawing up the procedure and timetable of educational and training programmes with a view of enhancing quality of public hearings during EIA
- Drawing up and adoption of the regulations of the EIA expert commission and of the procedure of keeping register of the EIA experts
- Development of the methodology for assessment of actual hydrocarbons extraction rates for each individual field and well

- Development and testing of the software environment for e-reporting
- Passing legislative amendments (beneficial ownership)
- Introducing amendments to the CMU Resolution No. 1374 (2004) as regards starting price for special permits
- Development of draft amendments to the Land Code of Ukraine and the Subsoil Code of Ukraine
- Development and approval of the concept of the Derzhgeonadra structural reform
- Development and adoption of a standard contract mechanism for implementation of the provisions of the Law No. 1793-VIII between an extractive company and an oblast council
- Drawing up and introduction of amendments to the Tax Code and the Budget Code of Ukraine (in terms of regulation of implementation of the Law of Ukraine No. 1793-VIII).

III

- Launch of the single portal
- Creation of a database (register) of contracts
- Approval of the procedure for verification of beneficial owners
- Introducing amendments to relevant laws and codes
- Introducing amendments to the CMU Resolution No. 1174 (2015) as regards Regulation on the Derzhgeonadra

IV

## 2019

- Start of updating the Unified State Register and verification
- Approval of amendments to the Law of Ukraine "On the Cabinet of Ministers of Ukraine" and Regulations on the MECI, the MENR, and the MEDT

I

- Development and approval of the concept of an umbrella-type licensing agency

II

- First submission of reports according to new requirements

III

- Certification of the software environment for e-reporting

IV

## 2020+

- Completion of the data room project

