

## ANNEX 2 - ACTION FICHE UKRAINE AAP 2011

### 1. IDENTIFICATION

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

### 2. RATIONALE

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

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

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

Project proposals presented for approval to the Steering Group:

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

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

Project proposals for information to the Steering Group:

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

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

## 2.1. Sector context

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

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

The Ukrainian Energy Strategy till 2030, adopted in 2006 and currently under revision, calls for substantial energy-saving measures in all industries, as well as for a noticeable increase in the use of renewable energies, from current 0.1 billion kWh up to 2.0 billion kWh by 2030. The Government has launched a number of measures to promote investments in renewable energies, starting with the introduction of green tariffs and tax incentives, and has set ambitious targets to replace or upgrade obsolete equipment in the industrial and residential sectors, in order to significantly decrease energy consumption and CO<sub>2</sub> emissions.

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

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

## 2.2. Lessons learnt

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

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

## 2.3. Complementary actions

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

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

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

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

- Under the **EU Covenant of Mayors** initiative, 16 large cities of Ukraine have now taken the commitment to go beyond the target of 20% CO<sub>2</sub> reduction by 2020 through the implementation of Sustainable Energy Action Plans, to be supported by the EU. Implementation of those Sustainable Energy Actions Plans could be supported by the Fund created under the E5P initiative. A specific technical assistance project in support of the Covenant of Mayors in the region is foreseen.

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

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

#### **2.4. Donor coordination**

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

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

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

### **3. DESCRIPTION**

#### **3.1. Objectives**

The purpose of the Fund is to allow a harmonised and effective delivery of international financial support over several years by pooling contributions from a group of donors and beneficiaries, to be used primarily for supporting energy efficiency and environmental projects, resulting in a significant reduction of carbon dioxide (CO<sub>2</sub>) and other greenhouse gases (GHG) emissions.

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

The main expected results of the proposed action are:

- A reduced energy consumption in Ukraine and in the countries of the region, thanks to a more efficient use of available energies. This will be achieved through the implementation of projects contributing decisively to this objective. Implementation of those projects will be supported by the Fund resources, on a proportional basis;
- A decrease in CO<sub>2</sub> and other greenhouse gases emissions in the region, thanks to decreased energy consumption;

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

#### **3.3. Risks and assumptions**

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

#### **3.4. Crosscutting Issues**

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

### **3.5. Stakeholders**

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

## **4. IMPLEMENTATION ISSUES**

### **4.1. Method of implementation**

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

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

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

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

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

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

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

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

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

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

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

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

Energy efficiency will be measured for example by the saving of energy (kWh p/a), reduced use of natural gas (cubic meters p/a), electricity efficiency (MWh p/a) and its equivalent in monetary terms (UAH, € p/a) and environmental benefits by the decrease of CO<sub>2</sub>/NO<sub>x</sub> emissions (tonne p/a), decrease in water use (cubic meters p/a) and the consumption of treated water (cubic meters p/a).

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

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

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

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