

**Promoting the Use of Performance-Based Contracts  
between Water Utilities and Municipalities in EECCA**

**Case Study No. 4: Berdyansk Miskvidokanal Public Utility  
(Berdyansk City Water Utility)**

**Chysta Voda-Berdyansk Concession Contract**



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*This report is also available in Russian under the title:*

***Содействие применению контрактов, основанных на показателях деятельности, между предприятиями ВКХ и муниципалитетами в странах ВЕКЦА***

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## FOREWORD

This report presents the results of a review of a concession contract awarded to a domestic private operator to manage the Berdyansk City Water Utility (Berdyansk Miskvidokanal Public Utility). This concession contract was signed between the Executive Committee of the Berdyansk Town Council and the Chysta Voda (Clean Water) private company in September 2008 for a period of thirty years.

The findings and conclusions of this report aim to support the Ukrainian government in its efforts to further improve the design and implementation of future performance-based contracts in the country in the water sector in line with international best practices. The report provides an objective analysis of the most important aspects of the contract (legal and financial aspects, performance indicators, etc.), identifies its strengths and weaknesses and proposes a set of recommendations for improvements. The OECD *Guidelines for Performance-Based Contracts* served as a benchmark to assess the concession contract.

The report was prepared in the framework of the Task Force for the Implementation of the Environmental Action Programme for Central and Eastern Europe (EAP Task Force), whose secretariat is located in the OECD's Environment Directorate. The project was managed by Nelly Petkova, with support provided by consultants Guy Leclerc and Francois Thueux (from PricewaterhouseCoopers) and Aliona Babak from Ukraine. The preparation of this report was financially supported by the EU Tacis.

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The views expressed in this report are those of the authors and do not necessarily reflect those of the OECD or its member countries.

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## **List of abbreviations**

BIP	Business Investment Plan
BMPU	Berdyansk Miskvidokanal Public Utility
CEE	Central and Eastern Europe
CM	Council of Ministers
EAP TF	Task Force for the Implementation of the Environmental Action Programme for Central and Eastern Europe
EECCA	Eastern Europe, Caucasus and Central Asia
EU	European Union
IDA	International Development Association of the World Bank Group
IFI	International financing institution
NGO	Non-governmental organisation
OECD	Organisation for Economic Co-operation and Development
USD	US Dollar
UAH	Ukrainian Hryvnia
WSS	Water supply and sanitation

## Exchange rates

In the conversion of financial data presented in this report, the following annual average exchange rates were used:

**Table 1. Exchange Rates, Hryvnia /USD and Euro; Yearly Average**

	2000	2001	2002	2003	2004	2005	2006	2007	2008 <sup>1</sup>
Hryvnias/USD	5.44	5.37	5.33	5.33	5.32	5.12	5.05	5.05	5.01
Hryvnias/Euro	5.03	4.81	5.03	6.02	6.61	6.39	6.34	6.92	7.66

1. Average data for 6 months. Monthly data for September are 4.85 and 6.99, respectively.

Source: IMF, World Economic Outlook database, October 2008, National Bank of Ukraine.

## Map of Ukraine



## EXECUTIVE SUMMARY

### Objectives of the review

This report reviews the performance-based contract for the Berdyansk Miskvodokanal Public Utility and provides a set of recommendations for its improvement. These recommendations can be considered by the Ukrainian government either within the framework of the existing contract (to the extent possible) or in designing future contracts for the water supply and sanitation sector.

The contract assessment was based on international good practices, such as those contained in the OECD's *Guidelines for Performance-Based Contracts*. The second major objective of this review was to identify good practices in the design and implementation of the contract, use these practices in updating the Guidelines and make them more relevant to the EECCA context.

### Background

Since its independence in 1991, Ukraine has undergone significant political and economic changes. Along with macroeconomic stabilisation, the government agenda focused on accelerating Ukraine's institutional transition toward a modern market economy. The municipal and housing sector has received particular attention. The government created a dedicated Ministry of Housing and Municipal Economy in March 2007 and is working on a new Housing Code and a Law on the Water Regulator. The process of decentralisation has transferred the responsibility of managing the previously state-owned water and sanitation services to the municipalities. The water utilities were transformed into communal-property enterprises. In parallel, the central government decided to eliminate the budget subsidies to these utilities.

As a result and due to the quick deterioration of water supply and sanitation facilities, the sector needs significant capital investments. Private sector participation in managing water infrastructure was seen as a possible way to finance these investments. The Ukrainian legislation has then been modified to allow a broader involvement of the private sector.

The concession agreement between the Executive Committee of Berdyansk Town Council and Chysta Voda-Berdyansk is one of the first contracts involving a private partner in the water sector in Ukraine. Under this concession contract, the Berdyansk Town council transfers the management, the development and improvement of the water and sanitation infrastructure to a private Ukrainian contractor. The Operator was selected in late 2008, through a tender procedure and the contract was signed in September 2008 for a period of 30 years (the contract allows for an additional extension of 20 more years). The operator has to pay a concession fee to the concessioner on a quarterly basis. No financial penalty or bonus is envisaged in the contract. The contractor's main responsibilities include: management, operations and maintenance of the utility but also the modernisation of the existing infrastructure and its development. The bulk of the commercial risk and all the capital and investment risks are now supported by the operator.

The overall conclusion of the review is that this concession contract contains most of the general requirements that need to be included in such types of contracts. The report has identified some good practices in the preparation of the contract. It also discusses some issues related to the specific elements of the contract, particularly those that could lead to possible conflicts between the operator and the Berdyansk Municipality.

## **Good practices in contract design and preparation**

The major good practices identified with regard to the contract preparation phase are highlighted below:

- The contract follows the legal requirements set in the Ukrainian legislation and more specifically in the Law on Concessions. The principles concerning concessions identified in this law are broadly in line with the major international standards for concession contracts (this implies: contract signed for a long period of time, assets remaining the contracting authority's property, operation risks borne by the operator, investments for extension, repair and maintenance of the facilities designed and carried out by the operator).
- The tender procedure has been open to non-Ukrainian companies which helps guaranteeing a fair competition and the attraction of experienced companies.
- The selection criteria identified for the selection of the winner reflect the most common criteria used in many countries in such a process.
- The 5 bidders were allowed to meet with representatives of the utility to obtain a better understanding of its technical and financial situation.
- The operator is required to provide the Contracting Authority with an annual report for the monitoring of its activities.
- The contract requires that all staff members be transferred from the previous utility (BMPU) to the new operator. The operator is given full responsibility for managing the company's personnel, with no undue influence from the contracting authority. This shields the contractor from political and external interference in its operational management.

## **Challenges to contract preparation and implementation and related recommendations**

Despite the good intentions and the good practices identified above, some specific issues for further consideration have been identified during our review. They concern the contract preparation stage, the selection procedure and the contract itself. The main issues identified and subsequent recommendations are related to:

- Having a long-term concession may be a viable option given the specific circumstances (need for massive investments) and providing that there is a strong and realistic contract in place which ensures that the expectations of the contracting authority are well defined and protected. Though, the lack of experience of the municipality with public-private partnership contracts and tender procedures could be compensated by:
  - ✓ Recommendation 1: Involving experienced experts in drafting the tender documentation and designing the selection criteria and evaluation procedure.
  - ✓ Recommendation 2: If possible, starting the cooperation with a private partner by a "lighter" type of contract (management contract or lease contract) providing the municipality has a sufficient capital investment budget or can attract other public (including international) sources of financing to fund investments in the utility.
- Even if the Berdyansk concession contract is prepared in line with the national legislation and with the Law on Concessions in particular, some elements should be further or better specified in order for the contract to meet international standards.
  - ✓ Recommendation 3: The contract should specify such issues as the treatment of assets, need of evaluating the assets and related investments, performance indicators, procedures and guidelines to adjust and review tariffs.

- ✓ Recommendation 4: The government should speed up the establishment of an independent water regulator in order to ensure that all the parties' interests are well-balanced and protected. The main functions of such a regulator can include, among others, setting service standards, developing affordability guidelines, designing and managing public expenditure programmes to support water utilities.
- The contract lacks major performance indicators as currently only one indicator is included (the minimum annual amount of investments). This lack of clear performance indicators implies that it will be difficult for the contracting authority to objectively assess the improvement of the level of service in the future and it will have no legal means to put pressure on the operator. Such a situation could lead to future conflicts between the parties.
  - ✓ Recommendation 5: Consider selecting a few key indicators to include in the contract. Such indicators should be easy to measure and monitor and should be financially achievable. They should be specified for each year and should also reflect the most urgent and critical issues to be solved by the operator. Such indicators could include: weighted average number of daily hours of drinking water services, percentage of individual subscribers billed on the basis of metered consumption, weighted average water bacteriological safety compliance.
  - ✓ Recommendation 6: Carefully assess the technical and financial conditions of the utility at the very start of the contract: the baseline data must be sufficiently accurate to avoid further conflicts between the parties. A good solution would be to define them in conjunction with the previous operator, under the control of an independent auditor.
  - ✓ Recommendation 7: Consider appointing an independent auditor to monitor the achievement of the performance targets. The technical auditor should be selected carefully and paid sufficiently well to do his job properly and honestly.
- Responsibilities of the different stakeholders involved in the tariff setting procedure are not clearly defined in the contract. Moreover, the contract does not specify how the tariff can be increased to finance investments for rehabilitation or extension of the facilities. The main recommendations are:
  - ✓ Recommendation 8: Simplify the regulation for tariff setting and tariff revisions as there are too many laws/decrees containing contradicting requirements, particularly those regarding the involvement of Local Councils and of Local State Governments (Oblast).
  - ✓ Recommendation 9: Define a clear methodology for annual water price revision to avoid political interferences and aim at covering operating costs and a portion of investment costs.
  - ✓ Recommendation 10: Determine in the contract how the investment part, which will not be included in the tariff, will be financed at local, regional and/or national levels in order to avoid financing gaps and inefficiency in the investment programmes implementation.
- No penalty or bonus is envisaged in the contract (mainly because the measurement of the operator's performance cannot be assessed). This gives few means of pressure for the contracting authority to make the operator meet the objectives set in the contract.
  - ✓ Recommendation 11: The contract should envisage financial penalties for two particular cases:
    - If the performance objectives set in the contract are not met;
    - If the main requirements of the contract are not met (in the Berdyansk case: mainly Business Investment Plan and the annual report).

- The preparation of an annual report by the operator to monitor and report on the contract implementation is a good practice. However, the contract does not specify the nature of the information to be included in this report and does not envisage the control of this report by an independent party.
  - ✓ Recommendation 12: The contract should clearly define the nature of the information to be provided in the annual report (for example: details on the levels of service, investments made in the contract year and planned for the next years, details of the assets acquired, disposed of or replaced by the operator during the contract year, etc).
  - ✓ Recommendation 13: The data provided in the annual report should be verified by a technical auditor in order to assess if those data are correctly calculated and interpreted.
- The conflict resolution mechanism envisaged in the contract does not specify the means to avoid the recourse to the jurisdictions, such as conciliation, mediation or arbitration which are usually used before moving to the court option. The conflict resolution mechanism which seems to be the most suitable for this contract is the arbitration.
  - ✓ Recommendation 14: An arbitration clause should be added to the contract describing the arbitration procedure that will apply and clearly defining the scope of the disputes to be arbitrated.
- There is no mention in the contract of the possibility for the operator to dismiss employees after the enforcement of the contract. Moreover, the operator has no obligation to develop and implement a training programme to improve the skills of the employees although this is a key condition to improve the productivity of staff.
  - ✓ Recommendation 15: The operator should be explicitly given the right to reduce staff costs (by decreasing the number of staff) if this is necessary for the optimisation of the operations. However, the contract should envisage a clear procedure for justifying closing job positions and staff who lose their jobs should be properly protected and should get all social benefits in accordance with the Ukrainian legislation.
  - ✓ Recommendation 16: The contract should include an article related to the training of staff and increasing their competencies in modern management practices, such as computer literacy, accounting, and technical safety at work.
- The rationale for the selection of the operator was not officially published. The reasons for awarding the contract to Chysta Voda-Berdyansk are thus not known to the public.
  - ✓ Recommendation 17: The rationale for the selection of the operator should be made available to the public. This is particularly relevant as there have been concerns among the city population with regard to inviting a private operator to provide water services to Berdyansk.

## CHAPTER 1. INTRODUCTION

Since its independence in 1991, Ukraine has undergone significant political and economic changes. Along with macroeconomic stabilisation, the government agenda focused on accelerating Ukraine's institutional transition toward a modern market economy. The municipal and housing sector has received particular attention. The government created a dedicated Ministry of Housing and Municipal Economy in March 2007 and is working on a new Housing Code and a Law on the Regulator. The budget code continues to subject municipal borrowing to tight central control, but bond issues and guarantees to utilities by municipalities (which are allowed under the budget code), are nonetheless increasing in reflection of this emerging priority.

Recently, in search of new investments in the water sector, the Ukrainian government has encouraged more private sector participation. While contracts with private operators are common in the energy sector, there still very few water utilities in the country which are managed by private water companies. Concession contracts seem to be the preferred type of private sector participation in the water sector in Ukraine. More and more municipalities are getting interested in involving private operators. The use of other types of PBCs is very limited, with few lease contracts that have been signed (most notably in Odessa and Lugansk). As such, the Berdyansk concession contract is among the first concession contracts in the water sector in Ukraine and can serve as an important benchmark and an example from which other cities can learn from.

### 1. Objectives of the review

The major objective of the Review was to conduct an independent and objective evaluation of all important aspects of the concession contract signed between the Executive Committee of the Berdyansk City Council and the operator Clean Water-Berdyansk in line with good international practices, such as those contained in the OECD's *Guidelines for Performance-Based Contracts*. The report analyses the strengths and weaknesses of the contract and proposes a set of recommendations for further improving the contract's effectiveness and efficiency. These recommendations are particularly relevant given the government's intentions to encourage other performance-based contracts in the future. Thus, the review aims to support the Ukrainian Government in its efforts to improve the design of such contracts. These recommendations do not pretend to be comprehensive; instead they are focused on selected issues which were identified as particularly important with regard to the smooth implementation of the contract.

Through this analysis, the review also seeks to identify good practices and draw conclusions which can then be used to further improve the relevance of the Guidelines with regard to specific EECCA experience. This experience was largely missing in the first version. In this context, the Berdyansk experience is extremely valuable as it demonstrates how other Ukrainian cities and other EECCA countries, for that matter, can implement performance-based contracts in the water sector.

### 2. Performance review process and methodology

In discussions with the Ministry of Housing and Municipal Utilities in March 2008, Berdyansk was identified as a city which has embarked on involving the private sector in managing its city water utility. OECD was interested to study and analyse the experience of the city. In July 2008, the Berdyansk municipality and the Berdyansk water utility agreed to participate in this project and have the concession contract reviewed by the OECD/EAP Task Force Secretariat. The EU Tacis provided

financial support for the project. The project was implemented under the supervision of the OECD and with the support of a team of consultants from PricewaterhouseCoopers.

The methodology developed to evaluate the contract is based on the good practices identified in the Guidelines. It consists of a detailed questionnaire coupled with direct interviews. The questionnaire was sent to the major stakeholders involved in the process. The review involves three stages: preparatory activities, review and drafting mission, and preparation of the final report.

A comprehensive set of background documents concerning and relevant to the concession contract were examined by the review team prior to and after the review mission (see the Section on References). The review mission took place from 30 September to 3 October 2008 when the team visited Berdyansk and Kiev. During that time the team engaged in discussions with staff of the Berdyansk water utility, the Berdyansk municipality and City Council and experts from the Ministry of Housing and Municipal Utilities, who were all directly or indirectly involved in the preparation of the contract (See Annex V). Unfortunately, the Operator did not accept to meet the team performing the review mission. The results and recommendations presented in the report were discussed at a meeting with the participation of major stakeholders on 15 December 2008 in Berdyansk. In addition, the main lessons learnt from this review will be presented at other international fora and will be disseminated through other meetings and mechanisms.

This report provides an opportunity and is a basis for discussion within the Ukrainian Government to further strengthen the design of such performance-based contracts.

## **Box 1. Major good practices identified in the Guidelines for Performance-Based Contracts**

### **1. Project scope**

#### **(i) Definition of contractual objectives and responsibilities**

The contract should define as precisely as possible the objectives to be achieved; establish the rights, obligations and responsibilities of each contractual party as well as joint responsibilities; identify a clear, reliable and efficient mechanism allowing the parties to quickly and efficiently respond to any new circumstances that may arise in the course of contract implementation.

#### **(ii) Service area**

The service area should be clearly identified early in the process and preferably before Due Diligence is conducted. The extent of the service area has a direct impact on the costs and revenues of the operator. A proper evaluation of the costs and revenues should be carried out in order to establish adequate contractual objectives and consequent performance indicators.

### **2. Legal and institutional framework**

#### **(i) Legal framework**

Before entering into a performance-based contract, the applicable legal framework, including all relevant laws and regulations should be carefully studied and assessed. Based on this analysis (as part of the Due Diligence process), the best contractual model should be selected. If changes in the law are needed, these should be made before the contract is finalised. The selected type of contract should be tailored to the needs of the utility while making the best possible use of the legal framework.

#### **(ii) Institutional framework**

The institutional set-up should provide for proper regulation and monitoring of the contract implementation. The regulatory authority should be given a sufficient level of independence in order to ensure that all the parties' interests are well balanced and protected.

### **3. Performance indicators**

#### **(i) Initial evaluation**

Before selecting the performance indicators, the parties to the contract should conduct detailed evaluation of the technical and financial conditions of the water utility in order to fully assess its pre-contractual performance. Such an evaluation will allow the parties to agree on realistic performance indicators given the existing state of the utility.

#### **(ii) Selection of performance indicators**

The contract should clearly specify all performance indicators that will be monitored during contract implementation and the mechanisms for their adjustment. If the operator's remuneration is based on the achievement of selected indicators, these should also be clearly identified. Performance indicators could be linked to the financial performance of the utility (e.g. operating ratio, collection efficiency), efficiency of operations (unaccounted-for-water, pipe breaks), operating performance (average hours of service, population served). The performance indicators should be few, simple, realistic and easy to measure to be able to properly monitor their achievement.

#### **4. Tariffs and financial obligations of the contracting authority**

##### (i) Tariffs setting and adjustment

A sound tariff policy should balance considerations related to the utility's financial viability, its social objectives and economic efficiency. The contract should allow for tariffs to be adjusted over time (tariff revision mechanisms) both in relation to inflation and improvement of services as well as in response to force majeure events or changes in the legal regime. Cross-subsiding should be avoided and replaced, if necessary, by transparent subsidy schemes targeted at well-identified poor households.

##### (ii) Financial obligations of the contracting authority

When public authorities are fully (e.g. service or management contracts) or partially (e.g. lease contracts) responsible for financing the investment programmes of the water utility, these obligations should be clearly defined in the contract, both in terms of amounts and timeframe of investments. In order to avoid conflicts during the implementation phase, the contract should draw a clear distinction between maintenance works, replacement works and emergency situations.

#### **5. Financial penalties, bonuses and incentives**

##### (i) Financial penalties

In the context of EECCA water utilities, which often face significant financial difficulties, penalties should be used with utmost prudence. In order to avoid putting at risk the general financial health of the utility, and consequently its operational capacity, penalties should be used only when utilities are operated by private contractors. Imposing a penalty would directly affect the ability of the utility to meet the performance levels specified in the contract.

##### (ii) Bonuses and incentives

If properly designed, bonuses and incentives could contribute significantly to the achievement of the level of services provided by a contractor. When the utility is run by a publicly-owned contractor, bonuses should be provided directly to individuals and not to the utility because no individual will benefit directly from higher performance levels of the utility. When the utility is run by a private operator, incentives should reflect the productivity gains of the utility.

#### **6. Monitoring**

Setting an effective system to monitor contract implementation is crucial for evaluating if parties meet their obligations and achieve specified targets. Monitoring provisions should focus on the contractor's success to meet the targets rather than on how it meets these targets. In countries where governments face limited monitoring and regulatory capacity, the monitoring function should be outsourced to an auditing company. The government should then reconfigure its task as monitoring the auditor.

#### **7. Contract enforcement / Contract resolution mechanisms**

Performance-based contracts should include formal dispute resolution procedures (e.g. judicial, quasi-judicial, administrative, arbitral). Arbitration should be the preferred dispute resolution mechanism in contracts that include a foreign private entity. The main advantages of arbitration include confidentiality (as it relates to commercial secrets); expertise (arbitrators are selected on the basis of their technical expertise); neutrality (arbitrators are chosen from among individuals unrelated to the parties in the dispute); integrity (arbitrators are chosen from among individuals of high moral repute).

**8. Risks**

Any long-term contractual relationships involve risks such as: operation and maintenance risks, revenue risks, regulatory risks, political risks. The allocation of key risks should be carefully considered when designing performance-based contracts. Risks should be fairly allocated among parties. The risks should be allocated to the party that is best suited to assume them both in terms of technical expertise and the possibility to mitigate the risk at least cost.

**9. Costs**

In considering implementing performance-based contracts, the public authorities should be aware of all costs, both direct and indirect, that such contracts may entail to the public sector. Apart from traditional “costs”, (overheads or expenditures inherent to the project), there are costs incurred due to indirect “losses” (e.g. costs of hiring consultants to prepare the contract, un-monitorable performance targets). Usually, the contract does not include provisions related to indirect costs. However, during the negotiation stage, the parties should always consider all actual and potential costs inherently and indirectly associated with performance contracting.

## CHAPTER 2. THE CONTEXT

This chapter briefly introduces the current developments in the water supply and sanitation sector in Ukraine. It looks at the legal and regulatory framework for managing water utilities in the country. In addition, it describes the main premises of the current concession contract.

### 1. Current developments of the water supply and sanitation sector

With regard to its water resources, Ukraine is one of the poorest countries in Europe (the annual per capita water supply totals 1 700 m<sup>3</sup> per year, whereas, for the sake of comparison, it is 4 570 m<sup>3</sup> in France, 7 280 m<sup>3</sup> in Switzerland, 7 700 m<sup>3</sup> in Austria and 24 000 m<sup>3</sup> in Sweden)<sup>1</sup>. Yet, Ukraine's population consumes more per capita than most countries in the region. The daily average water consumption per capita amounts to 320 litres per day, while generally European cities report between 100 to 200 litres per capita. However, rural water consumption reaches only 60 litres per capita and per day, due to the weak connection rate to water supply networks in those areas<sup>2</sup> (26% on average, see below). Starting in 1995, there has been a gradual decrease in water consumption: an average 2-4% annual decrease due to economic stagnation, higher water tariffs, water metering, decrease of water availability and access to it.

In addition, offer and demand for water resources are extremely unbalanced in Ukraine: the greatest amount of water resources (58%) is in boundary regions of the Danube river basin, where demand for it does not exceed 5% of the resource. On the contrary, the least quantities of water resources are in the industrial regions of Donbass, Kriviy Rig, Crimea and the southern regions of Ukraine (where Berdyansk is located) where the main consumers are concentrated.

Regarding water supply and sanitation, the current situation in Ukraine shows that:

- In most municipalities, the current water sector service levels are quite low. Many water utilities are not able to provide a 24-hour continuous supply.
- The water quality is often not consistently adequate and deteriorates over time (especially in flood seasons).
- The water and wastewater networks are in a very poor condition as a result of a backlog of investment in maintenance and repair.

About 70% of the Ukrainian population (but only 26% in rural areas) is provided by centralised water supply. The water supplied comes mainly (75%) from surface water sources which require heavy treatment as compared to ground water. 53% of the population has access to sewage system/sanitation (74% in urban areas and only 9% in rural areas).

According to the Ukrainian Water Association, water resources are reportedly used and polluted more intensely than in any other European country. The lack of permanent access to clean drinking water is an important environmental, as well as health issue in Ukraine. Since independence, substantial progress has been made towards cleaning up the rivers but much remains to be done. Although most of the urban population is connected to the water distribution system, the existing networks are

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<sup>1</sup> Dobryanskiy, L. (2003), Water and Waste Water International, Kiev and Manukalo, V., Development of the Surface Water Quantity and Water Quality Monitoring in Ukraine: Problems and Needs, Kiev.

<sup>2</sup> Kuznyetsov, V., Decision-making on the reform of urban water services in Ukraine, USRIEP, Kiev.

overburdened. Inefficient sewage plants that need repairs or rehabilitation and were constructed to meet obsolete water quality standards (former USSR regulations now out-of-date) are polluting centralised water supply sources. Sewage effluent treated by these plants is discharged into rivers, which are then used for drinking water resources in centralised systems.

In terms of technical conditions, it is estimated that:

- 26% of water supply and sewerage networks are in an emergency state;
- 40% of pump stations require major repair or replacement;
- the number of pipe bursts reaches a level of 2 per 1 km.

Most of the Ukrainian water supply and sewage facilities cannot meet existing water regulations without a massive rehabilitation of their water supply and wastewater treatment facilities<sup>3</sup>. This major effort requires a mixed approach involving national water reforms, private capital and international financial assistance and investments.

Since 1995, there have been several State Programmes related to improved water supply and sanitation. The main are:

- State Programme on centralised water supply for the rural settlements which use the transported water (for the period 2002-2008). Now, this programme will be extended until 2010.
- State Programme 2005 “Drinking Water of Ukraine”.

Numerous countries and international financial institutions have provided assistance to the water sector over the past ten years, such as DEPA, USAID, EBRD and the World Bank. Despite all these efforts it has become obvious that new solutions are needed. One of the avenues explored has been the involvement of the private sector in the management and operation of water infrastructure.

The concession contract for the water utility in Berdyansk is one example of a private-public partnership. Berdyansk is a medium-sized city located in Southern Ukraine on the coast of the Azov Sea. The service area of the Berdyansk Miskvidokanal Public Utility includes the city of Berdyansk and one village. The utility supplies water to around 49 500 consumers (109 000 individuals on a population of 118 000, and companies). Around 35 700 subscribers (or 77 000 people) are connected to the sanitation network. The utility produces drinking water mainly from raw water purchased by the Oblast and withdrawn from the river Dniepr. The raw water is brought to Berdyansk through a 175 km-long pipe. The raw water is treated at the start of the pipe but it needs a second treatment at its end due to the bad conditions of the pipeline. In addition, the leakage rate all along the pipe is very high. All this results in a high purchasing cost (0,75 UAH /m<sup>3</sup> as compared to the 4,02 UAH / m<sup>3</sup> price for individuals).

The Berdyansk Miskvidokanal Public Utility operates:

- One water treatment plant;
- One wastewater treatment plant;
- Pumping stations;
- A water distribution and sanitation networks (384 km).

The main technical problem is related to the pumping stations which are very old and whose operating costs are then very high. The overall leakage rate on the network is also high: around 42%. Due to the

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<sup>3 3</sup> Dobryanskiy, L. (2003), Water and Waste Water International, Kiev and Manukalo, V., Development of the Surface Water Quantity and Water Quality Monitoring in Ukraine: Problems and Needs, Kiev.

<sup>3</sup> Kuznyetsov, V., Decision-making on the reform of urban water services in Ukraine, USRIEP, Kiev.

lack of financial resources, the water infrastructure in the city has been rapidly deteriorating. To raise much-needed investments and improve the system, the City Council has opted to seek private sector financing. This process has led to the current concession contract.

## 2. Regulatory context

The *Water Code of Ukraine (of June 6, 1995)* identifies roles and responsibilities of representative and executive bodies in regulating water relations. Water supply requirements in Ukraine are based on former USSR regulations that are now out-of-date; however the government is trying to adjust its legislation and regulatory acts to approximate them with those of the European Union (EU) (e.g. Directive 2000/60/EC or the Water Framework Directive (WFD)).

### 2.1. Regulations on drinking water and drinking water quality monitoring

- *The standard No. 2874-82 “Drinking water. Sanitary requirements and quality control” (adopted in 1982)* is the State standard currently in force to regulate drinking water quality. This includes standards for physical properties, chemical and bacteriological composition of water used for the drinking water supply.
- *The state sanitary rules and standards “Drinking water. Hygienic requirements of quality of water used for economic purposes” (1996)*. These rules provide stricter approaches for current and new indicators of water quality. These standards include 56 parameters instead of the 28 indicators in Standard No. 2874-82.
- A new *State Standard of Ukraine No. 4808-2007 “Sources of centralized drinking water supply. Hygienic and ecological requirements to the water quality and rules of a choice”* has been adopted (2007) and will enter into force in 2009.
- Finally, a new *State Standard of Ukraine “Drinking water. Requirements and quality control”* has been developed but has not yet been adopted.

### 2.2. Regulations on payments for water use and wastewater discharges

The Law on Environmental Protection of 25 June 1996 defines the type of nature protection payments (including payments for discharges of effluents into water and payments for the placement of production and consumption of waste in the environment) as well as the types of payments for the use of natural resources (including payments for water use). This law is administered by three main government agencies: the Ministry of Nature Protection (which designs/introduces the economic instruments and controls the volumes of pollution and natural resources use); the Ministry of Finance and Economy (which proposes the pollution charge rates and allocates the charge revenues) and the State Tax Service (which collects the payments). Each enterprise providing water services pays a fee for special water use (water abstraction and discharges). The amount of the fee is based on actual volumes consumed. The Law also sets limits for water consumption. An additional fee is applied when exceeding this limit.

### 2.3. Regulations on provision of water supply and sanitation services

- According to the *Law on Local Self-Governance* (of 21 May, 1997, Art. 28), local governments are held responsible for providing high-quality water supply services. In this context, local governments are authorized to enter into contractual relationship with enterprises (having various forms of ownership) for water service provision to consumers.

- The *Law on Drinking Water and Drinking Water Supply (No. 2918-III of 10 January 2002)* determines the legal, economic and organizational principles of the use of the drinking water supply system. It applies to business entities which supply drinking water and bodies of executive power or local authorities which regulate and monitor water quality, state of sources and the drinking water supply systems as well as consumers of drinking water. Activities linked to drinking water supply can be carried out by entities having any form of ownership, but infrastructure cannot be subject to privatization. This prohibition reflects the *Law on Privatization of State Property of March 4, 1992, No. 2163-XII*.
- Economic activities carried out by water suppliers are subject to licensing. The application for a license has to be addressed to the *State Committee on Water Resources*, which will validate (or not) the compliance with drinking water regulations
- The Law on Concessions (No. 997-XIV of 16 July 1999) is the main legislative act in the area of concessions in Ukraine. This law governs the procedure for the concession of state- and municipally-owned facilities, including the procedure for the possession and use of the concession facilities and the, payment of concession fees.

#### 2.4. Regulations on tariff setting for water supply and sanitation services

- The *Law on Local Self-Governance (Law No. 280/97 of May 21, 1997, Art. 28)* establishes that local governments have a primary responsibility for setting respective tariffs for communally-owned enterprises and negotiate them with non-communally owned companies.

Indeed, following the transfer of assets to local governments, in 1997, the Cabinet of Ministers (CM) has delegated the powers to set tariffs for communal services (including for water supply services) to the oblast state administrations, and the Kyiv and Sevastopol city state administrations and the Crimean Council of Ministers (*CM Decree No. 1168 of 28 October 1997, "On Improvement of the State Tariff Regulation System for Housing and Communal Services"*). The transfer of responsibility for tariff setting from the state to the local governments also envisaged the termination of subsidies from the state to the water supply companies to cover the difference between approved tariffs and the actual cost of service provision. Those subsidies were previously paid to the suppliers from the state budget in order to reduce tariffs for residential customers. As a result, the *Law No. 776-XIV of June 29, 1999, "On the State Budget for 1999"* did not envisage any subsidies to communal utilities to cover the losses resulting from the difference in actual and approved tariffs for residential customers. No money was budgeted by the state for the compensation of losses of water operators since the second half of 1998 until 2006, when the subsidy mechanism was renewed by the state.

### **3. Institutional context**

The institutions in Ukraine with direct responsibilities for the management of the water sector at national, regional and local levels include:

#### **3.1. At national level**

##### **1. The Cabinet of Ministers of Ukraine**

The main responsibilities of the Cabinet are the implementation of the policies, the organization and coordination of programmes and activities of the state executive bodies, approval of

protection zones covering more than one oblast<sup>4</sup>, setting the regimes of sanitary protection zones, defining the objectives of centralized water supply as well as rules of withdrawing certificates to housing and communal services. The cabinet also defines the type of information required in relation to the quality and status of drinking water, the procedure for the approval of contracts for provision of housing and communal services and approval procedure for the setting of tariffs.

## 2. The Ministry of Housing and Communal Economy

This Ministry is the main actor at the national level regarding water sector issues. Indeed, it is responsible for the definition of procedures for monitoring drinking water quality and water supply systems, coordination of the implementation of the programmes for the protection of drinking water supply centralised systems; coordination of activities of regional authorities, enterprises, institutions, organisations, reporting at national level on the state of the drinking water industry, calculation of tariffs for centralised water supply and wastewater systems, control of the implementation of regulations as well as compliance of the providers, licensing, design of tariff setting rules, implementation of research outputs in relation to water resources management.

## 3. The Ministry of Economy

One of its main responsibilities is to control water tariff setting and their application in each oblast.

## 4. Ministry of Environmental Protection

The Ministry of Environmental protection is divided into several committees with their own specific responsibilities, such as:

The State Committee on Water Resources: *The Committee on Water Resources* is responsible for allowing water abstraction in the framework of the permitting system for special water use.

The Committee of Geology and Mineral Resources and the Committee of Hydrometeorology: *These two Committees* are responsible for protecting and monitoring groundwater sources.

## 5. The Epidemiological Inspectorates of the Ministry of Health

*The Epidemiological Inspectorates* are responsible for the control of drinking water quality.

## 6. Antimonopoly Committee of Ukraine

*The Antimonopoly Committee* controls regulations associated with economic competition, prevention, detection, and termination of violations of the laws on anti-monopoly (e.g. the Law on economic competition protection, Law on protection from unfair competition).

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<sup>4</sup> Typical Ukrainian administrative entity.

### 3.2 At regional and local levels:

#### 1. Executive oblast administration bodies

In each Oblast of Ukraine, there is a *Department of housing and communal services* which is administratively subordinated to the Ministry of Housing and Communal Economy and integrated in the oblast state administration. In the Autonomous Republic of Crimea, the *Council of Ministers of Autonomous Republic of Crimea* (and its own Ministry of Housing and Communal Services) are the key administrative bodies in this sector.

The main responsibilities of the Departments of housing and communal economy in the oblasts include: licensing, financing enterprises transferred into management of the local state administration of housing and communal economy, controlling tariffs for housing and communal services, approving tariffs for water supply and wastewater services, organizing and conducting programmes aiming at improving water and wastewater facilities, imposition of fines and sanctions to water suppliers when water quality standards are not met.

#### 2. Local governments (city, rayon and village levels)

Local governments' responsibilities include: approval of programmes within the water sector, allocation of funds from the local budget for water infrastructure projects, informing the public regarding procedures for setting up water tariff, approval of regulations on water consumption and water quality, preparing contracts for delegating the operation of water utilities to water suppliers and control of drinking water quality.

## 4. **History and current status of the contract**

After the Ukrainian declaration of independence in August 1991, the previously state-owned utilities in Ukraine were transferred to municipalities, and the central government ended subsidies to these utilities<sup>5</sup>. Currently, pursuant to the Law "On Local Self-Government in Ukraine" local governments are held responsible for providing high-quality water supply services<sup>6</sup>. In this context, local governments are authorized to enter into contractual relationship with enterprises of various forms of ownership for water service provision to consumers. In 2004, municipalities owned 61 utilities, while 4 remained owned and run by central government.

Municipalities have legal right to transform water utilities into autonomous communal production enterprises, the operations of which can be given into concession or leased, but the main assets (infrastructure) still remain municipal property.

The majority of Ukrainian water utilities are communal enterprises operating water supply and sanitation systems. They remain the property of municipalities. The main problem is that there are currently no formal agreements (contracts) between these water utilities and the municipal authorities defining mutual obligations with regard to management, funding and quality of service (no rule of law and economic principles, but predominantly administratively and politically motivated relations). The number of privately-managed water utilities is negligent and their number is very small.

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<sup>5</sup> The transfer was carried out pursuant to Presidential Decree No. 84 of 12 March 1994, « On Strengthening of the Economic Basis of Local Government ». After adoption of the Constitution of Ukraine, the Supreme Rada passed Law No. 147 of 3 March 1998, « On Transfer of State and Communal Properties», which governs the transfer procedure.

<sup>6</sup> Supreme Rada Law No. 280/97 of 21 May 1997, "On the Local Government in Ukraine" Art. 28.

However, the legal framework allows operation of water infrastructure assets by the private sector in the form of management contract, lease and concession. Privatization of water and wastewater infrastructure is prohibited by Law “On Privatization of State Property” No. 2163-XII (March 4, 1992). Depending on the ownership forms, the following types of utilities are operating in Ukraine:

- private utilities, either individuals and legal entities;
- communal utilities, owned by the territorial community of the cities, villages and residential settlements;
- state utilities;
- utilities, which have a mixed form of ownership.

In Berdyansk, the Local Council has decided to enter into a concession contract with a private partner. This is mainly due to the lack of investments during the past years, the limited financial resources of the municipality and the necessity to implement an ambitious investment programme to substantially improve the quality of the service for water supply and sanitation and the satisfaction of water users as well.

The contract between the Executive Committee of Berdyansk Town Council and Chysta Voda-Berdyansk is one of the first concession contracts in the water sector in Ukraine involving a private operator. The contract was signed in September 2008. This concession contract was prepared following the requirements of the Law on Concessions and implies that:

- The private operator is given a contractual right to use the existing infrastructure assets to provide customers with water supply and sanitation services;
- The assets remain however the property of the Territorial Community of Berdyansk;
- The private operator has obligations to finance extensions and upgrades to the existing networks and facilities;
- As a consequence of the obligation to finance them, the contract duration of much longer than a lease or a management contracts: 30 years.

The contract sets that the operator’s obligations are:

- Managing and operating the conceded facilities;
- Improving (i.e. reconstructing and re-equipping) in accordance with the approved Business Investment Plan (BIP), at its own cost or at the cost of any loaned funds, the property conceded. The minimum amount to be invested is 120 million UAH (23,5 millions USD) in accordance with the following manner:
  - no less than 1 500 000 UAH (290 thousand USD) over the first year of the contract validity;
  - no less than 7 000 000 UAH (1,4 million USD) annually between the second and the sixth years of the contract validity;
  - no less than 9 000 000 UAH (1,75 million USD) annually in the years following the sixth year of the contract validity until the completion of the contract;
- Designing and constructing such improvements for the fulfilment of the contract;
- Improving the quality of the water supply and sewage and waste water treatment services;
- Maintaining the Concession Facilities in the proper technical condition.

## **CHAPTER 3. ANALYSIS OF THE CONTRACT AND CONTRACT IMPLEMENTATION**

This chapter aims at analysing the concession contract with regard to good international practices such as those described in the OECD's *Guidelines for Performance-Based Contracts*. First, we discuss the preparation of the contract. Then, various issues related to legal and institutional matters, tariff setting, contract monitoring, and measurement of the performance are analysed. Challenges identified at each step, as well as good practices, are highlighted.

### **1. Preparation of the contract**

#### **Presentation and analysis**

##### ***1.1 Tender and awarding procedure***

The choice of a concession-type made by the Berdyansk town authorities was dictated by the following reasons:

- The public water supply and sanitation infrastructure was deteriorated due to a lack of investments for the modernisation of the system in the past years;
- A need for massive investments in both upgrading of the facilities and the development of new networks and facilities;
- The bad financial situation of the previous operator (the Berdyansk Miskvidokanal Public Utility).

The process that led to the tender and the call for proposals was as follows:

- The Town Council was approached by a Ukrainian Company (Chysta Voda-Berdyansk, which is an affiliate of an Ukrainian energy company) to propose a concession project on water services;
- A working group was set up to discuss the opportunity to enter into a Public-Private Partnership. This group included representatives of the Town Council and the public utility (Berdyansk Miskvidokanal Public Utility);
- The decision to delegate the water services to a private operator, through a concession contract, was taken by the Town Council on the basis of a tender procedure.

The municipality of Berdyansk prepared the terms of reference for the call for tender and published it at the beginning of 2007. Five companies applied: two Russian companies, two companies based in Berdyansk and 1 company based in Kiev.

The major criteria for selecting the winner from the tender are specified in the tender documentation. The seven selection criteria are:

- 1) Reliability of the concessionaire, seriousness of its intentions and of the intentions of its partners;
- 2) Most advantageous and reliable financing proposal;
- 3) Level of the operation costs (providing maximum profitability and optimum cost recovery);
- 4) Earliest date of investments in the repair and upgrading of the facilities;

- 5) Best level of tariff collection rate;
- 6) Best level of satisfaction of public needs;
- 7) Maximal number of utility's current staff kept by the concessioner after the concession comes into force.

The five bidders who applied were allowed to meet representatives of the water utility to collect information on the tariff and business investment plan. The five bids were assessed by a selection commission on the basis of the 7 criteria listed above. The winner was announced in August 2007. After the selection of the operator, the concession contract was drafted by a commission consisting of 23 members of the Town Council and lawyers. The contract was then signed at the end of September 2008.

Preparing precise tender documents is key to selecting the most cost-effective proposal. Berdyansk authorities prepared the tender documents themselves without external support of experienced experts. It is difficult to judge the quality of the tender documentation as the review team did not get access to these documents, however, it seems that the technical part of the documentation may have been prepared by staff of the water utility who are sufficiently experienced. In addition, to compensate for any possible deficiencies of the tender description, all bidders were allowed to meet with representatives of the utility and obtain a better understanding of its technical and financial situation. In theory, this implies that all bidders were given equal access to information. However, in practice, some bidders may have had access to more limited information than others. While this may not have been the case in Berdyansk, the good practice should have been to organise a meeting for all five bidders with utility representatives at the same time in order to ensure that all of them have obtained exactly the same information. In preparing tenders for such complex contracts, local authorities may choose to hire experienced experts to provide advice. While such experts and consultants cost money and need to work closely with lawyers, the complexity of the operation and the duration of the contract may rightly justify the need for external consultations.

The Berdyansk authorities conducted an open, publicly-announced tender, as required by the Law on Concessions and in accordance with international practices. The seven criteria identified for the selection of the winner generally reflect the most common criteria used in many countries in such a process. They roughly correspond to generally accepted criteria, such as: technical soundness of the proposal, operational feasibility, quality of service, social development potential of the utility. However, no explicit environmental criterion is included in the evaluation package. In addition, the criteria are defined in only very generic terms and leave room for different interpretations by the members of the selection commission (e.g. how is the best level of satisfaction of public needs defined). In such conditions, the absence of precisely-specified criteria can lead to a more subjective approach to the selection process. It seems that in reality it is the level of the concession fee (which is significant) that has determined the winner in the tender and it is not obvious if the concessioner will be able to pay it, as will be discussed later on.

### ***1.2 Type of public private partnership***

Despite its lack of experience with a private operator for the management of public services, the Berdyansk Town Council chose to offer a concession contract for the water services in the town. This may not be the best option to start public-private cooperation. Indeed, concession contracts link the two parties for a very long period of time (30 years in this case) and limit the involvement and control of the public body in the management of its operations. International experience shows that most countries choose to start with simpler types of contracts (management contract or lease contract). In the case of a management contract, the public utility managing the water services remains in place but it is technically helped by a private operator. The duration of the contract is usually short (around 5 years). In a lease contract, the contracting authority leases the full operation and maintenance of its

facilities to the operator but remains in charge of investments in major extensions and upgrading of the facilities. The contract is usually signed for a shorter period of time (10-15 years).

While starting with management and lease contracts allows local authorities to learn and gain experience with major infrastructure contracts, in both cases, the responsibility for major investments remains with local governments. Given the financial difficulties facing the city budget of Berdyansk it is understandable why the city authorities chose a concession as an option where the concessioner is expected to make all investments and at the same time pay a concession fee to the city budget. A longer-term concession (as in the case of Berdyansk) may also provide additional incentives for the operator to make long-term investments already at the beginning of the concession and invest in maintenance as well.

### **Recommendations**

Having a long-term concession may be a viable option given the specific circumstances of the city and providing that there is a strong and realistic contract in place which ensures that the expectations of the contracting authority are well defined and protected. As a matter of principle, the lack of experience of the municipality with public-private partnership contracts and tender procedures could be compensated by:

- Involving experienced experts in drafting the tender documentation and designing the selection criteria and evaluation procedure.
- If possible, starting the cooperation with a private partner by a “lighter” type of contract (management contract or lease contract) providing the municipality has a sufficient capital investment budget or can attract other public (including international) sources of financing to fund investments in the utility.

## **2. Legal and institutional issues**

### **Presentation and analysis**

The analysis of legal and institutional issues deals mainly with the coherence between the law on concessions and the contract. It also looks at the means of regulation of both parties by a regulator.

The Law on Concessions was adopted by the Ukrainian Parliament on 16 July 1999. It is largely inspired by the French model of concessions. This law defines the concept of concession as a contract by which a competent authority of the central executive power or a local community concedes with an operator, against payment and for a given duration, the right to create or manage facilities in order to satisfy the public needs, providing that the operator takes his responsibility for the possible risks of the operation.

The law also provides a general framework which the contracts of concession have to respect and follow and also specifies the issues and elements that have to be reflected in future contracts of concession. Moreover, the law determines the services which may be granted to concession. The facilities of state or communal property which are used for carrying out economic activities in such areas as water supply, cleaning, collection and treatment of household waste, provision of services related to the distribution of heating, construction and exploitation of ports, airports and routes transportation, mail service and telecommunication, energy, social and cultural services, may be granted to concession.

It is worth noting that all possible areas which can be given in concession are clearly spelled out in the law. This makes the choices transparent and allows to avoid ambiguities and debates as to whether a

certain activity can be granted in concession or not which has been the case in a number of countries that have failed to precisely define what constitutes a subject of concession.

## **2.1 Requirements for the concession agreement**

The law sets requirements for the concession agreement, which are mainly:

- The concession agreement shall be concluded for the term defined in it, which shall be not less than 10 years, but not more than 50 years;
- The concessioner shall pay a concession fee for the use of the subject of concession. The concession payment shall be made by the concessioner according to the conditions of the concession agreement regardless of the results of the economic activity (The process of settlement and limit amounts of concession payments shall be determined by the Cabinet of Ministers of Ukraine);
- The transfer of subjects of concession does not cause a transfer of the ownership rights to the concessioner and does not cease state or communal ownership right to these objects;
- The property created for the implementation of the conditions of the concession agreement shall be the subject to the communal ownership right;
- The concessioner shall have the ownership right of the profit obtained from the management (operation) of the subject of concession, as well as of the products obtained as a result of the implementation of conditions of the concession agreement;
- Depreciation deductions calculated to the capital assets obtained in concession or created due to the implementation of conditions of the concession agreement shall remain at the disposal of the concessioner;
- The property obtained in concession shall be included into the balance of the concessioner's legal entity, with indication that this property was obtained in concession;
- Customs duty, value added tax and excise duty, while importing tangible assets due to the implementation of the conditions of the concession agreement, shall be levied in compliance with the legislation of Ukraine.

The review of the contract shows that the contract was prepared in conformity with the main requirements of the Ukrainian concession law. These requirements are in line with international practices regarding concession contracts (which are mainly: contract signed for a long period of time, assets remaining the contracting authority's property, the operator managing the profits but also the risks resulting from the operations, investments for extension, repair and maintenance of the facilities designed and supported by the operator). However, these are mostly framework requirements and they provide little practical guidance to local authorities that need to develop specific concession contracts.

Moreover, the contents of the contract itself is not in line with international standards as major elements such as tariff setting, performance measurement and monitoring by an independent regulator are not included there. The contract needs to be made more specific with regard to some key issues, mainly: the treatment of assets, the need of evaluating the assets and related investments, performance indicators, procedures and guidelines to adjust and review tariffs. Indeed, the lack of sufficiently well-defined concepts on these issues may result one day in conflict situations and prolonged re-negotiations. In addition, the frequent changes in the legislation may cause additional problems with contract implementation. The contract needs to provide some stability to the work of the concessioner at least for a certain period of time (e.g. 3-4 years), particularly when the issues in question are in the competence of the local authority. The contract could also specify the re-negotiation procedures.

Some of these potential conflicts can be smoothed out if there was an independent national regulator that can oversee and regulate both the economic and technical aspects of such contracts. This is a major issue for this contract as it is the first of this kind for public services between the Town Council

and a private operator in Berdyansk. Given the growing interest among municipalities in attracting private operators to manage water utilities in the country, regulation of both operators and contracting authorities is urgently needed in Ukraine. The Ministry of Housing and Municipal Economy is aware of this need and is working on this but the process needs to be speeded up. Experience from other public-private partnerships shows that such an independent body can be very helpful in smoothing out issues that can arise between the parties.

### **Recommendations**

The Berdyansk concession contract is prepared in line with the national legislation and with the Law on Concessions, in particular. To meet international standards for such contracts, some key elements should be developed or included in the contract. The main recommendations are:

- To speed up the establishment of an independent national regulator in the water sector (as it exists in the energy sector). The independence of such an actor is of highest importance in order to ensure that all the parties' interests are well-balanced and protected. The main responsibilities of such a body can include, among others, setting service standards, developing affordability guidelines, designing and managing public expenditure programmes to support water utilities.
- Clarify and include in the contract key issues such as clauses on the treatment of assets, the need for evaluating the assets and related investments, performance indicators, procedures and guidelines to adjust and review tariff.

### **3. Performance indicators**

#### **Presentation and analysis**

Setting performance indicators in contracts is intended to promote savings, efficiency and responsiveness. Indeed, by spelling out clear monitorable performance targets to be achieved by the contractor (leaving the manner to achieve them to the contractor's discretion) linked to financial penalties or bonuses, performance targets can provide incentives to the contractor to improve the level of service and its efficiency.

The concession contract does not include any performance indicators (except the annual level of investments mentioned in article 2.2.2<sup>7</sup>). The objective fixed for the operator in terms of management of the water services is quite vague: *"Improve (reconstruct, re-equip) in accordance with the approved Business Investment Plan (BIP) and at its own cost or at the cost of any loaned funds the property conceded, design and construct such improvements for the fulfilment hereof"*<sup>8</sup>.

However, it is important to give the operator clear and easily measurable targets to assess its performance. This is a major weakness of the contract and the lack of such indicators could lead to further challenges in the management of the utility. Indeed, with such indicators the contracting authority can not properly assess the level of service provided by the operator. Moreover, if the operator fails to improve the water supply and sanitation services in Berdyansk, the contracting authority will have no legal means to put pressure on the operator.

There is a broad international experience with setting performance indicators. Based on this experience, below, we offer some suggestions concerning the possible definition and monitoring of indicators. As the achievement of the targets is measured by comparing the situation at a specific moment of the contract implementation and the situation at the beginning of the contract, we also

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<sup>7</sup> The minimum amount to be invested is 120 million UAH (during the duration of the contract).

<sup>8</sup> Concession Contract on Property Management of Berdiansk Miskvodokanal Public Utility, 2.2.1.c.

briefly discuss the definition of a baseline scenario which is a major first step in setting realistic indicators.

### 1. Definition of performance indicators

Performance indicators can broadly be divided into two main groups reflecting different aspects of the work of the operator. These groups concern:

- The financial performance (it refers to the financial health of the operator); and,
- The efficiency of the operations and the operating performance (it refers mainly to the productivity of the utility's staff, the rate of incidents and the responses chosen to deal with them and the level of service provided).

To become a good and meaningful performance indicator, a target needs to be:

- Carefully designed for and targeted to the specific contract: indicators have to be selected based on an initial evaluation of the conditions of the water utility. This evaluation should be carried out by the contracting authority. Indeed, performance indicators should be selected with the aim of making the operator work on the most urgent and critical aspects of the management and investments. The initial evaluation should at least focus on the following issues<sup>9</sup>:
  - Utility's current and proposed service area;
  - Current characteristics of the service (quantities supplied, metered and paid for);
  - Basic inventory of the assets of the utility as well as their condition;
  - Management of human resources;
  - Tariffs (level, structure, subsidies);
  - General financial performance.
- Realistic: the indicators have to be carefully chosen so that they can be easily monitored and achieved by the operator. A good example of such an indicator is "Continuity of the service". In some cases, for technical reasons, assessing the continuity of water supply is extremely difficult. If this is the case, it is better to drop such indicators. The capacity of the operator to achieve the performance targets is also of high importance. Indeed, fixing a 100% continuity of service if this is not technically and financially realistic could be counterproductive.

In addition, the number of performance indicators should be limited. In some recent EECCA contracts more than 100 indicators have had to be followed by the operator. Monitoring so many indicators can lead the operator to spend more time on monitoring and producing reports than actually achieving the targets set up by the contract. Experience shows that a reasonable number of indicators is around 20. Some examples of specific indicators are provided below.

#### *Financial performance indicators*

The most commonly-used financial indicators are: operating ratio, accounts receivable, collection efficiency, salary or energy costs, profitability level, debt service, coverage ratio. As the private operator has to finance new investments as well as operations and maintenance expenditure, these financial indicators are usually left to his discretion. As such, these indicators are not the most relevant ones from the point of view of the contracting authority.

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<sup>9</sup> OECD (2006), Guidelines on Performance-Based Contracts between Municipalities and Water Utilities in Eastern Europe, Caucasus and Central Asia (EECCA).

### *Efficiency of operations and operating performance*

The group of indicators related to these topics include:

- Promptness to react to customers' inquiries and complaints;
- Continuity of service measured, for instance, by the average daily hours of service or by the percentage of customers with constant supply (weighted hours of supply / total hours for all customers);
- Water quality (for example, the number of days where the national regulatory water quality standards are not met);
- Percentage of the population connected to the water supply and sewage networks;
- Percentage of the customers metered (as it is a relevant tool for water demand management from customers: experience shows that installing meters reduces the consumption of water as customers pay for what they actually consume);
- Compliance of the wastewater treatment plant discharges with the local or national regulation on the level of pollution in the wastewater discharged in the environment.

It is also worth noting that the procedure for the adjustments of the indicators can be specified in the agreement. Indeed, the long duration of the concession contract can make some of them irrelevant after some period of time. So it is advisable that the contract include a clause on performance targets revision provision on both:

- the nature of the performance indicators (for example, if after 10 years all the population is connected to the water supply and sanitation networks, the indicator of "the percentage of the population connected" becomes irrelevant);
- the level of the performance target (for example, if a 80% continuity of service was the initial target and is achieved after 5 years of operation, a new target could be to reach 100% of continuity).

However, just defining performance indicators is not sufficient in a performance-based contract. A clear definition of the initial situation as well as an efficient monitoring are also needed.

### 2. Definition of a baseline situation

Experience from other performance-based contracts shows that the definition of the initial (or baseline) data is crucial to avoid further conflicts between parties. Indeed, these data are used to assess the contractor's performance achievement by comparing the situation each year to the base year conditions. Thus, when incentive or penalties are at stake, determining accurately the base year data is fundamental as they are calculated on the basis of the achievement of the performance indicators.

In order to minimise potential problems during contract implementation with regard to the assessment of the contractor's performance, strong baseline values need to be built. Experience shows that it is best to define these baseline values according to the following criteria:

- First, they need to be easy to measure. For example, the continuity of service is difficult to assess in some specific situations. Indeed, to measure reliably the continuity of service, the operator needs a great number of pressure loggers (providing reliable statistics require to have a sufficient number of data). This can be close to impossible if the network is very long (it would require hundreds of loggers). If the measurement is too difficult or impossible to conduct, the best solution is to drop this indicator.

- Second, the existence of sufficiently reliable data for the calculations (in terms of completeness, accuracy and consistency of data) needs to be taken into account. If such data are known not to be available, it is not worth considering the indicator.
- Third, whenever possible, the baseline values should be determined and agreed upon in close cooperation with both the contracting authority and the previous operator. As the previous operator has the best knowledge of the technical and economic situation of the company prior to the start of the new contract, he should be able to advise on the most appropriate methodology that could be used to determine the baseline values.
- Fourth, it is best when the methodologies used to calculate the baseline values and the performance indicators at a later stage are exactly the same in order to avoid any methodological discrepancies during the implementation stage.

### 3. Monitoring of the indicators

To be credible, performance indicators need to be closely and regularly monitored in order to clearly assess the performance achievement of the operator. Experience shows that hiring an independent auditor to monitor the achievement of some of the main performance indicators is particularly helpful. The first task of the auditor would be to validate the baseline values at the start of the contract which are usually calculated by the operator. Its second task would be to assess the achievement of performance targets used to calculate the operator's bonus or penalty (if there are any envisaged in the contract) and if necessary to propose adjustments to these criteria for each subsequent year.

While the technical auditor is supposed to play a key role in contract monitoring, the process for selecting such an auditor should be carefully carried out. This needs to be a transparent and open procedure. Moreover, the technical background of and the methodologies proposed by the auditor to evaluate the contractor's performance need to be at the heart of the selection process. In addition, the contract can require that these methodologies be agreed upon by all major parties involved in the monitoring of the contract.

Another issue to consider with regard to the auditor is linked to his remuneration. If, because of a lack of funding, the auditor's technical capacity is not guaranteed or if the auditor cannot perform his duties properly, this may lead to significant problems between the parties, as it has happened in some EECCA countries. In choosing to appoint such an auditor, the contracting authority needs to consider two major issues: the technical capacity of the auditor and the availability of funds to pay him so that he can do his job properly.

### Recommendations

The contract clearly lacks performance indicators to assess the achievements of the operator. Performance indicators are intended to stimulate the improvement of the level of service and the efficiency of operations provided by the operator. The major recommendations when setting up performance indicators are:

- Consider selecting a few key indicators to include in the contract. Such indicators should be easy to measure and monitor and should be financially achievable. They should be specified for each year (as done with the investment levels in 2.2.2b). They should also reflect the most urgent and critical issues to be solved by the operator. Such indicators could include: weighted average number of daily hours of drinking water services, percentage of individual subscribers billed on the basis of metered consumption, weighted average water bacteriological safety compliance. Ideally, these indicators should be agreed upon with the operator.
- The technical and financial conditions of the utility should be carefully assessed at the very start of the contract: the baseline data must be sufficiently accurate to avoid further conflicts

between the parties. A good solution would be to define them in conjunction with the previous operator, under the control of an independent auditor.

- An independent auditor could be appointed to monitor the achievement of the performance targets. The technical auditor must be selected carefully and paid sufficiently well to do his job properly and honestly.

#### **4. Tariffs and financial obligations of the contracting authority**

##### **Presentation**

##### ***4.1. General provisions regarding tariff setting in Ukraine***

With respect to tariff setting in Ukraine, regulatory powers are divided among the national and regional governments (oblast state administrations and local self governments) in the following way:

- *The national government* adopts general requirements related to the identification of costs that can be recovered through water and wastewater tariffs. These requirements are spelled out in the procedures and instructions of the central executive bodies, such as the Cabinet of Ministers of Ukraine, Ministry of Housing and Municipal Economy<sup>10</sup> and passed on to the local level to be enforced.
- *At the local level*, pursuant to the Law “On Housing and Municipal Services”, enacted in January 2005, the local self-government bodies are empowered to set tariffs for the public services, provided by the utilities (regardless of the form of ownership of the utility) on their territories.

Until now, there is still a lack of clearly defined responsibilities between regulatory authorities of oblasts and local self-governments especially when several water and wastewater enterprises serve more than one municipality and neighbouring residential settlements in a particular oblast and/or when facilities of such utilities are located in different cities; or when a communally owned utility is operated by a lease company or a concessioner as it will be the case in Berdyansk.

A key issue, currently under discussion, is the issue of subsidies, which have to be provided to utilities when regulated tariffs are not set at full cost recovery levels. This follows from the enactment of tariff setting provisions included in the Law “On Housing and Municipal Services” which may create uncertainty with respect to the financial viability of the utilities.

This Law authorises local governments to set tariffs for communal services (including water and wastewater) for utilities of all types and ownership forms, which leads to a confusion with a number of other laws and regulations, such as: the Law "On Local Self-Governance in Ukraine", Law "On Local State Administrations" and the Cabinet of Ministers Decree “On Determining the Tariff Setting Authority of the Executive Bodies and Local Government Executive Bodies” of 25 December 1996.

The Law "On Local Self-Governance in Ukraine” does not allow local governments to set tariffs for services that are provided by non-communally owned utilities. Article 28 of the Law specifies that local governments only agree upon the level of tariffs for services that are provided by non-communally owned utilities.

The Law "On Local State Administrations" allows oblast state administrations to set tariffs for non-communally owned utilities. Availability of two other laws – the Law “On Housing and Municipal Services” and the Law “On Local State Administrations” – that allocate similar functions of tariff setting to two different bodies (local governments in the first case and local state administrations in the

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<sup>10</sup> Instruction of the Ministry of Construction, Architecture and Housing and Municipal Economy of Ukraine (June 2005).

second one) - creates regulatory conflicts in those parts of Ukraine where services are provided by non-communally owned utilities.

#### **4. 2. Tariff setting and annual tariff revision**

The Berdyansk concession contract deals with tariff setting and tariff revision issues in Article 8. The four main points set in the contract are<sup>11</sup>:

- the tariff must be established in accordance with the resolutions of the Berdyansk Town Council (No. 660 of 14.12.2006 and No.476 of 23.08.2006);
- the price of the tariff for water supply and sanitation services must be changed following the procedure established by the Ukrainian law;
- the operator must not change the established tariff on its own initiative;
- The 120 million UAH investments mentioned in paragraph 2.2.2b of the contract as well as the financial expenses linked to the loan used to finance these investments must not be taken into account as an investment component of the tariff.

Currently in Berdyansk, tariff levels are set as follows:

- water: domestic users:	4,02 UAH/m <sup>3</sup>	industrial users: 7,94 UAH/m <sup>3</sup>
- waste water: domestic users:	2,36 UAH/m <sup>3</sup>	industrial users: 4,80 UAH/m <sup>3</sup>

The numbers make the Berdyansk's tariff one of the highest in Ukraine at the moment. Tariff setting is a mix of two approaches: the historical approach and the normative approach. The historical approach is based on past data while the normative approach considers classical operating costs (such as labour, energy, financial costs, taxes) but also capital costs (depreciation of buildings, networks, machines, equipments, pumping stations, vehicles and office equipments). Such costs of the past year are increased by 5,2% - a provision called "profit level" - while this increase does not even cover the inflation whose official rate is around 13% - 15% but will probably exceed 20% in 2009. The last tariff revision goes back to October 2006 and was due in particular to a price increase of the raw water purchased and transferred by the Zarapojia Vodokanal along the 175 km pipeline from the Dnipro River.

The key legal document regulating tariff calculation is the Decree of the Cabinet of Ministers "On Approving the Order for Calculating of Tariffs for Centralised Water Supply and Wastewater Disposal Services", 12.07.2006. The price setting order specifies the types of costs which can be recovered by tariffs:

- Most of the operation costs can be recovered through tariffs and most of them should be calculated on a normative basis. This specifically regards major cost items, such as labour, material resources, energy (electric energy, gas,...), chemicals, etc.
- Calculation of depreciation is also included in the tariff; it is done on a normative basis but should follow the tax law calculation method.
- Capital costs which correspond to the profit of the operator can also be recovered but their amount is limited to 12% of all operating costs (= allowable profit). The utilities should plan profit, based on an approved capital investment programme or an available business plan.
- The tariff can also include the recovery of costs for setting a capital reserve, which needs to be accumulated for capital investment purposes. This amount is limited to and based on financing

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<sup>11</sup> Concession contract: Article 8.

needs for renovation and expansion of fixed assets and other non material assets that can be depreciated. When applying for a new tariff the utility should identify what investments will be financed from depreciation and profit.

It is therefore required to provide technical and economic estimates or business plans to the specified programme, by which it is possible to prove the effectiveness of the planned investments, sources of investment funding and the term of project implementation. This provision is foreseen in Article 8.3 of the concession contract: “the Municipality shall consider, approve and sign a Business Investment Plan submitted by the Operator”.

### **4.3. Concession fee**

Article 3 of the Berdyansk concession contract includes a provision for the payment of a concession fee on a quarterly basis. The first payment will be due after signing the contract. It will be paid after the approval of the Antimonopoly Committee and after obtaining the license for operating the water utility. The payment of a concession fee is usual when using the assets belonging to the contracting authority, but it is generally a rather small amount. From the information obtained in Berdyansk, the first payment would be based on an annual concession fee equivalent to 7% of 103 million UAH (estimated amount of net assets), that is a little more than 7 million Euro.

### **Analysis**

Despite the fact that the rules allow full cost recovery, the Berdyansk municipality did not follow these rules and has not increased tariffs in accordance with the increase of costs. Water tariff is based on political considerations below cost recovery level in order to protect residential customers and to make tariffs affordable to the majority of the population. As such, the Berdyansk water utility typically operates at a loss and does not have sufficient resources to cover operating and investment costs. Currently, tariff for domestic customers covers only 80% of water and sewage costs.

Berdyansk middle class is close to poverty while payments of the low income families for communal services (water, sanitation, electricity, hot water, heating...) are capped at 15% of their net income. However, the difference is paid by the Labour and Social Protection Ministry through the Low Income Subsidies Department in Berdyansk. Although the tariff collection rate seems extremely good since it reaches 98,3% of the water billed (where water and sewage tariffs appear separately), revenues are not sufficient to cover operating and capital expenditure. The Law on Housing and Municipal Services (Article 31) indicates that subsidies are due from the Local Executive Committee when there are losses resulting from the absence of full cost recovery. Moreover, the Law on the State Budget allows compensating losses if local budget subsidies are not sufficient. In fact, State subsidies are an offset and are not directly paid to the water utility but they are used for paying debts (such as electricity, whoever the producer, public or private, taxes, etc.).

In Berdyansk, the choice of a concession contract was mainly motivated by a substantial need for investments in drinking water and sanitation. Normally, investments are repaid through tariffs. However, an annex to the contract mentions that there will be no tariff increase during one year. In a country where inflation is currently high, preventing water tariff increase during 3 years is not realistic and is in contradiction with the ambitious investment policy agreed in the contract.

In addition, the contract does not clearly define the division of responsibilities between different stakeholders with regard to tariff setting. The Berdyansk water utility is in a process of passing from a communally operated to a privately operated utility. Therefore, in case of a conflict with the municipality, the operator could argue in the future that tariff revision depends on the Local State Administration (Law on Local State Administration) and not on the Town Council. All these discrepancies in the system of tariff regulation for water and wastewater services point to the need for substantial revisions. If a National Regulatory Water Commission is established, as planned by the

government, this regulator can be tasked with the responsibility for cleaning up the legislation from all these overlapping mandates and conflicting situations.

Moreover, even if the concession contract requires the operator to submit Business Investment Plans, there is no contractual provision describing how the investment component, either rehabilitation or new investments, will be supported by the tariff. In other words, there is no methodology explaining how the tariff can be increased to contribute to the financing of the investments. As long as contractual mechanisms for tariff indexation are not defined and are left only to the good will of the Town Council, achieving an investment plan corresponding to the needs of the City of Berdyansk will remain practically impossible. In such conditions, there is a risk that the concession contract will fail and the current investment backlog will become even worse.

Regarding the concession fee, the amount required seems pretty high compared to international experience. Such a high fee may jeopardise the financial sustainability of the concession. It is also important to know if the municipality is planning to use the concession fee to reinvest in the water utility. If not, it will mean that some of the water revenues will be used for other purposes at a time when financial resources for water are not sufficient to meet financing needs.

### **Recommendations**

Having a provision in the contract that ensures the financial equilibrium of the operator is a key to securing the financial sustainability of the concession in the long run. Tariff setting and tariff revision are at the heart of this equilibrium which will allow improving the performance of the utility and the smooth implementation of the investment programme both of which are among the main challenges in the Berdyansk. In this context, the recommendations address both the improvement of the regulatory framework for tariff setting and the way tariff setting is reflected in the contract. The major recommendations are:

- Simplify the regulation for tariff setting and tariff revisions, reduce the number of conflicting laws and decrees with regard to tariffs. Clarify the roles of Local Councils and Local State Governments (Oblast) in this respect;
- Facilitate sustainable cost recovery in tariff setting as full cost recovery seems unreachable in the short/medium term in Berdyansk through an improvement of costs monitoring;
- Take into consideration, as the law enables it, a more important portion of the investment components when 5 year business plans are presented with a gradual increase of the tariff in accordance with the improvement of the service;
- Define a clear methodology for annual water price revision to avoid political interferences and aim at covering operating costs and a portion of investment costs;
- Determine in the contract how the investment part which will not be supported by the tariff will be financed at local, regional and/or national levels to avoid financing gaps and inefficiency in the investment programmes implementation;
- Adjust the concession fee to a significantly smaller amount or use it for water/sanitation investments.

## **5. Financial penalties and incentives**

### **Presentation and analysis**

The contract does not envisage any penalty or bonus for the operator (mainly because the measurement of a performance is not possible as no performance indicators exist). This is another major weakness of this agreement. Indeed, the contracting authority has no means of put pressure to

make the operator meet the objectives set in the agreement. As such, the only way for the contracting authority to enforce the achievement of objectives is to sue the operator.

There are two main cases when penalties can be envisaged:

- The first case is when the performance objectives set in the contract are not met. Apart from the annual level of investments, no other performance indicator is included in the contract. However, in a concession-type contract, there are a number of ways to link indicators and penalties. Below are some example of indicators for which penalties can be imposed in case of non-achievement of these indicators:
  - Level of investments set up in the contract;
  - Promptness to react to customers' inquiries and complaints;
  - Continuity of service measured;
  - Water quality (for examples, number of days where the national regulatory water quality standards are not met);
  - Percentage of the population connected to the water supply and sewage networks;
  - Percentage of the customers metered;
  - Compliance of the wastewater treatment plant discharges with the local or national regulation.

It is worth noting that the imposition of penalties when performance indicators are not met is important as it is the only way to guarantee a good level of service for the customers.

- The second case is observed when the main requirements of the contract are not met. For the Berdyansk contract, penalties can potentially be envisaged for:
  1. The development of the Business Investment Plan (BIP) in due time;
  2. The fulfilment of the works envisaged by the BIP;
  3. Provision of an annual report;
  4. Payment of the concession fee.

It is recommended to apply a penalty if these requirements are not met when: a/ the fulfilment of the requirements is easy to assess (as in points 1, 2, and 3), b/ when the requirement is a key factor for the success of the contract (points 1 and 2) and c/ when the requirements provide the contracting authority with information on the enforcement of the contract (point 4). On the contrary, no penalty (or incentive) should be applied on the operating performance of the operator as its revenues are directly linked to the good management of the operation.

## **Recommendations**

The inclusion of possible financial penalties in the contract is crucial for the control and monitoring of the contract implementation. Even if never applied, the existence of penalty clauses in the contract has a disciplining effect. In this context, the main recommendation is:

- Consider including penalties in the contract for cases where either contractual requirements or performance targets are not met by the operator. Do not apply penalties on the operating performance of the concessioner as his revenues are directly linked to the good management of the operation.

## **6. Monitoring of contract implementation**

### **Presentation and analysis**

The contract provides for regular reporting from the operator, in order to monitor contract implementation. The contract requires that the operator prepare an “annual report on the concession Facilities, the depreciation deductions and investments”<sup>12</sup>. The frequency of the reporting (once per year) is a good practice. Indeed, more frequent reports would divert the operator from its main objectives (managing efficiently the facilities and designing and implementing investment plans) by bureaucratic issues. On the contrary; less frequent reporting would prevent the contracting authority from efficiently monitoring the contract implementation. However, for the smooth implementation of the contract, it is key that the two parties maintain regular contacts and inform each other of any important developments without waiting for the official reporting deadlines. This could help improve the trust and confidence between the parties to the contract.

However, the main weakness identified in the contract is the lack of precision in the nature of the information to be included in the report. Indeed, the requirements for the coverage of the annual report are very vague: no indication is provided with regard to the level of detail, the kind of data or indicators to report on. Experience from other countries shows that when reporting requirements are not specified, this may lead to conflicts during the implementation stage due to the fact that different parties may have different understanding of what information should be provided in the annual reports.

Examples of the type of information that could be required in the annual report are:

- details on the levels of service (for example, the quality of the water supplied, the conformity of the wastewater discharge with the national regulation) achieved during the contract year in question and the failures to achieve the levels of service;
- information on the works and actions to be carried out in the following contract year;
- investments made in the contract year;
- investments planned in the next X years;
- methods employed by the operator to maintain the quality of the service and the steps taken to monitor and determine the quality of the service;
- explanations of reasons which in the opinion of the operator may result in its being unable to meet the required levels of service or the levels of investment;
- details of the assets acquired, disposed of or replaced by the operator during the contract year.

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<sup>12</sup>Concession contract : paragraph 2.2.2 f.

In addition, the contract does not envisage the control of the information provided in the annual report. This can be a sensible issue especially as this contract is the first experience of the Town Council with a private operator.

### **Recommendations**

While monitoring of contract implementation is regulated in the contract and annual reporting is required, the contract lacks clear reporting requirements. The lack of precision of these requirements may lead to misunderstanding at a later stage. To avoid future conflict situations in this regard, it is recommended to:

- Clearly define in the contract the nature of the information to be provided in the annual report;
- Have the data provided in the annual report verified by a technical auditor. Such an auditor could help the contracting authority assess if these data are correctly calculated and interpreted. The technical auditor could be the same as the one selected to monitor the achievement of the performance indicators (as stated in part 3 of this report).

## **7. Contract enforcement and conflict resolution mechanisms**

The contract enforcement and conflict resolution mechanisms are a key point highlighted in the OECD's *Guidelines for Performance-Based Contracts*. This part aims at analysing how these issues are treated in the contract and makes some recommendations.

### **Presentation and analysis**

According to the terms of the contract, the contract comes into force upon its signature by the parties and its State registration. The State registration should be completed three days after the signature of the contract by the contracting authority with the agreement of the executive committee of the relevant council. The Ukrainian State Property Fund should be notified of the conclusion of the contract in order to include it into the Concession Contract Register. The contract also provides that the operator get a license upon the signature and the contract registration.

Regarding the conflict resolution mechanism, the contract provides that any dispute in relation with the concession contract have to be settled by the parties through negotiations. If the negotiations on any disputed issue fail such an issue shall be considered further in accordance with the Ukrainian law. The contract and its interpretation shall be governed by the Ukrainian law.

Altogether, the conflict resolution mechanism appears to be too light as it does not specify any means to avoid the recourse to the jurisdictions, such as conciliation, mediation or arbitration.

Given the technical (water specifications), legal (contractual interpretation, relevant laws and regulations) and financial (tariffs and financial performance incentives) complexity of performance-based contracts in the water sector, they usually require comprehensive provisions relating to dispute settlement. The conflict resolution mechanism which seems to be the most appropriate for this contract is arbitration. If the parties agree to this alternative conflict resolution it can be included as a clause in the contract. The arbitration seems to be even more appropriate for a country like Ukraine where the political influence over courts is significant and where the corruption of judges is possible.

In order to be workable, an arbitration clause should include, at a minimum:

- a clear choice of the arbitration mechanism that will apply (as several arbitration mechanisms exist); and,
- a clear definition of the scope of the disputes to be arbitrated.

The parties may also wish to include in the clause a choice of the law to be applied to the merits of the dispute (that is, the law that applies to the interpretation and application of the contract itself); the place of arbitration; the number of arbitrators and other requirements regarding nationalities and qualifications of arbitrators; and mandatory prior recourse to conciliation or mediation. Finally, it is also important to determine how the host country will treat an arbitral award.

Based on examples of arbitration procedures in other contracts, the following procedure could be proposed in case of significant technical and financial disputes between the parties:

- Resolving the conflict by referring to an independent auditor. This auditor will assess the technical or financial issue and make a proposal to the parties on how to resolve the problem;
- Involving a panel of arbitrators, if the proposal made by the independent auditor does not resolve the conflict within a limited period of time (for example, 30 days). The panel of arbitrators can be selected jointly by the two parties involved, or, if they fail to agree on the nomination, by a national court.

Even if these formal conflict resolution mechanisms are not always a sufficient condition to effectively resolve conflicts of interest, they are necessary, particularly in such concession contracts where huge financial amounts are at stake. But the willingness of the parties to cooperate and to find solutions is obviously equally important.

### **Recommendations**

In case of conflicts and disputes, before going to court, the parties may consider other, lighter, conflict resolution mechanisms. Arbitration appears to be the most appropriate conflict resolution mechanism for this contract. As arbitration is currently not included in the contract, it is suggested that:

- The parties consider an arbitration clause in the contract as such a clause will be beneficial to both sides. This clause may include at least two items: a clear definition of the arbitration mechanism that will be applied and a clear definition of the scope of disputes to be arbitrated. An arbitration procedure frequently observed in other contracts and which produces good results include first the involvement of an independent auditor and then a panel of arbitrators.

## **8. Personnel management**

### **Presentation and analysis**

Article 10 of the contract addresses employees issues. It specifies that:

- the operator shall employ 100% of the staff transferred from the BMPU;
- the operator shall preserve the social guarantees for the staff as established in the BMPU agreement;
- a new collective agreement must be signed within 3 months after the signature of the contract, but this agreement should not deteriorate the current conditions of the staff.

The positive aspect is that all employees keep their jobs and are transferred to the new operator at the beginning of the contract. However, this raises two additional issues with regard to staff management:

- First, there is no mention in the contract of the possibility for the operator to dismiss employees after the enforcement of the contract. This is a critical point as improvements in the the operations may come from a reduction of staff costs (by improving productivity);
- Second, the operator has no obligation to develop and implement a training programme for the employees although this is a key condition to improve the productivity of staff.

## **Recommendations**

Two main recommendations are offered with regard to personnel management:

- First, the operator should be explicitly given the right to reduce staff costs (by decreasing the number of staff). Not mentioning this in the contract could lead to conflicts between both parties if the operator intends to fire some staff members. In addition, staff concerned should be clearly explained why their posts are closed and any job suppression should be clearly justified. The contract should envisage a clear procedure for closing job positions. Staff who lose their jobs should be properly protected and should get all social benefits in accordance with Ukrainian legislation.
- Second, the contract should include an article related to the training of staff and increasing their competencies in modern management practices, including, among others, computer literacy, accounting, technical safety at work. Require the operator to prepare and implement a training plan for the employees.

## **9. Transparency**

### **Presentation and analysis**

#### ***9.1 Transparency in the operator selection process***

The field review has established that the rationale for the selection of the operator was not officially published. The reasons for awarding the contract to Chysta Voda-Berdyansk are not known to the public in the town as well. This confronts the parties with a major transparency issue particularly given that there have been concerns among the city population with regard to inviting a private operator to provide water services to Berdyansk. Once the operator starts working, the city authorities may take this opportunity to provide the population with more information and respond to their concerns.

#### ***9.2 Transparency during contract implementation***

The transparency of the operator is partly ensured through the “annual report on the use of the concession facilities, the depreciation deductions and the investments”<sup>13</sup>. In this context, two main issues have been identified:

- The contract does not specify that the annual report should be verified by an independent body (technical auditor, for example); and,
- The nature of the information to be provided in the report is not listed in the contrat. The main risk is that the operator may limit the reporting to one official annual report only. Official reporting needs to be supplemented by other channels of communication between the parties.

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<sup>13</sup> Concession contract, article 2.2.2.

The absence of an officially-published rationale for the selection of the operator as well as the potential lack of control on the information provided to the contracting authority do not ensure transparency and good governance *per se* (which are very sensitive issues in the water sector). Experience from other countries show that transparency and good communication pay off, particularly with long-term contracts, providing the operator has come to stay.

### **Recommendation**

Some of the recommendations are the same as those presented in part 6 of this report. Transparency will be improved if:

- The rationale for the selection of the operator is made available to the public;
- The contract gives a clear definition of the nature of the information to be provided in the annual report;
- The data provided in the annual report are verified by an experienced technical auditor.

## **CHAPTER 4. CONCLUSIONS**

### **1. Major findings**

This concession contract has been signed very recently (September 2008). It is the first contract of this kind signed by the City Council of Berdyansk. The analysis has mainly focused on the contents of the contract agreement. Some of the major findings from the review are:

- Absence of external advice (from experienced technical experts to prepare the tender procedure and draft the contract).
- No specific performance indicators have been defined in the contract. As a consequence, the achievement of the operator's performance cannot be objectively assessed.
- No independent regulator nor a technical auditor will assess the operator's performance and act as an independent party to smooth possible conflicts between the parties.
- No financial penalty is envisaged if the operator fails to improve the state of the infrastructure or the level of service delivered to the customers.
- The conflict resolution mechanism identified in the contract does not specify the means to avoid the recourse to court, such as conciliation, mediation or arbitration.
- The contract does not allow the operator to dismiss some of the staff members if the staff costs appear to be too high.

### **2. Summary of good practices**

- The contract follows the requirements for concessions set in the Ukrainian legislation which are in line with the broad international standards for concession contracts (mainly: contract signed for a sufficiently long period of time, assets remaining the contracting authority's property, operation risks borne by the operator, investments for extension, repair and maintenance of the facilities designed and carried out by the operator).
- The tender procedure has been open to non-Ukrainian companies which helps guaranteeing a fair competition and the attraction of experienced companies.
- The selection criteria identified for the selection of the winner reflect the most common criteria used in many countries in such a process.
- The 5 bidders were allowed to meet with representatives of the utility to obtain a better understanding of its technical and financial situation.
- The operator is required to provide the contracting authority with an annual report for the monitoring of its activities.
- The contract requires that all staff members must be transferred from the previous utility (BMPU) to the new operator. The operator is given full responsibility for managing the company's personnel, with no undue influence from the contracting authority. This shields the contractor from political and external interference in its operational management.

### 3. **Proposal for improvements**

- During the preparation stage, it is recommended to involve experienced experts in drafting the tender documentation and designing the selection criteria and evaluation procedure.
- When starting the cooperation with a private partner, a good option could be to start with a “lighter” type of contract (management contract or lease contract) providing the municipality has a sufficient capital investment budget or can attract other public (including international) sources of financing to fund investments in the utility.
- The establishment of an independent national regulator in the water sector is urgently needed (as it exists in the energy sector). The independence of such an actor is of highest importance in order to ensure that all parties’ interests are well-balanced and protected.
- Including a few key indicators in the contract (easy to measure and monitor and financially achievable) is a major recommendation. They should be specified for each year and should also reflect the most urgent and critical issues to be solved by the operator. Such indicators could include: weighted average number of daily hours of drinking water services, percentage of individual subscribers billed on the basis of metered consumption, weighted average water bacteriological safety compliance.
- An independent auditor could be appointed to monitor the achievement of the performance targets. The technical auditor should be carefully selected and paid sufficiently well to do his job properly and honestly.
- Regarding tariff setting, the main recommendations are to:
  - simplify the regulation for tariff setting and tariff revisions as there are too many laws/decrees containing contradicting requirements, particularly those regarding the involvement of Local Councils and of Local State Governments;
  - define a clear methodology for annual water price revision to avoid political interferences and aim at covering operating costs and a portion of investment costs;
  - determine in the contract how the investment part, which will not be included in the tariff, will be financed at local, regional and/or national levels in order to avoid financing gaps and inefficiency in the investment programmes implementation.
- Possible financial penalties should be envisaged by the contract if the performance objectives or if the main requirements of the contract are not met (in Berdyansk case: these are mainly the Business Investment Plan and the annual report).
- The contract should clearly define the nature of the information and data to be provided in the annual report and these data should be verified by a technical auditor in order to assess if they are correctly calculated and interpreted.
- The conflict resolution mechanism which seems to be the best suitable for this contract is arbitration. An arbitration clause should be added to the contract describing the arbitration procedure that will apply and clearly defining the scope of the disputes to be arbitrated.
- The operator should be explicitly given the right to reduce staff costs (by decreasing the number of staff) but the contract should envisage a clear procedure for closing job positions and staff who lose their jobs should be properly protected and should get all social benefits in accordance with Ukrainian legislation. Moreover, the contract should include an article related to the training of staff and increasing their competencies in modern management practices, including, among others, computer literacy, accounting, and technical safety at work.

- Finally, the rationale for the selection of the operator should be made available to the public. This is particularly relevant as there have been concerns among the city population with regard to inviting a private operator to provide water services to Berdyansk

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### 2. Laws

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Presidential Decree of 12 March 1994 on Strengthening of the Economic Basis of Local Government, Kiev.

Law of 3 March 1998 on Transfer of State and Communal Properties, Kiev.

Law of 21 May 1997 on the Local Government in Ukraine, Kiev.

### 3. Documentation related to the concession contract

Concession Contract on Property Management of Berdyansk Miskvidokanal Public Utility.

## ANNEXES

### Annex I: Socio-economic indicators for Ukraine

	2000	2001	2002	2003	2004	2005	2006	2007	2008
GDP (USD mln)	31 262	38 009	42 393	50 133	64 883	86 137	108 002	141 644	198 006
GDP (% change, real terms)	5,9	9,2	5,2	9,6	12,1	2,7	7,3	7,6	6,4
GDP per capita, PPPs (current international dollars)	161	180	193	216	249	263	291	322	350
Population, total (million)	48,7	48,2	47,8	47,4	47,1	46,7	46,5	46,2	45,8
Population, urban (% of total)	67.1	67.2	67.4	67.5	67.7	67.8	67.9	67.9	..
Consumer price inflation (average, %)	28,2	12,0	0,8	5,2	9,0	13,5	9,1	12,8	25,3
Unemployment (end-year, % of labour force)	4,2	3,7	3,8	3,6	3,5	3,1	2,7	2,3	..
Current account balance (USD million)	1 481	1 402	3 173	2 891	6 804	2 531	-1 617	-5 918	-13 057
Current account (% of GDP)	4,7	3,7	7,5	5,8	10,5	2,9	-1,5	-4,2	-7,1
Trade balance (USD million)	779	198	710	-269	3 741	-1 135	-5 194	-10 572	-18 697
Gross capital formation (% of GDP)	19,7	19,7	19,2	20,6	22,6	22,0	24,6	27,4	..
External debt (% of GDP)	37,81	31,79	51,10	47,47	47,27	45,97	50,60	59,90	59,90
External debt (% exports of goods and services)	60,54	57,37	54,69	82,24	77,16	89,28	108,51	132,06	..
Foreign direct investment, net inflows (% of GDP)	1,9	2,0	1,6	2,8	2,6	8,7	5,3	6,5	4,0
Aid (% of GNI)	1.8	1.4	1.2	0.7	0.6	0.5	0.5	..	..

Source: EBRD, *Transition report 2007*; IMF, *World Economic Outlook database*, April 2008; WB, *World Development Indicators database*, 2007.

### Annex II: Ukrainian water sector indicators

	1995	2000	2006
Access to improved water supply (%)	97	97	97
Rural areas	90	92	97
Urban areas	100	100	97
Access to improved sanitation (%)	96	96	93
Rural areas	93	91	83
Urban areas	98	98	97

Source: United Nations Statistics Division, Common Database: <http://unstats.un.org/unsd/databases.htm>

### Annex III: Contract summary table

<b>General provisions</b>	
Contracting authority	Executive Committee of Berdyansk Town Council represented by the acting Mayor, acting on the basis of the Berdyansk Territorial Community Charter.
Operator	Chysta Voda-Berdyansk Llc (Limited liability company) represented by Mr Valeriy Perepelytsia, Director.
Type of contract	Concession contract.
Award, date, duration, possible extension	<p>Contract signed in September 2008.</p> <p>Come into force: upon its signature by the Parties and State registration.</p> <p>Duration: 30 years.</p> <p>Extension is possible for 20 years under the same conditions unless neither of the Parties receives – six months before the contract expiry - a letter from the other Party expressing its intention to terminate this Contract or change its conditions<sup>14</sup>.</p>
<b>Scope of the contract</b>	
Coverage area	<p>Integral property complex of the Berdyansk Miskvidokanal Public Utility :</p> <p>1 town and 1 village representing :</p> <p>- 49 431 subscribers for the water supply service;</p> <p>- 35 688 subscribers for the sanitation service.</p>
Types of activities	<ul style="list-style-type: none"> <li>• Water supply;</li> <li>• Sewage collection;</li> <li>• Waste water treatment services to private and corporate consumers.</li> </ul>
<b>Rights and obligations of the Contracting authority and the Operator</b>	
Contracting authority's obligation	<p>The main contracting authority's obligation are<sup>15</sup> to:</p> <ol style="list-style-type: none"> <li>1. provide the Concession Facilities free of any encumbrances, restrictions or claims of any third parties;</li> <li>2. support the Operator in the exercise of its rights and fulfilment of its obligations;</li> <li>3. ensure that the Town Council issues its resolution within the terms and in accordance with the procedure envisaged;</li> </ol>

<sup>14</sup> Contract article 14.4.

<sup>15</sup> Contract article 2.1.2.

	<ol style="list-style-type: none"> <li>4. abstain from increasing prices for the purchased water without consulting the Operator and abstain from interfering into the Operator's business.</li> </ol>
Operator's rights and obligations	<p>The main Operator's rights obligations are<sup>16</sup> to:</p> <ol style="list-style-type: none"> <li>1. fund the Concessions Facilities<sup>17</sup>;</li> <li>2. have the exclusive right to manage/operate the Concession Facilities;</li> <li>3. own the profit received from the management of the Concession Facilities</li> <li>4. contract third parties, including foreign companies, organisations and individuals, for the performance of special works on the Concession Facilities without prior authorisation by the Contracting authority;</li> <li>5. make suggestions to the Contracting authority and Berdyansk local self-governance bodies on the tariff-setting for the water supply and sewage and waste water treatment services</li> <li>6. make suggestions to the Contracting authority and Berdyansk local self-governance bodies on the tariff-setting for the water supply and sewage and waste water treatment services;</li> <li>7. use technologies, materials, raw materials, and equipment certified for the use in Ukraine on the Concession Facilities;</li> <li>8. be responsible for the observance of this contract and the Law by any third parties contracted for the fulfilment of special works on the Concession Facilities;</li> <li>9. return the Concession Facilities to the Concessionaire upon the expiry of the term in proper technical conditions in accordance with the contract terms and conditions, while the land plots shall be transferred in accordance with the relevant land lease contracts.</li> </ol>

<b>Financial condition</b>	
Concession fees	The Operator shall pay a fee to the contracting authority on a quarterly basis. The amount of the fee was not disclosed by the parties during this review <sup>18</sup> .
Provision and return of Concession Facilities <sup>19</sup>	The legal regime of the property provided into Concession (or created) shall be defined with due consideration of the Law on Concessions, in

<sup>16</sup> Contract article 2.2.1 and 2.2.2.

<sup>17</sup> Contract article 1.5.

<sup>18</sup> Contract article 3.1.

<sup>19</sup> Contract article 4.

	<p>particular it shall be considered that it is owned by Berdyansk Territorial Community. Its provision into Concession does not entail the transfer of the ownership title to the Operator and does not terminate the municipality ownership.</p> <p>Upon expiry of the term of validity or cancellation, as well as in the case of the Operator's liquidation, the Operator shall return the Concession Facilities (all property received under the acceptance act) to the Contracting authority in the proper technical condition with due consideration of the investments made, including those that have not been compensated by the Operator as a result of the Concession activities.</p> <p>The Operator shall receive into its lease the plots of land that are necessary for the management of the Concession Facilities. The land plots are for the term which shall not be smaller than the term of the contract validity. The terms and conditions of the land lease contracts shall be defined separately and in accordance with the current law.</p> <p>As of the effective date of the contract, the Contracting authority shall develop and approve the land allotment papers and other documents confirming the right to use the land where the Concession Facilities are located. It shall also complete the technical stock-taking and make technical passports for all real estate Facilities making part of the Concession Facilities and pass such documents to the Operator.</p> <p>The rent for the land where the Concession Facilities are located shall be defined in the amount of the land tax to be calculated in accordance with the current legislation.</p>
<p>Improvement of the Concession Facilities and compensation procedure for the improvements <sup>20</sup></p>	<p>In order to use the Concession Facilities efficiently for the provision of services to satisfy public needs for uninterrupted district water supply and sewage and waste water treatment, the Operator shall make improvements to the Concession.</p> <p>Upon expiry of the Concession, the property (equipment, machinery) purchased by the Operator pass into the ownership of Berdyansk Territorial Community.</p> <p>The Contracting authority shall reimburse the Operator for the expenses made due to the improvements or for the cost of the created/purchased property in the part that has not been compensated by the Operator as a result of Concession activities if the Contract is cancelled on the initiative of the Contracting authority.</p>
<p>Price and tariff setting</p>	<p>The prices/tariffs for the district water supply and sewage and waste water treatment services shall be established in accordance with Berdyansk Town Council Resolutions No. 660 of 14.12.2006 and No. 476 of 23.08.2006.</p> <p>The investments shall not be included in the tariffs for district water</p>

<sup>20</sup> Contract article 6.

	<p>supply and sewage and waste water treatment</p> <p>The prices/tariffs for the services shall be changed in accordance with the procedure established by the Ukrainian law.<sup>21</sup></p>
Conditions for the revision of the tariff	The Operator must not change the established tariffs for the district water supply and sewage and waste water treatment services on its own initiative <sup>22</sup> .
<b>Guarantees and sanctions</b>	
Legislation	<p>For the failure to fulfil or improper fulfilment of the obligations, the parties shall be liable in accordance with the Ukrainian legislation.</p> <p>Losses of one party caused by the violation by another party of its obligations shall be indemnified by the default party in full.<sup>23</sup></p>
Dispute and governing law	<p>Any disputes shall be settled by the Parties through negotiations. Should they fail to agree on any disputed issue, such an issue shall be considered in accordance with the Ukrainian law.<sup>24</sup></p> <p>This Contract and its interpretation shall be governed by the Ukrainian law.<sup>25</sup></p>
Financial penalties <sup>26</sup>	<p>Losses of one party caused by the violation by another party of its obligations shall be indemnified by the default party in full.</p> <p>Should the Operator violate the dates set for the payment of the Concession fees, the Operator shall pay a penalty of the double National Bank of Ukraine (NBU) rate applied to the delayed payment per each day of the delay.</p> <p>Should the Contracting authority violate the reimbursement for the expenses, the Contracting authority shall pay a penalty of the double NBU rate applied to the delayed payment per each day of the delay.</p> <p>Payment of the penalty shall not free the Operator from the fulfilment of its obligations.</p> <p>Should the Operator admit the deterioration of the Concession Facilities condition or its destruction, the Operator shall indemnify the Contracting authority for the losses, unless it proves that such losses or such destruction have not been its fault.</p>
Force Majeure	The Parties shall be free from any liability in case of full or partial failure to fulfil their obligations under this contract if such failure is

<sup>21</sup> Contract article 8.1.

<sup>22</sup> Contract article 8.2.

<sup>23</sup> Contract article 12.1.

<sup>24</sup> Contract article 17.1.

<sup>25</sup> Contract article 17.2.

<sup>26</sup> Contract article 12.

	caused by circumstances of insurmountable force which occurred upon the signature of the contract due to reasons that either could not be foreseen or which could not have been avoided in a rational manner. <sup>27</sup>
<b>Responsibilities of the Operator</b>	
Insurance obligation	The Operator shall bear the risk of the incidental loss of the Concession Facilities. The conceded property shall be insured by the Operator at its own expense. The Operator shall conclude a civil liability contract setting out the Operator's liability for its actions related to the operation of the Concession Facilities and insure the Concession Facilities as required by the Ukrainian law. <sup>28</sup>
<b>Organisation of the service</b>	
Operator's staff	The Operator may employ both Ukrainian and foreign citizens. The Operator shall employ 100% of the staff transferred from BMPU, shall preserve the social guarantees and conclude a collective agreement in accordance with the regulations and provisions of the regional sector agreement. <sup>29</sup>

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<sup>27</sup> Contract article 15.

<sup>28</sup> Contract article 11.

<sup>29</sup> Contract article 10.

**Annex IV: Technical information on the Berdyansk Miskvidokanal Public Utility (2007 data)**

Number of subscribers connected to the water supply network	49431
Number of subscribers connected to the water sewage system	35688
Area of service	1 town, 1 village
Water production	8404 thousand m <sup>3</sup>
Water for which payment bills are issued	4807 thousand m <sup>3</sup>
Actually paid water	4725 thousand m <sup>3</sup>
Percentage of clients having water meters (%)	Population - 72% Companies - 94%
Tariff for the water supply	Population 4.02 UAH/ m <sup>3</sup> Companies 7.94 UAH/ m <sup>3</sup>
Staff in the municipal water company	653 people
Length of the water supply network	384 km
Capacity of the water purification plant	23.5 thousand m <sup>3</sup> / day

Water supply services: <i>thousand UAH</i>			
Revenues	2006	2007	1 <sup>st</sup> half of 2008
Profits	11511,2	18247,4	8490,7
Subsidies	218,3	519,6	224,0
Other	2012,8	2113,2	674,9
TOTAL	13742,3	20880,2	9389,6
Expenditures	2006	2007	1 <sup>st</sup> half of 2008
Energy consumption	1324,1	1611,5	938,0
Staff	2462,8	3425,5	1926,3
Operation	7652,9	12781,8	6289,3
Other (taxes, etc.)	1956,2	2236,4	1222,6
TOTAL	13396,0	20055,2	10376,2
Sewage services: <i>thousand UAH</i>			
Revenues	2006	2007	1 <sup>st</sup> half of 2008
Profits	5494,7	8644,8	4045,8
Subsidies	104,2	234,9	102,4
Other	2286,3	978,0	312,9
TOTAL	7885,2	9857,7	4461,1
Expenditures	2006	2007	1 <sup>st</sup> half of 2008
Energy consumption	2094,7	1980,9	1920,6
Staff	2660,8	3858,2	1985,9
Operation	929,0	1228,9	599,8
Other (taxes, etc.)	1930,3	2654,1	1423,3
TOTAL	7614,8	9722,1	5299,6

## **Annex V: List of people interviewed**

### ***City Council of Berdyansk***

Peter Goncharuk, First Deputy Mayor of the City of Berdyansk

Anatolyi Anatolievich Stepanenko, Secretary of the City Council of Berdyansk

### ***Municipality of Berdyansk***

Alexander Alexeevich Kalinkin, Department of Municipal Economy

### ***Ministry of Housing and Municipal Economy***

Irina Viktorovna Zapatrina, Deputy Minister

Volodimir O. Omelianenko, Director, State Agency for Development of Housing and Communal Economy

### ***Parliament of Ukraine***

Valery Alexeevich Baranov, Member of Parliament of Ukraine, Former mayor of Berdyansk

Viktor Anatolievich Koulybaba, Head of the Environmental Committee at the Local Council - Advisor to a MP of Ukraine

### ***Berdyansk Miskvidokanal Public Utility***

Ivan Ivanovich Sarskyi: Chief Engineer

Tatiana Ivanovna: Chief Accountant

Galina Nikolaevna: Head of the Financial Planning Department

### ***Municipal Development Institutue Ltd.***

Alyona Babak, General Director

### ***European Bank for Reconstruction and Development***

François Gaudet, Principal Banker Municipal & Environmental Infrastructure