RESTRUCTURING PLAN
of NJSC Naftogaz of Ukraine aimed at separation of the natural gas transmission activities in accordance with the Law of Ukraine “On the Natural Gas Market”

INTRODUCTION
1. This Plan is developed in pursuance of para 18 of the Gas Sector Reform Plan approved by decision of the Cabinet of Ministers of Ukraine (hereinafter – “CMU”) of 25.03.2015 №375-p,¹ with a view to ensure separation of the natural gas transmission activity according to requirements of Law of Ukraine of 09.04.2015 №329-VIII “On the Natural Gas Market” (hereinafter – the “Law”).

2. This Plan shall not determine measures as regards other forms of restructuring of the Group of NJSC Naftogaz of Ukraine not related to natural gas transmission.

It is understood that relations between the transmission system operator and other market participants (including the storage system operator) will be built on an arms-length basis and as part of standard commercial practices.

3. This Plan is subject to approval by the Energy Community Secretariat.

EXECUTIVE SUMMARY
1. The Proposal as elaborated in this Plan envisages that as regards the operator of the gas transmission system which belongs to the state the OU unbundling model shall be selected as prescribed in Law of Ukraine of 09.04.2015 №329-VIII “On the Natural Gas Market”.

2. The Proposal as elaborated in this Plan envisages that:
1) The TSO shall be newly established Joint-Stock Company Main Gas Pipelines of Ukraine, a company 100% of shares of which belong to the state. Management of corporate rights of the state in this company shall be exercised by the State Property Fund of Ukraine.

Insulation of the TSO from political meddling and graft shall be ensured by appropriate corporate governance in line with the OECD Corporate Governance Principles;

2) The gas transmission system which belongs to the state shall be transferred to the TSO by the State Property Fund of Ukraine as a contribution to its share capital;

3) The TSO shall perform all functions and obligations of the TSO under the law without attracting resources of vertically integrated undertakings.

3. The Cabinet of Ministers of Ukraine is the supreme body in the system of executive authorities of Ukraine. It directs, coordinates and controls activities of all other executive bodies, including ministries and central executive bodies with the special status (such as the State Property Fund of Ukraine).

However, the legal status of the State Property Fund of Ukraine has certain peculiarities which make it different from the one of ministries. The principal distinguishing feature of the State Property Fund of Ukraine is that the law specifically provides for guarantees of independence of the State Property Fund of Ukraine from interventions on the part of executive authorities. This, in turn, provides legal grounds for the State Property Fund of

¹ According to para 18 of the Gas Sector Reform Plans, the Ministry of Energy and Coal Industry of Ukraine (hereinafter – “MECI”), the National Commission for State Regulation of Energy and Utilities (hereinafter – “NCSREU”) (upon consent), and the Antimonopoly Committee of Ukraine shall be assigned with “development and submission to the Energy Community Secretariat of the draft plan of restructuring of NJSC Naftogaz of Ukraine with a view to ensure separation of the natural gas transmission activity under the Law of Ukraine “On the Natural Gas Market”; timeline for completion - April – October 2015.
Ukraine to refuse to execute instructions which relate to activities of the TSO the shares of which it will manage.

In addition, the scope of powers of the State Property Fund of Ukraine as a shareholder granted by the law is minimal compared to powers of ministries which manage corporate rights of the state. This allows limiting the political influence on the TSO on the part of state bodies, including of the shareholder, without the immediate need to introduce changes into primary legislation.

As a result, the State Property Fund of Ukraine is the optimal state authority to perform functions of the TSO’s shareholder both from the viewpoint of legal independence and considering the scope of legal powers for intervention with the TSO’s activities.

This conclusion is reinforced by the fact that shares of the TSO (up to 49%) will in any event end up with the State Property Fund of Ukraine when they are privatized by the qualified partner.

Privatization of up to 49% of the TSO’s shares is allowed by the law adopted in 2014. The government of Ukraine emphasized that attracting a qualified foreign company as a partner to manage the TSO was a key factor to modernise the Ukrainian gas transmission system, build a competitive gas market and integrate into the EU gas market as well as secure transit flows through Ukraine.

4. Implementation of the Proposal according to which the State Property Fund of Ukraine acts as the TSO’s shareholder does not require immediate amendments to laws of Ukraine but rather to acts of secondary legislation related to separation of two public bodies pursuant to Article 9(6) of Directive 2009/73/EC.

5. Having due regard to concerns expressed by the Energy Community Secretariat at the hearing held on 14 March 2016, the Proposal envisages that the gas transmission system shall be further transferred to MGU as a contribution to its share capital with unrestricted ownership rights. This will require a series of amendments to the laws of Ukraine.

Such politically sensitive amendments would only be possible if they are directed at operationalization of the TSO which is a new company free from historical risks. Currently, claims of third parties (including NJSC Naftogaz of Ukraine) to PJSC Ukrtransgaz amount to circa 19-20 bcm of natural gas.

Contribution of the gas transmission system to the share capital of the TSO appears to be the only viable option to avoid any future controversies over the scope of rights enjoyed by the TSO in respect of the gas transmission system. To ensure that the right to dispose of assets of the gas transmission system should not be compromised, relevant clauses can be included in MGU’s Articles of Association.

6. Implementation of the Proposal elaborated in this Plan or of any other proposal for the TSO unbundling in accordance with Law of Ukraine of 09.04.2015 №329-VIII “On the Natural Gas Market” depends on resolution of issues related to transit of Russian gas through the territory of Ukraine. Such issues include:

1) impact of any proposal for the TSO unbundling on non-interruptible transit flows of Russian gas through the territory of Ukraine (in particular, it must be ascertained based on which legal grounds the transit of Russian gas will take place after the TSO unbundling, and the responsibility of NJSC Naftogaz of Ukraine and the state of Ukraine must be determined if following the TSO unbundling the absence of legal grounds for continued transit of Russian gas leads to interruption of transit);

2) impact of any proposal for the TSO unbundling on the Contract ТКГУ of 19.01.2009 on volumes and conditions of transit of natural gas through the territory of Ukraine for the
period of 2009-2019 between NJSC Naftogaz of Ukraine and PJSC Gazprom (hereinafter – the “Contract”); [CLASSIFIED information removed from this paragraph]

3) impact of any proposal for the TSO unbundling on performance of financial obligations of NJSC Naftogaz of Ukraine under the relevant loan agreement (hereinafter – the “Loan Agreement”). [CLASSIFIED information removed from this paragraph]

Until 01.01.2020 the Contract is effective according to which the contractor of natural gas transit services shall be NJSC Naftogaz of Ukraine. This contract is premised on the fact that NJSC Naftogaz of Ukraine has relevant technical and material resources to perform natural gas transit services (namely, using the technical capacity of its subsidiary) as well as the rights of use of the gas transmission system.

[CLASSIFIED information]

In addition, termination, cancellation or invalidation of the Contract in any way is deemed an instance of default under the Loan Agreement. The default may also occur if in the reasoned opinion of the bank any intrusion of the state into the activity or transactions of NJSC Naftogaz of Ukraine exerts material negative impact on the activity, transactions, property, financial state and other perspectives of NJSC Naftogaz of Ukraine or its ability to perform its obligations under the Loan Agreement. In case of default under the Loan Agreement, the lender may require prior settlement of the liability under the Loan Agreement as well as enforce the security. Apart from the state guarantee and the pledge of gas in underground gas storages, performance of the Loan Agreement is secured with the pledge of property rights to receive revenues under the Contract. As of 01.03.2016 the outstanding liability under the Loan Agreement amounts to USD 1.242 bln. [CLASSIFIED information removed from this paragraph]

Before the Contract is amended in a manner acceptable for Ukraine – either by mutual consent of the parties (i.e. with all necessary amendments included to comply with the current legislation of Ukraine) or by virtue of an arbitral award – NJSC Naftogaz of Ukraine shall retain the possibility to perform the Contract. This possibility will be lost if the gas transmission system of Ukraine and its operator are outside of the Group of NJSC Naftogaz of Ukraine.

While amendments to the Contract by mutual consent seem unlikely, the option of gradual implementation of the Proposal should be considered. To this end, the following steps may be taken:

1) JSC^2 MGU is established by NJSC Naftogaz of Ukraine;

2) JSC MGU develops the target operational model of the future TSO using its own staff and consultants engaged with donor funds;

3) the Corporate Governance Action Plan for JSC MGU is implemented in line with the OECD Corporate Governance Principles as developed within the framework of the EBRD project;

4) JSC MGU starts to perform individual functions of the TSO based on contracts with PJSC Ukrtransgaz and using the IT systems purchased with its own funds or donor funding;

5) following amendments to the Contract shares in JSC MGU are transferred by NJSC Naftogaz of Ukraine to the State Property Fund of Ukraine, and the fully-fledged implementation of the Proposal is launched.

^2 To speed up the establishment of a new legal entity, it may be considered to establish MGU as an LLC with its subsequent reorganization into a JSC with a view to, inter alia, implement the corporate governance action plan.
The expected timeline from the approval of this Plan till the start of the fully-fledged implementation of this Proposal is 12 to 18 months, which corresponds to the timeframe for issuing of the award by the arbitration tribunal in the transit case between NJSC Naftogaz of Ukraine and PJSC Gazprom.
A. TARGET MODEL FOR THE TSO UNBUNDLING

I. Possible unbundling models under the Law

1. The Law provides for two possible unbundling models: OU model and ISO model. Deriving from Articles 23 and 27 of the Law, the OU unbundling model determines the general requirements of unbundling and independence of the TSO, while the ISO unbundling model sets out special requirements in case para 2 of Article 23 is not observed (regarding the single person of the gas transmission system owner and the TSO). This approach is fully compliant with the Third Energy Package.3

2. Article 23 of the Law determines the key requirements to the OU model as follows:

“1. The gas transmission system operator shall be a separate legal person which is not part of a vertically integrated undertaking and carries out its commercial activities independent from activities of production, distribution, supply of natural gas, activities of wholesale sellers.

The gas transmission system operator may not carry out activities of production, distribution or supply of natural gas.

2. Only the owner of the gas transmission system may be its operator, expect for the case specified in para 1 of Article 27 of the present Law.

3. To ensure independence of the gas transmission system operator an individual or a legal person shall not simultaneously:

1) directly or indirectly exercise sole or joint control over at least one business entity (including a foreign one) carrying out production and/or supply of natural gas and/or electricity, and directly or indirectly exercise sole or joint control over the gas transmission system operator (including be the gas transmission system owner) or exercise any right over the gas transmission system operator (including any rights in respect of the gas transmission system itself);

2) directly or indirectly exercise sole or joint control over the gas transmission system operator (including be the gas transmission system owner), and directly or indirectly exercise sole or joint control over at least one business entity (including a foreign one) carrying out production and/or supply of natural gas and/or electricity or exercise any right over at least one business entity (including a foreign one) carrying out production and/or supply of natural gas and/or electricity;

3) appoint at least one official of the gas transmission system operator, and directly or indirectly exercise sole or joint control over at least one business entity carrying out production and/or supply of natural gas or exercise any right over at least one business entity carrying out production and/or supply of natural gas; and

4) be an official of the gas transmission system operator and of at least one business entity (including a foreign one) carrying out production and/or supply of natural gas.

4. The right referred to in para 3 of the present Article shall be understood as:

1) the voting right in the bodies of a legal person if the establishment of such a body is provided by the statute or other constituent document of the legal person;

2) the power to appoint officials of a legal person;

3) the holding of 50% or more of corporate rights of a legal person.

3 In the text of this Plan references to requirements of the Third Energy Package or its acts shall be understood as referring to the relevant acts binding within the Energy Community.
5. The gas transmission system operator which was part of a vertically integrated undertaking and the staff of such an operator shall not transfer information containing commercial value and held at their disposal to business entities carrying out production and/or supply of natural gas.

6. A gas transmission system operator shall ensure performance of its functions specified in para 1 of Article 20 of the present Law using its own financial, material, technical, human and other resources.

3. Article 27 of the Law determines the key requirements to the ISO model as follows:

1. The requirement of para 2 of Article 23 of the present Law shall not apply if before or on 6 October 2011 the gas transmission system was part of a vertically integrated undertaking and the gas transmission system owner has determined the business entity entitled to submit a request for certification. […]

3. A gas transmission system operator (ISO unbundling model) shall:

1) comply with requirements of paras 1, 3 of Article 23 of the present Law;

2) maintain at its disposal financial, technical, material and human resources necessary to carry out its tasks under Articles 28 of the present Law, including as regards cooperation with gas transmission system operators of neighbouring states.

4. If the ISO unbundling model is selected, the gas transmission system owner shall comply with requirements of para 2 of Article 28 of the present Law.

During the certification procedure the gas transmission system owner shall provide to the Regulator all draft contracts with the business entity which has submitted a request for certification and with any other relevant person.

Special rules applicable in case of selection of the ISO model are also stipulated in Articles 28-29 of the Law.

II. Functions and obligations of the TSO under the Ukrainian legislation

1. Functions of the TSO are provided in Article 20 of the Law whereby the TSO “shall be exclusively responsible for reliable and safe operation, maintenance, and development (including new construction and re-construction) of the gas transmission system for purposes of meeting the expected demand for transmission services with due account of gradual development of the natural gas market”.

2. Article 22 of the Law lists the following obligations of the TSO:

1. Rights and obligations of a gas transmission system operator shall be determined by the present Law, the gas transmission system code, other legislative acts as well as the transmission contract.

2. With a view to perform functions stipulated in para 1 of Article 20 of the present Law, a gas transmission system operator shall:

1) elaborate, submit for the Regulator’s approval, and place on its website the gas transmission system code;

2) elaborate, annually by 31 October submit for the Regulator’s approval, place on its website and implement the gas transmission system development plan for next 10 years taking into account development plans of gas distribution systems, gas storages, and the LNG facility;

3) take necessary measures to ensure the security of natural gas supply, including as regards uninterrupted work of the gas transmission system;
4) perform balancing as well as functions of operational dispatching of the gas transmission system in an efficient, transparent, and non-discriminatory manner;

5) elaborate and implement a compliance program as well as nominate a compliance officer in accordance with Article 31 of the present Law;

6) cooperate with other gas transmission system operators of Ukraine and operators of gas transmission systems of other states (in particular states parties of the Energy Community), including by means of operational arrangements, with a view to create regional (international) natural gas markets, cooperate with the Energy Community Regulatory Board and, in case of need, the national energy regulators of other states;

7) take necessary measures to increase rational use of energy resources and to protect the environment in the course of its activity;

8) provide information as required by the legislation;

9) ensure confidentiality of information obtained in the course of commercial activity as well as place on its website information which stimulates development of the natural gas market in a non-discriminatory manner;

10) take other measures necessary for safe and stable work of the gas transmission system as prescribed by the present Law or which do not contradict legislation. […]

5. Taking into account forecasted indicators of demand for transmission services and technical potential of the transmission system, a gas transmission system operator shall take all reasonable and possible measures to ensure the due level of interconnection of gas transmission systems of Ukraine with gas transmission systems of other countries, in particular states parties of the Energy Community.

6. A gas transmission system operator shall cooperate with other gas transmission system operators as well as with gas transmission system operators of other states parties of the Energy Community with a view to harmonize balancing rules and eliminate of obstacles to cross-border trade in natural gas as well as to create conditions for exchange trade in natural gas.

3. Detailed functions of the TSO are listed in the Gas Transmission System Code approved by the Regulator. Such functions include: collection of nominations/re-nominations and their confirmation; capacity allocation and congestion management; physical balancing of the gas transmission system; provision of balancing services if transmission services customers have failed to settle their imbalances, etc.

III. TSO unbundling proposal

1. The Plan proposes that as regards the operator of the gas transmission system which belongs to the state (hereinafter - the “TSO”) the OU unbundling model shall be selected (hereinafter - the “Proposal”).

2. The Proposal envisages that:

1) The TSO shall be Joint-Stock Company Main Gas Pipelines of Ukraine (hereinafter - “MGU”), a company 100% of shares of which belong to the state.4

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4 Under Article 24(1) of the Law of Ukraine “On Joint-Stock Companies” (per the wording effective as of 01.05.2016) a public JSC shall undergo the procedure for listing, and its shares shall remain in at least one stock exchange register in Ukraine. This requirement shall apply to all public JSCs as of 01.01.2018. At the same time, due to requirements of Article 5 of the Law of Ukraine “On Privatization of State Property” shares of MGU may not be included in the stock exchange register. If amendments are not made to the Law of Ukraine “On Joint-Stock Companies” excluding the TSO from the scope of application of the said requirement, then it is proposed that MGU be established in the form of a private JSC.
Management of corporate rights of the state in MGU shall be exercised by the State Property Fund of Ukraine (hereinafter - “SPFU”).

Independence of the TSO shall be ensured by appropriate corporate governance of MGU in line with the OECD Corporate Governance Principles;

2) The gas transmission system which is the state property shall be provided to MGU by SPFU as a contribution to its share capital.

3) MGU shall perform all functions and obligations of the TSO under the Law without attracting resources of vertically integrated undertakings.

The Proposal is graphically presented in Annex 1.

3. It should be noted that qualification of the unbundling model described in the Proposal depends on the interpretation of the term “owner” in para 2 of Article 23 of the Law. During the drafting of the Law some state authorities expressed the view that this term shall be understood as referring to the state as the owner of the gas transmission system (main gas pipeline transport) of Ukraine according to the legislation. In connection with this interpretation the conclusion was made that it was impossible to apply the OU unbundling model in case of the Ukrainian TSO.

In our view, this approach is discriminatory and contradicts the Law. First of all, the Law does not contain rules which would limit the choice of the unbundling model for the TSO depending on whether the gas transmission system belongs to the state. This rule as such would be unacceptable as it would discriminate against the state as one of the subjects of ownership.

Secondly, according to para 2 of Article 2 of the Law “authorities as well as courts in applying provisions of the present Law shall take into account the case law of the Energy Community and the EU, in particular judgments of the Court of Justice of the EU (the European Court of Justice, the General Court), case law of the European Commission and the Energy Community Secretariat regarding application of provisions of the EU acquis mentioned in para 1 of the present Article”. The practice of application of Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC (hereinafter – “Directive 2009/73/EC”) by the European Commission (hereinafter – the “Commission”) while issuing opinions on certification of transmission system operators evidences that regardless of the form of ownership to the asset itself (either state or private) the owner of the transmission system shall be a certain legal entity (ministry, other state authority, private or state company). If the legal entity which is the owner of the transmission system is a state authority, Directive 2009/73/EC does not require privatization of the transmission system with a view to implement the OU unbundling model. It suffices to comply with the requirement that no control or other rights as regards the transmission system operator or the transmission system are exercised by individuals and/or legal persons controlling producers and/or suppliers of natural gas and/or electricity.

IV. Justification of the Proposal: compliance with requirements on elimination of influence on the TSO’s activities through control or rights of other persons

1. Requirements as regards elimination of influence on the TSO’s activities through control or rights of other persons with relations to producers and/or suppliers of natural gas and/or electricity are contained in subparas b), c) and d) of para 1, in paras 2 and 3 of Article 9 of Directive 2009/73EC. These requirements include:

- requirements regarding the absence of control and rights over the TSO with person/persons controlling producers and/or suppliers of natural gas and/or electricity (hereinafter – “Unbundling requirement №1”);
- requirement regarding the absence of control and rights over producers and/or suppliers of natural gas and/or electricity with person/persons controlling the TSO (hereinafter – “Unbundling requirement №2”);
- requirements regarding limitations on the scope of persons which may make nominations in the TSO (hereinafter – “Unbundling requirement №3”);
- requirements regarding simultaneous holding of office by officials of the TSO (hereinafter – “Unbundling requirement №4”).

Similar requirements are transposed in para 3 of Article 23 of the Law.

2. Under para 6 of Article 9 of Directive 2009/73/EC, it is allowed that the state simultaneously exercise control over transmission, extraction (production) and supply of natural gas and electricity.

In this case, it is necessary to designate two separate state bodies one of which controls the gas transmission system operator and the gas transmission system on behalf of the state, and the other one controls producers and suppliers of natural gas and electricity which belong to the state sector of economy.

At the same time, it is necessary that there is no control from any other person in respect of the two bodies. The absence of control on the part of a third person as well as independence of the two designated state bodies from one another shall be determined based on the analysis of the scope of their legislative powers, including powers to give mandatory assignments and instructions.\(^5\)

This rule of para 6 of Article 9 of Directive 2009/73/EC is applicable by virtue of para 2 of Article 2 of the Law considering that under the legislation of Ukraine the state as such is not a person while state authorities are established as legal entities.

3. The Proposal envisages that Unbundling requirements №1-4 shall be fulfilled as follows:

1) Compliance with Unbundling requirement №1

Pursuant to subpara 1 of para 3 of Article 23 of the Law, “an individual or a legal person shall not simultaneously … directly or indirectly exercise sole or joint control over at least one business entity (including a foreign one) carrying out production and/or supply of natural gas and/or electricity, and directly or indirectly exercise sole or joint control over the gas transmission system operator (including be the gas transmission system owner) or exercise any right over the gas transmission system operator (including any rights in respect of the gas transmission system itself)”.

Currently state authorities controlling the activities of producers and/or suppliers of natural gas and/or electricity are:

- MECI; and
- the Ministry of Economic Development and Trade of Ukraine (hereinafter –“MEDT”).

i. MECI

According to the MECI Regulation approved by Decree of the President of Ukraine of 06.04.2011 №382/2011,\(^6\) MECI shall be the main body within the system of central

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\(^6\) In connection with the renewal of the parliamentary-presidential republic based on Law of Ukraine of 21.02.2015 №742-VII, the Law of Ukraine of 17.03.2011 №3166-VI “On central executive bodies” (hereinafter – “CEB Law”) was amended to determine the body authorized to adopt regulations of ministries and other central executive authorities. According to these amendments inserted by Law of Ukraine of 27.02.2014 №795-VII, CMU shall be entrusted with these powers, which in line with the current version of the Constitution of Ukraine. Thus, the MECI Regulation adopted by the decree of the President of Ukraine contradicts the Constitution of Ukraine and laws of Ukraine.
executive authorities in the field of development and implementation of the state policy in electricity, nuclear industry, coal industry, peat industry and oil and gas complexes. According to this Regulation, MECI shall in pursuance of its assignments:

- take decisions on establishment of state enterprises of the fuel and energy complex, on reorganization and liquidation of state enterprises, institutions and organizations belonging to the sphere of management of MECI;
- exercise management of state corporate rights within the competence and per the procedure established by CMU;
- in respect of state enterprises, institutions and organizations within the sphere of management of MECI – adopt their statutes (regulations), carry out control of their performance, per the established procedure adopt their restructuring and rehabilitation plans;
- in respect of state enterprises, institutions and organizations within the sphere of management of MECI as well as of business entities in respect of which MECI performs management of corporate rights of the state⁷ - approve their annual financial and investment plans as well as medium-term (3-5 year) investment plans, per the established procedure control their implementation, perform internal audit, including control of financial and business activity;
- perform accounting of state property managed by MECI;
- take decisions on further use of state property not contributed to the share capital of companies established in the process of corporatization.⁸

In order to organize its activities MECI:

- performs selection of candidates for management positions in state enterprises, institutions and organizations within its sphere of management;
- organizes planning and financial work at state enterprises, institutions and organizations within its sphere of management; performs control over the use of financial and other resources; ensures and helps with improvement of the statutory accounting.⁹

The Minister¹⁰ leading MECI shall:

- appoint with the consent of local state administration heads and dismiss management of enterprises, institutions and organizations within the sphere of management of MECI except in cases provided in the law;
- impose disciplinary sanctions on directors of state enterprises, institutions and organizations within the sphere of its management.¹¹

According to MECI Decree of 15.01.2016 №16, the sphere of management of MECI shall cover the following enterprises of the energy sector: State Enterprise Lysychanska Cogeneration Plant, State Enterprise Zuyivska Experimental Cogeneration Plant, State Enterprise Donuzlavskaya Wind Power Station, State Enterprise Kaluska Cogeneration Plant, State Enterprise National Energy Company Ukrenergo, State Enterprise Regional

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⁷ In Ukraine, business entities of the state sector of economy may be divided into two groups: enterprises which have not yet undergone corporatization or are not subject to corporatization and companies. In relation to the first group, CMU determines the central executive body to whose sphere of management this entity belongs, and this body shall control the activities of such an enterprise. In relation to the second group, CMU determines the person (central executive body, another company) in charge of management of corporate rights of the state in the capacity of the shareholder.

⁸ MECI Regulation approved by Decree of the President of Ukraine of 06.04.2011 №382/2011, para 4(38)-(42), 4(46).

⁹ MECI Regulation approved by Decree of the President of Ukraine of 06.04.2011 №382/2011, para 5(2)-(3).

¹⁰ According to Law of Ukraine of 10.12.2015 №889-VIII “On the State Service of Ukraine” these powers shall be transferred to the state secretary of MECI as of 01.05.2016.

¹¹ CEB Law, art.8(2)(12)-(13).

This Decree also determines the list of business entities in respect of which MECI performs management of state corporate rights, which includes: PJSC Dniprovska HAPS, PJSC Ukhrhydroenergo.

In addition, in practice MECI exercises powers in respect of energy sector enterprises even if they do not belong to its sphere of management or if they are not included in the list of business entities in respect of which MECI performs management of state corporate rights. For instance, by Decree of 21.01.2016 №24 MECI obliged PJSC DTEK Dniprooblenergo, shares of which are managed by SPFU, to transfer state property on its balance sheet into municipal property of the municipality of the city of Dnipropetrovsk. It may be concluded that in this case MECI realized its powers as regards state property on the balance-sheet of this company.

ii. MEDT

The other state authority controlling producers and/or suppliers of natural gas is MEDT.

According to para 15 of the Charter of NJSC Naftogaz of Ukraine approved by CMU Resolution of 05.12.2015 №1002, 100% of shares of NJSC Naftogaz of Ukraine is owned by the state through MEDT. Per para 48 of the Charter of NJSC Naftogaz of Ukraine, MEDT exercises a series of powers which belong to the competence of the General Shareholders' Meeting, namely:

- determination of the main directions of activity of NJSC Naftogaz of Ukraine and approval of its strategy and mission;
- amendments to the charter;
- approval of regulations of the General Shareholders' Meeting, Supervisory Board and the Management Board, as well as amendments thereto;
- taking of decisions on dismissal of members of the Supervisory Board except in cases provided in the law;
- selection and dismissal of the chairman and members of the Management Board (per nominations of the independent committee for nomination and remuneration);
- approval of the business plan of NJSC Naftogaz of Ukraine, in particular of the financial plan (budget) and the investment program, etc.

Per this Resolution the Supervisory Board of NJSC Naftogaz of Ukraine consists of five persons, and it shall be approved by MEDT as a shareholder. MEDT approves one member of the Supervisory Board with the agreement of the President of Ukraine and another one with CMU's agreement. Other three members of the Supervisory Board are determined upon competitive selection of candidates who meet the criteria of independence.

It shall be noted that according to para 11 of its Charter NJSC Naftogaz Ukraine is a fully-fledged shareholder (founder, participant) of business entities shares/corporate rights of which are transferred to its share capital, as well as of entities established by it or companies shares/corporate rights of which have been otherwise acquired. These companies include, in particular, PJSC Ukrgazvydobuvannya, PJSC Ukrnafta and JSC State Joint-Stock Company Chornomornaftogas.
It follows that MECI and MEDT exercise control over producers and suppliers of natural gas and/or electricity, and thus neither of them may be the person that exercises control or any rights over the TSO in the meaning of the Law (taking into account the case law of the Commission and the Energy Community Secretariat).

According to the Proposal, neither MECI nor MEDT may exercise control over the TSO. Moreover, MECI may not control MGU as this would contradict the best international practice of corporate governance. MECI is the central executive body in charge of development and implementation of the state policy in the fuel and energy complex, which includes the authority to determine the direction of the industry development and instruments to that effect. MECI shall be responsible for performance of its functions and powers (for example, safeguarding of the security of natural gas supply, response to crisis situations, determination of technical rules and security standards in the sector). At MECI’s level the real conflict of interests is thus created where MECI’s interests as a shareholder – to maximize the return on assets represented by TSO’s shares – contradict MECI’s status as the line ministry required to ensure the least burdensome conditions for the functioning of the market as a whole.

Finally, as shown in Exhibits 1 and 2, MECI has been active in promoting interests of heat and electricity enterprises by requesting preferential treatment for these consumers from the TSO.

2) Compliance with Unbundling requirement №2

Pursuant to subpara 2 of para 3 of Article 23 of the Law, “an individual or a legal person shall not simultaneously … directly or indirectly exercise sole or joint control over the gas transmission system operator (including be the gas transmission system owner), and directly or indirectly exercise sole or joint control over at least one business entity (including a foreign one) carrying out production and/or supply of natural gas and/or electricity or exercise any right over at least one business entity (including a foreign one) carrying out production and/or supply of natural gas and/or electricity”.

The Proposal envisages that control over the TSO shall be performed by SPFU. The Proposal is premised on fulfilment of two conditions:

- SPFU does not control and does not have rights over producers and/or suppliers of natural gas and/or electricity within the meaning of the Law (taking into account the case law of the Commission and the Energy Community Secretariat);
- there is no third person controlling the decision-making process of SPFU and MECI/MEDT with the regard of the TSO.

i. General characteristics of SPFU as the shareholder of MGU

SPFU is the central executive body with the special status in charge of implementation of the state policy in privatization, lease, use and alienation of state property, management of state property objects, including of state corporate rights. SPFU’s activities are regulated by a separate law as well as by the CEB Law to the extent that it does not contradict the Constitution and other laws (in particular the SPFU Law).

The SPFU Chairman shall be appointed upon submission of the Prime-minister of Ukraine and dismissed by the Verkhovna Rada of Ukraine (hereinafter – “VRU”). The SPFU

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13 CEB Law, Article 24(4).
14 Constitution of Ukraine, Article 85; CEB Law, art.24.
Deputy Chairmen shall be appointed and dismissed by CMU upon submission of the Prime-minister of Ukraine.\(^{15}\)

The main functions of SPFU include, *inter alia*:

- implementation of the state policy in the sphere of privatization;
- control in the sphere of organization and carrying out of privatization of state property;
- management of state property objects;
- facilitation of demonopolization of economy and creation of conditions for producers to compete;
- enforcement of the Constitution and laws of Ukraine, acts of the President of Ukraine, of CMU and of other relevant legislation and monitoring of their implementation.\(^{16}\)

SPFU shall be guided by the Constitution of Ukraine, laws of Ukraine, acts of the President of Ukraine, of VRU and of CMU, other legal acts of Ukraine, orders of the President and the Prime-minister of Ukraine.\(^{17}\) At the same time, the SPFU Law stipulates that SPFU shall within its competence, based on and in pursuance of the Constitution and laws of Ukraine, acts of the President of Ukraine and of CMU issue decrees to be signed the SPFU Chairman.\(^{18}\)

The special status of SPFU is determined by the Constitution and laws of Ukraine, acts of the President of Ukraine and consists of the special procedure for appointment and dismissal of the SPFU Chairman.\(^{19}\) The special status of SPFU also envisaged the following:

1) SPFU shall be accountable to the President of Ukraine.\(^{20}\)

2) The SPFU Chairman is not a member of CMU, and thus rules binding on the Ministers being members of CMU are not applicable thereto. According to the law, CMU members are jointly liable for the results of CMU’s activities as a collegial executive body.\(^{21}\) Per the CMU Rules of Procedure approved by CMU Resolution of 18.07.2007 №950 (hereinafter – “CMU Rules of Procedure”), CMU members may not act contrary to the position of CMU, disclose without the consent of the Prime-minister of Ukraine any information on the course of CMU meetings and assessments of the positions provided by CMU members.\(^{22}\) Moreover, CMU members shall ensure harmonization and coordination of their actions during implementation of the state policy.\(^{23}\)

Similar to those of the Antimonopoly Committee of Ukraine, the State Committee for Television and Radio Broadcasting of Ukraine and other authorities with the special status, issues related to SPFU’s activities shall be raised in CMU by the Prime-minister of Ukraine.\(^{24}\)

\(^{15}\) CEB Law, art.24. SPFU Law Article 8 stipulates that the President of Ukraine shall appoint the SPFU Deputy Chairmen, which contradicts the current version of the Constitution of Ukraine.

\(^{16}\) SPFU Law, art.4(1).

\(^{17}\) SPFU Law, art.3(1).

\(^{18}\) SPFU Law, art.9(1).

\(^{19}\) SPFU Law, art.1(1).

\(^{20}\) SPFU Law, art.1(1).


\(^{22}\) CMU Rules of Procedure, para 4(3).

\(^{23}\) CMU Rules of Procedure, para 8(4).

\(^{24}\) CEB Law, art.24(3).
3) The SPFU Law includes a separate guarantee of independence for SPFU employees. Per Article 13 of the SPFU Law:

“1. Intervention by central and local executive authorities, local governments and their officials, civil organizations and representatives into the activities of the State Property Fund of Ukraine shall be prohibited except in cases provided by the law.

2. Any form of influence on employees of the State Property Fund of Ukraine with the aim to obstruct the fulfilment of their duties or to induce an illegal decision entails the responsibility according to the law.”

Any instructions or other assignments may be given to SPFU by the state authorities (in particular, CMU) only in cases stipulated by the law. According to the CMU Law, special rules governing relations between the CMU and certain central executive bodies (in particular, SPFU) may be prescribed by the laws of Ukraine.  

The CMU Rules of Procedure take account of this provision by stipulating that CMU’s powers in relations with central executive bodies of which the status and special rules of activity are prescribed by separate laws shall be performed with account of provisions of such laws.

4) The SPFU Law stipulates specific rights of SPFU to receive information related to performance of its tasks from the state and local authorities as well as from enterprises, institutions and organizations of all forms of ownership, which may be useful in the course of management of corporate right of MGU for determination of the level of functional independence of MGU. In addition, SPFU has a wide network of regional offices, which will provide an effective tool of control on the part of the shareholder.

Management of state corporate rights by SPFU is performed per one of the two work streams:

- management of objects of privatization, i.e. of state corporate rights in companies in respect of which the decision on privatization has been taken or the privatization or share placement plan has been adopted;
- management of objects of management, i.e. state corporate rights in companies within the sphere of management of SPFU, in particular management of companies established by SPFU.

Separate department of the central office of SPFU handle each of these streams:

- Department of competitive sales of privatization objects – in respect of privatization objects;
- Department of contract management, international property and corporate relations – in relation of objects of management.

SPFU performs duties assigned thereto in the sphere of property privatization pursuant to Law of Ukraine of 04.03.1992 №2163-XII “On Privatization of State Property” (hereinafter – the “Privatization Law”), the SPFU Law and other laws (e.g., Law of Ukraine of 06.03.1992 №2171-XII “On Privatization of Small State Enterprises (Small-Scale Privatization)”). Stages of privatization and engagement of SPFU and other persons in the privatization process are presented in Annex 2.

In the sphere of privatization, SPFU shall, inter alia:

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25 CMU Law, art.21(8).
26 CMU Rules of Procedure, para 82(4).
27 SPFU Law, art.10.
29 SPFU Law, art.4(1)(3).
- perform powers of the owner of state property, including of corporate rights, in the
course of the privatization process and control activities of enterprises, institutions
and organizations within its sphere of management;
- perform the sale of state property in the privatization process;
- adopt the decision on privatization (except in cases where such a decision shall be
made by CMU);
- establish privatization commissions and other similar bodies;
- approve plans of privatization of state property, plans of placement of shares of
joint-stock companies in the privatization process (except for objects of the fuel and
energy complex decision on which shall be approved by CMU);
- conclude agreements on preparation of objects to privatization and their sale,
contracts for performance of independent appraisal of property in the privatization
process and in other cases provided in the legislation;
- terminate contracts with directors of state enterprises management functions over
which have been assigned to SPFU;
- control performance of contracts of sale-purchase of state property.\textsuperscript{30}

Under the Privatization Law, state privatization authorities have no rights to interfere with
the activities of enterprises except in cases stipulated by the legislation of Ukraine and by
constituent documents of these companies.\textsuperscript{31}

It shall be noted that under the Privatization Law decisions on privatization and conditions
for the sale of objects of the fuel and energy complex shall be approved by CMU.\textsuperscript{32}

SPFU performs duties assigned thereto in the sphere of state property management
pursuant to Law of Ukraine “On Management of State Property Objects” of
21.09.2006 №185-V (hereinafter – “State Property Management Law”) as well as to the
SPFU Law.

Importantly, powers of managing subjects in the state sector of economy in respect of
business entities shall be defined by the law.\textsuperscript{33} Likewise, special rules regarding
management of companies with the state shareholding shall be determined by laws of
Ukraine.\textsuperscript{34} This means that secondary legislation may not prescribe additional powers for
managing subjects with respect to business entities within their sphere of management.

Under the law managing subjects shall perform management of state corporate rights in
companies management functions over which have been assigned to them by means of
appointment of state representatives for participation in the General Shareholders'
Meetings and appointment (selection) of state representatives and independent members
of the Supervisory Board of companies where the state acts as the sole shareholder
(participant).\textsuperscript{35} If state corporate rights represent 100% of shares, according to the State
Property Management Law functions of management of state corporate rights shall be
performed directly and without holding of the General Shareholders’ Meeting.\textsuperscript{36}

In the sphere of management of state property (state corporate rights) SPFU shall:

\textsuperscript{30} SPFU Law, art. 5(1)(2). See also Privatization Law, art. 7(3).
\textsuperscript{31} Privatization Law, art.7(6).
\textsuperscript{32} Privatization Law, art. 5(5). See the Procedure for making decision on privatization and approval of
conditions for sale of Group D objects and objects of the fuel and energy complex approved by CMU
Resolution of 13.06.2012 №525.
\textsuperscript{33} Commercial Code of Ukraine, art. 22(3).
\textsuperscript{34} Commercial Code of Ukraine, art. 89 (per the wording of Draft Law №3062 adopted by VRU in the second
reading and as a whole on 18.02.2016).
\textsuperscript{35} State Property Management Law, art.11(3) (per the wording of Draft Law №3062 adopted by VRU in the
second reading and as a whole on 18.02.2016).
\textsuperscript{36} State Property Management Law, art.11(4).
- perform management of state corporate rights within its sphere of management per the procedure set by CMU;
- ensure approval of contracts of pledge and financial loans for companies within its sphere of management;
- perform analysis of efficiency of management of state corporate rights within its sphere of management;
- pursuant to the legislation appoint state representatives in management bodies of business entities state corporate rights of which it manages, enter into agency agreements with them, instruct them in terms of voting per the agenda of the General Shareholders' Meeting and Supervisory Board meetings, as well as define candidates of independent members of the Supervisory Board nominated for appointment to the Supervisory Board of companies state corporate rights of which it manages;
- control performance of conditions of contracts with chairpersons of executive bodies of companies within its sphere of management;
- approve agreements of joint activity, commission, agency and property management agreements as well as amendments thereto for companies with the state shareholding of more than 50%;
- perform other functions related to management of state corporate rights stipulated in the legislation.

Also, if state corporate rights exceed 25% of the share capital of the business entity, a representative of SPFU or of the authorized managing organ shall be included in the Supervisory Board and the revision commission.

It should be noted that the scope of powers as regards management of state corporate rights (and, accordingly, possibilities for intrusion in the activities of objects of management) assigned to SPFU by the State Property Management Law is much narrower than the one of the authorized managing organs (namely, ministries). According to the State Property Management Law and acts of secondary legislation SPFU does not belong to authorized managing organs. Per the State Property Management Law, authorized managing organs shall:

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37 SPFU Law, art.5(1)(3).
38 State Property Management Law, art.7(1)(3)(a).
39 SPFU Law, art.5(1)(3).
40 SPFU Law, art. (1)(3).
41 State Property Management Law, art.7(1)(3)(и).
42 State Property Management Law, art.7(1)(3)(и).
43 State Property Management Law, art.7(1)(3)(и).
44 State Property Management Law, art.7(1)(1)(й).
45 State Property Management Law, art.7(1)(1)(п).
46 State Property Management Law, art.11(12). Per Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016, Article 11 of the State Property Management Law shall be subject to the following amendments: instead of a representative of SPFU or of the authorized managing organ, the chairperson of the Supervisory Board of a business entity with the state shareholding exceeding 50% may be any of its members; the provision shall be repealed according to which members of the Supervisory Board representing state interests shall vote upon instructions provided by SPFU or the authorized managing organ; the provision shall be repealed according to which the state representative shall participate in the General Shareholders' Meeting and vote on every question of the agenda exclusively in accordance with voting instructions provided in the representation assignment issued by the authorized managing organ or SPFU.
47 Throughout the text of the State Property Management Law the wording “SPFU or the authorized managing organs” is used. See, for example, State Property Management Law, art.11.
48 See, e.g., CMU Resolution of 30.10.2014 №678 according to which the procedure for management of corporate rights for authorized managing organs and SPFU is set separately with reference to Article 6(1)(13) and 7(1)(3)(а) of the State Property Management Law, respectively.
- approve charters (regulations) of business entities and control their observance;\(^{49}\)
- appoint and dismiss directors of business entities, conclude and terminate contracts with them, control compliance with their requirements;\(^{50}\)
- develop and approve strategic development plans for business entities corporate rights of which they manage or control over which activity they perform, and control their performance;\(^{51}\)
- approve annual financial and investment plans as well as medium-term (3-5 years) investment plans for business entities within their sphere of management, control their performance per the prescribed procedure;\(^{52}\)
- monitor the financial activity, in particular performance of financial plan indicators, of enterprises within their sphere of management and take measures to improve their work;\(^{53}\)
- determine persons to represent the state in the managing bodies of companies state corporate rights of which they manage and ensure their appointment (selection), conclude agency contracts with them, instruct them in terms of voting per the agenda of the General Shareholders’ Meeting;\(^{54}\)
- approve agreements of joint activity, commission, agency and property management agreements as well as amendments thereto for companies with the state shareholding exceeding 50%;\(^{55}\)
- organize and carry out competitive selections to determine directors of business entities of the state sector of economy;\(^{56}\)
- ensure bringing into compliance with the legislation of constituent documents and bylaws of business entities;\(^{57}\)
- ensure stock-taking of property of business entities per the procedure approved by CMU.\(^{58}\)

In view of the above, SPFU is the most optimal state authority to become the shareholder of MGU considering the level of its legal independence and the scope of powers assigned thereto by the law as regards intervention into the TSO’s activity.

**ii. Whether SPFU exercises control or any rights as regards producers and/or suppliers of natural gas and/or electricity in the meaning of the Law (account given to the case law of the Commission and the ECS)**

Per the publicly available data, SPFU does not control and does not have rights in respect of producers and/or suppliers of natural gas.\(^{59}\)

At the same time, SPFU manages state corporate rights in 21 companies engaged in production and supply of electricity. Among them:

\(^{49}\) State Property Management Law, art.6(1)(3).
\(^{50}\) State Property Management Law, art.6(1)(4).
\(^{51}\) State Property Management Law, art.6(1)(5).
\(^{52}\) State Property Management Law, art.6(1)(6).
\(^{53}\) State Property Management Law, art.6(1)(7).
\(^{54}\) State Property Management Law, art.6(1)(14-1).
\(^{55}\) State Property Management Law, art.6(1)(20).
\(^{56}\) State Property Management Law, art.6(1)(21).
\(^{57}\) State Property Management Law, art.6(1)(24).
\(^{58}\) State Property Management Law, art.6(1)(25).
\(^{59}\) In the gas sector, SPFU manages corporate rights of PJSC Korostyshivgaz. According to the NCSREU Licensing Register as of 01.01.2016, PJSC Korostyshivgaz is licensed in natural gas distribution. The license for natural gas supply is absent. The NCSREU Licensing Register is available here: \[\text{http://www.nerc.gov.ua/?id=11995}\]. According to the official website of SPFU, it was proposed to include PJSC Korostyshivgaz into the list of state property objects subject to privatization in 2015-2016. See: \[\text{http://www.spfu.gov.ua/ua/news/FDMU-proponue-vkluchiti-do-postanovi-N\#271-20-ob/'ektiv-i-viluchiti-z-nej-75-502.html}\].
- two companies (PJSC Krymteploelectrotsentral and PJSC Krymenergo) are located in the temporarily occupied territory of Ukraine, and SPFU is effectively deprived of the possibility to manage this state shareholding;
- other 19 companies are currently undergoing the privatization process (see Annex 3).  

Among these 19 companies:
- five (PJSC Khmelnyskoblenergo, PJSC Mykolayivoblenergo, JSC Kharkivoblenenergo, OJSC Zaporizhzhyaoblenergo, OJSC Ternopiloblenergo) are state property objects of strategic significance to the state economy and defence;  
- five (PJSC Mykolayivska Cogeneration Plant, PJSC Dniprodzerzhynska Cogeneration Plant, PJSC Khersonska Cogeneration Plant, PJSC Odeska Cogeneration Plant, PJSC Kyivenergo) are active in production of heat as well as of electricity by cogeneration plants, and the sales of electricity generated by cogeneration plants is subject to regulated tariffs approved by NCSREU;  
- PJSC Khmelnyskoblenergo, PJSC Mykolayivoblenergo, JSC Kharkivoblenenergo, OJSC Zaporizhzhyaoblenergo, OJSC Ternopiloblenergo, PJSC Cherkasyoblenergo, PJSC DTEK Donetsoblenergo, PJSC Kyivenergo, PJSC Sumyoblenergo, PJSC DTEK Dniprooblenergo, PJSC Odesaoblenergo are licensed suppliers of electricity at regulated tariffs which also have licenses for electricity distribution. Per the licensing conditions for electricity supply set by NCSREU, such companies (as well as their affiliated enterprises) may not carry out activities of supply of electricity at non-regulated tariffs within their defined territory.  
- PJSC DTEK Dniproenergo, PJSC DTEK Zakhidenergo, PJSC Donbasenergo, PJSC Tsentrenergo are licensed producers of electricity and heat by cogeneration stations. All electricity generated by cogeneration stations is sold to State Enterprise Energorynok at prices calculated based on the method of the forecasted wholesale price used by NCSREU.  

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60 SPFU Decree of 30.12.2015 №2064 “On approval of the list of Group C,D objects subject to privatization in 2016”.
61 See the List of state property objects of strategic significance to the state economy and defence approved by CMU Resolution of 04.03.2015 №83.
62 In respect of state property objects of strategic significance to the state economy and defence, CMU shall approve decisions of the authorized managing organs on their establishment, reorganization and liquidation; approve conditions of privatization and restructuring of such objects; approve projects of pre-privatization preparation and the procedure for control of fulfilment of undertakings stipulated in the sale-purchase agreements; adopt a decision on privatization and conditions of their sale. See State Property Management Law, art.5; Privatization Law, art.5(9), 10-1, 27. Moreover, according to current legislation appointment of the director of a business entity of strategic significance to the state economy and defence with the asset value per the latest annual financial statements or annual net income exceeding UAH 200 million shall be made based on results of special selection and shall be approved by CMU upon submission of the chairman of the relevant managing subject.
63 Rules of Wholesale Market of Ukraine approved by NCSREU Resolution of 09.08.2012 №1028, para 1.1.2. Regulated tariffs for electricity generated by cogeneration plants are established and approved according to NCSREU Resolutions of 12.10.2005 №896 “On approval of the Procedure for calculation of tariffs for electricity and heat generated by cogeneration plants, cogeneration stations and nuclear plants and by installations using alternative or renewable energy sources” and of 12.10.2005 №898 “On approval of the Procedure of revision and approval of tariffs for licensees of production of electricity and heat energy”.
64 Conditions and rules of supply of electricity at regulated tariffs approved by NCSREU Resolution of 13.06.1996 №15/1, para 2.3.
65 See annual information on PJSC DTEK Dniprooblenergo, PJSC DTEK Zakhidenergo, PJSC Donbasenergo.
Based on the case law of the Commission, the fact that SPFU has rights over 21 afore-mentioned companies should not be an obstacle for SPFU’s control of MGU. According to the Commission, Unbundling requirement №2 is met where the body that controls the TSO has no rights over producers/suppliers of natural gas/electricity or when there is no conflict of interests which may lead to abuse of control over the TSO in favour of other assets managed by this body and to the detriment of other network users. In its opinion on certification of REN Rede Elétrica Nacional S.A. and REN Gasodutos S.A. the Commission noted that there shall be no conflict of interests and thus no obstacle to control where the body controlling the TSO or the transmission system simultaneously controls and/or has rights over producers/suppliers of natural gas/electricity if:

- such control or rights are of temporary nature;
- such producers/suppliers of natural gas/electricity perform their activities within the regulated segment of the market regulated by the national energy regulator, thus their income is limited by set tariffs.

In this case, the Commission also took into account additional measures stipulated by the national energy regulator in the preliminary certification decision:

- prohibition of simultaneous holding of office in the TSO and in other controlled companies in the natural gas/electricity sector;
- prohibition of IT systems shared by the TSO and others controlled companies in the natural gas/electricity sector;
- prohibition of use of shared consulting services by the TSO and other controlled companies in the natural gas/electricity sector.

While analysing the potential conflict of interest at the level of SPFU associated with simultaneous management of state corporate rights in 21 companies and in MGU, the following factors must be accounted for:

- SPFU manages corporate rights of 21 afore-mentioned companies for further privatization, and it thus presents a temporary activity minding that the Privatization Law sets the maximum timeline for privatization which may not be more than two years;
- the Privatization Law prohibits SPFU to interfere with business activities of enterprises the shares of which are subject to privatization except in cases provided by the legislation or constituent documents of these enterprises;
- management of state property in the course of privatization shall be made according to the plan of privatization/share placement approved by CMU which contains basic parameters of privatization;
- within SPFU’s organizational structure management of privatization objects and of management objects is functionally performed by separate structural units;
- compliance with privatization legislation is controlled, in particular, by VRU’s Special Control Commission on privatization.

Privatization Law, art.10.
In the course of privatization potential buyers have sufficient information to detect possible manipulations of SPFU aimed at artificial increase of the value of privatization objects. Before approval of the plan of privatization/share placement a compulsory audit of financial statements of the company whose shares are to be privatized is carried out.\(^69\) The draft plan of privatization developed by the privatization commission shall be accompanied by the act of property appraisal of the privatization object or the report of appraisal of the privatization object alongside the approved opinion on its value.\(^70\) The appraisal is performed according to the methodology approved by CMU.\(^71\) The law requires SPFU to ensure transparency of the privatization procedure and disclosure of information on privatization objects, including information on their financial state and other economic indicators.\(^72\) This is in particular related to Group D objects which include shares of companies of strategic significance to the state economy and defence or which show signs of dominance on the all-nation market of goods and services. In respect of such objects, the legislation establishes the obligation of prior disclosure of their financial statements (balance sheet, income statement, cash flow statement, statement of equity) and of other economic information per the list set by SPFU.\(^73\) The Privatization Law prescribes administrative sanctions to be imposed on SPFU officials for groundless refusal to provide information on the privatization object.\(^74\) Finally, in the course of privatization potential buyers can conduct additional verifications of information on the financial state of the privatization object, which is commonplace.

Thus, SPFU has limited economic incentives to abuse its control over MGU in favour of energy sector companies constituting objects of privatization with a view to, for instance, increasing the sales value of the relevant state property object. This is so because any such manipulations can be effectively detected during the privatization process, particularly given the duties of information disclosure, nature of information and its available amount.

In addition, the analysis of business activities of electricity sector companies' shares of which are managed by SPFU provides grounds to believe that it is almost impossible for SPFU to create target benefits for such companies through intervention in TSO's business activities. This is so since all these companies currently sell electricity either at regulated prices or at prices formed using the pricing algorithm of the single wholesale market. The pricing algorithm of the wholesale electricity market prevents creation of target benefits for individual companies as the increased demand for electricity is satisfied through selection of bids in a pre-approved order.

All these factors demonstrate that management of shareholdings in energy companies by SPFU in the form of privatization objects should not create grounds for a conflict of interest at the level of SPFU and should thus not preclude certification.

On a separate note, SPFU has certain powers in respect of state representatives in the General Shareholders' Meeting and managing bodies of state enterprises or companies shares of which are owned by the state but not managed by SPFU. In particular:

- a state representative is appointed from among members of the Supervisory Board by a decision of the authorized managing organ based on the general agreement

\(^{69}\) Privatization Law, art.11.
\(^{70}\) Privatization Law, art.14(2).
\(^{71}\) Method for property appraisal approved by CMU Resolution of 10.12.2003 №1891.
\(^{72}\) Privatization Law, art.19.
\(^{73}\) Privatization Law, art.18-4(2). See Standard list of information for different modes of sales to be mandatorily published in the official media of state privatization authorities approved by SPFU Decree of 23.04.2012 №562.
\(^{74}\) Privatization Law, art.29(3).
with SPFU and upon conclusion of a contract between the person and the authorized managing organ;
- SPFU approves the standard form of the general agreement;
- the authorized managing organ forms a list of candidates to the Supervisory Board of the company upon approval of SPFU;
- SPFU analyses activities of state representatives based on his/her report and a generalized report of the authorized managing organ which concluded the relevant agency contract.  

In addition, the authorized managing organ and the state representative shall annually submit to SPFU an annual report on financial and economic activities of the respective company alongside the explanatory note with a list of information of relevance to its business.  

At the same time, SPFU is not authorized to initiate or decide on prior dismissal of the state representative. Such a decision shall be taken by the authorized managing organ.  

The Proposal envisages the need to establish sufficient restrictions on SPFU’s activities with a view to eliminate the possibility for a conflict of interests at the level of SPFU caused by its management of shareholding in MGU. Such restrictions include:

- restrictions on the transfer to SPFU’s sphere of management of state enterprises or shares in companies engaged in production and/or supply of natural gas and/or electricity except where such objects are transferred to SPFU for purposes of privatization;
- restrictions regarding SPFU’s approval of candidates of authorized representatives for participation in General Shareholders’ Meetings and managing bodies of gas and electricity companies;
- conditions of use of information obtained by SPFU in the course of performance of its duties related to control of state property management in order to prevent its unlawful use;
- additional measures regarding monitoring and control of the privatization process in the fuel and energy complex.

Such restrictions may be established in secondary acts of CMU and/or SPFU.

**iii. Whether there is a third person who controls decision-making within SPFU and MECI/MEDT as regards the TSO**

Justification of the Proposal requires that there is no control over SPFU and MEDT/MECI on the part of any third person. Theoretically, this can be CMU or the Prime-minister of Ukraine.

**a) CMU**

According to Article 113 of the Constitution of Ukraine, CMU is the highest body within the system of executive authorities. The CMU is composed of the Prime-minister of Ukraine, First vice prime minister, vice prime ministers and ministers of Ukraine. Ministers shall be appointed by VRU upon submission of the Prime-minister of Ukraine (except for the Minister of Foreign Affairs and the Minister of Defence to be appointed by VRU upon submission of the President of Ukraine). The first deputy minister, deputy ministers shall

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75 Regulation on the state representative authorized to manage respective state corporate rights in managing bodies of companies approved by CMU Resolution of 15.05.2000 №791, paras 1-2, 4, 9.
76 Regulation on the state representative authorized to manage respective state corporate rights in managing bodies of companies approved by CMU Resolution of 15.05.2000 №791, paras 1-2.
77 Regulation on the state representative authorized to manage respective state corporate rights in managing bodies of companies approved by CMU Resolution of 15.05.2000 №791, paras 1-2.
78 Constitution of Ukraine, art. 114.
79 Constitution of Ukraine, art. 114.
be appointed and dismissed by CMU upon submission of the Prime-minister of Ukraine according to the proposals of the Minister.\textsuperscript{80}

CMU exercises the executive power on the basis, within the powers and in the manner envisaged by the Constitution and laws of Ukraine.\textsuperscript{81} CMU is guided by the Constitution of Ukraine, laws of Ukraine as well as acts of the President of Ukraine and resolutions of VRU adopted in accordance with the Constitution and laws of Ukraine.\textsuperscript{82}

CMU exercises the executive power directly and through ministries, other central executive bodies. It directs, coordinates and controls activities of these bodies.\textsuperscript{83} Ministries and other central executive bodies are answerable to CMU, accountable to and controlled by it.\textsuperscript{84} CMU directs its activities towards fulfilment of the Constitution and laws of Ukraine, acts of the President of Ukraine, resolutions of VRU adopted in accordance with the Constitution and laws of Ukraine, CMU’s Program of Action approved by VRU.\textsuperscript{85} CMU performs continuous control of compliance with the Constitution of Ukraine and other legislative acts of Ukraine by executive bodies, takes measures to eliminate shortcomings in the work of these bodies.\textsuperscript{86}

CMU is a collegial body.\textsuperscript{87} According to the Constitution and laws of Ukraine CMU exercises its powers by way of taking decisions at its meetings by a majority vote of its members.\textsuperscript{88} If the draft decision is supported by one half of CMU members and the Prime-minister of Ukraine has voted for such a decision, the decision is deemed to be adopted.\textsuperscript{89}

CMU has the power to fully or partially repeal acts of ministries\textsuperscript{90} and of SPFU.\textsuperscript{91} According to the CMU Rules of Procedure, CMU fully or partially repeals acts of central executive bodies in the event of their non-compliance with the Constitution and laws of Ukraine, acts of the President of Ukraine and acts of CMU by adopting respective decisions. The draft of a decision shall be prepared by the Ministry of Justice of Ukraine upon instruction from the Prime-minister of Ukraine.\textsuperscript{92}

Despite the existence of these powers, CMU is not a legal entity under the Ukrainian legislation.\textsuperscript{93} This means that CMU may not be considered as a person that exercises control over SPFU and MEDT/MECI in the meaning of the Law. In addition, according to the Commission’s case law powers to repeal acts of MEDT/MECI and SPFU should not provide grounds to consider CMU as a body that controls the two state bodies.\textsuperscript{94} This conclusion is confirmed by the special decision-making procedure within CMU where decisions are taken collectively and by voting, which eliminates the possibility to fully control the two bodies.

\textit{b) Prime-minister of Ukraine}

\textsuperscript{80} CMU Law, art. 44(1)(4).
\textsuperscript{81} CMU Law, art. 3(2).
\textsuperscript{82} CMU Law, art. 4(1).
\textsuperscript{83} CMU Law, art. 1(2).
\textsuperscript{84} CMU Law, art. 21(2).
\textsuperscript{85} CMU Law, art. 41(1).
\textsuperscript{86} CMU Law, art. 19(2).
\textsuperscript{87} CMU Law, art. 3(3).
\textsuperscript{88} CMU Law, art. 41(2).
\textsuperscript{89} CMU Law, art. 51(1).
\textsuperscript{90} CEB Law, art.15(9).
\textsuperscript{91} SPFU Law, art. 9(7).
\textsuperscript{92} CMU Rules of Procedure, para 84.
\textsuperscript{93} Under Article 47(10) of the CMU Law, the CMU Secretariat is a legal person. Its status is prescribed in Article 47 of the CMU Law and does not include powers to issue orders or instructions binding on state authorities.
The powers of the Prime-minister of Ukraine are stipulated in Article 42 of the CMU Law. The Prime-minister of Ukraine shall:

- manage CMU’s activity, direct CMU towards implementation of domestic and foreign policy of the state, of CMU’s Program of Action and other functions of CMU;
- direct, coordinate and control activities of CMU members, heads of other central executive bodies, for that purpose issue instructions binding on the said bodies and officials.\(^{95}\)

The Prime-minister of Ukraine may exercise other powers provided by the Constitution and laws of Ukraine.\(^{96}\) The Prime-minister of Ukraine raises issues related to central executive bodies with the special status, in particular SPFU.\(^{97}\)

It should be noted that in relation to the Prime-minister restrictions on interference with SPFU’s activities apply as stipulated by the SPFU Law.\(^{98}\) Thus, instructions of the Prime-minister of Ukraine may be issued with the aim to guide, coordinate and control the activities of SPFU but without interference into SPFU’s activities related to management of corporate rights of MGU. SPFU may refuse to execute instructions given by executive bodies if they interfere with its activities unless otherwise is provided by law.

To eliminate issues with practical application of the independence requirements of SPFU, it should suffice to amend the secondary legislation, namely the CMU Rules of Procedure, and to interpret powers of the Prime-minister of Ukraine to give instructions to SPFU in respect of SPFU’s shareholding in MGU.\(^{99}\)

**iv. Legislative authorities in respect of MGU deriving from its special legal status**

According to the legislation of Ukraine, state authorities possess certain competences in respect of MGU by virtue of the fact that its shareholder is the state. Pursuant to the case law of the Commission not all competences shall be deemed as rights in the meaning of Directive 2009/73/EC and thus of the Law. In its opinion on certification of TenneT TSO B.V.\(^{100}\) the Commission noted that the availability of powers as regards the Dutch electricity TSO (e.g., powers to approve individual bylaws and investment decisions) with the Ministry of Economic Affairs of the Netherlands, which is not the shareholder of such a TSO and which at the same time controls producers/suppliers of natural gas, shall not impede certification of the TSO according to the OU model provided that such powers did not create an incentive or a possibility for the Ministry of Economic Affairs to influence the decision-making of the TSO with a view to grant benefits to producers or suppliers of natural gas in which this Ministry holds shareholding and to the detriment of other network users. In particular, the powers which correspond to the general competence of the ministry as regards carrying out of the state policy in a specific area as well as those which are not directly related to shareholdings in producers or suppliers of natural gas are concerned. However, the Commission highlighted that the power to approve appointments to the Supervisory Board shall be treated as a violation of the EU legislation.

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95 CMU Law, art. 42(1)-(2).
96 CMU Law, art. 42(2).
97 CEB Law, art. 24(3).
98 SPFU Law, art. 13(1).
99 It is possible to amend para 9(2) of the CMU Rules of Procedure, according to which "the Prime-minister while managing the work of CMU gives instructions binding on CMU members and heads of other central executive bodies except on those whose activities are directed and coordinated by CMU through the relevant ministers, to the Prime-minister of the Autonomous Republic of Crimea and heads of local state administrations", by adding that this provision does not cover instructions to SPFU which interfere with the business activity of MGU except in cases provided by law.
The need to amend certain legislative acts with a view to eliminate conflicting competences of CMU and other state authorities as regards MGU or SPFU as MGU’s shareholder shall be assessed based on the foregoing principles.

Main competences of state authorities other than SPFU which may intrude with TSO’s activities are presented in Annex 6.

a) Powers of CMU as regards objects of state property

Under the law, CMU possesses a series of competences in respect of state property objects (namely state corporate rights). Annex 4 presents the list of such competences, the mode of their realization in secondary acts as well as proposals regarding relevant legislative amendments.

b) Powers of MEDT as regards objects of state property

Certain powers regarding MGU and SPFU as MGU’s shareholder belong to MEDT. In this connection, MEDT shall:

- prepare and submit the draft CMU decision related to the transfer of powers of management of state corporate rights to authorized managing organs and business entities;¹⁰¹
- determine criteria of efficiency of management of state corporate rights,¹⁰²
- perform control over performance of functions of management of state property objects by managing subjects by way of single monitoring of efficiency of state property management;¹⁰³
- carry out analysis of efficiency of performance of functions of management of state corporate rights, verify performance of agency contracts for management and prepare proposals regarding improvement of management;¹⁰⁴
- perform methodological and, within its competence, legislative support of management of state property, including on stock-taking and accounting of state property objects; of assessment of efficiency of state property management; of management of state corporate rights, namely ensuring of representation of the state in management bodies of business entities with the state shareholding; of single monitoring of efficiency of management of state property objects, including of state corporate rights; of protection of proprietary rights of the state.¹⁰⁵

In addition, SPFU shall submit to MEDT per the form approved by MEDT:

- information on financial and business activity of each state enterprise, institution and organization within its sphere of management as well as of companies share in which are managed by SPFU (namely, MGU);
- information on contracts concluded with directors of business entities of the state sector of economy (namely, MGU);¹⁰⁶ and
- aggregated information on indicators of financial plans of enterprises within SPFU’s sphere of management by 01 September of each year preceding the reporting year, and on their performance – by 01 April of the year following the reporting one.¹⁰⁷

Notwithstanding that MEDT is the shareholder of NJSC Naftogaz of Ukraine, the aforementioned powers should not create a conflict of interest at the level of MEDT since such powers derive from MEDT’s general competence to develop and implement the state

¹⁰¹ State Property Management Law, art.5(2)(14).
¹⁰² State Property Management Law, art.5-2(1)(2).
¹⁰³ State Property Management Law, art.5-2(1)(7).
¹⁰⁴ State Property Management Law, art.16(4).
¹⁰⁵ State Property Management Law, art.16(6).
¹⁰⁶ State Property Management Law, art.7(1)(1)(к) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
¹⁰⁷ State Property Management Law, art.16(6).
policy related to management of state property and they should not affect the performance of TSO’s functions.

c) Powers of state authorities in respect of business entities of the state sector of economy

According to the current legislation of Ukraine, MGU shall qualify as the business entity of the state sector of economy. By virtue of this legal status, MGU shall be opposable with the following rules enshrined in the primary legislation (except for those powers of CMU and MEDT mentioned earlier):

- the procedure for utilizing funds allocated by the State Budget of Ukraine for financing of buy-back of shares of secondary emission of business entities with state corporate rights as well as of restructuring, pre-trial rehabilitation and other measures related to the functioning of objects of the state sector of economy approved by CMU shall apply to MGU;
- the procedure for performance of annual state financial audit of business entities of the state sector of economy approved by CMU shall apply to MGU;
- the State Audit Service shall per the procedure established by CMU carry out state financial audit of MGU directed at avoidance of financial violations, ensuring effective use of budget funds and of state property.

According to the legislation, state financial audit consists of verification and analysis of activities, actual state of affairs with lawfulness and effectiveness of use of state or municipal funds and property, other assets of the state, correctness of statutory accounting and reliability of financial statements, functioning of internal control systems of business entities of the state sector of economy as well as of other business entities which receive (or received in the reporting period) funds from budgets of all levels and state funds or use (used in the reporting period) state or municipal property. While state financial audit shall be carried out on an annual basis, certain business entities of the state sector of economy (including NJSC Naftogaz of Ukraine, other key enterprises of the fuel and energy complex) are subject to a more stringent treatment in terms of financial controls, which is governed by a separate CMU decision.

The afore-mentioned powers of CMU and other state authorities in respect of MGU as a business entity of the state sector of economy should not create a conflict of interest since such powers derive from the general competence of such bodies, namely in respect of control of effective utilization of MGU’s funds, and should not affect the performance of TSO’s functions. However, if necessary, relevant secondary legislation may be amended to limit intrusions into the business activities of the TSO.

d) Powers of state authorities in respect of objects of state property of strategic significance for the economy and state defence

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108 Article 22(2) of the Commercial Code of Ukraine defines business entities of the state sector of economy as those which act exclusively based on state property or those with the state shareholder exceeding 50% or where the state’s share represents the amount which ensures the ultimate decision-making right in respect of these entities’ business activities to the state.
109 State Property Management Law, art.5(2)(18)(6).
110 State Property Management Law, art.5(2)(18)(k).
111 State Property Management Law, art.16(7).
112 Procedure for carrying out state financial audit of business entities by the State Financial Inspectorate and its territorial sub-divisions approved by CMU Resolution of 25.03.2006 №361, para 1.
113 Procedure for carrying out state financial audit of separate transactions by the State Financial Inspectorate and its territorial sub-divisions approved by CMU Resolution of 25.06.2014 №214.
It is highly likely that MGU be included in the list of state property objects of strategic significance to the economy and defence of the state.\textsuperscript{114} In this case, MGU shall be opposable with the following rules enshrined in the primary legislation (except for those powers of CMU and MEDT mentioned earlier):

- CMU shall approve conditions of privatization and restructuring of MGU;\textsuperscript{115}
- SPFU shall elaborate of conditions of restructuring and rehabilitation of MGU and seek approval of CMU;\textsuperscript{116}
- voting on additional emission of shares at the General Shareholders’ Meeting of MGU shall be made based on the CMU decision.\textsuperscript{117}

The afore-mentioned powers of CMU in respect of MGU as a state property object of strategic significance to the economy and defence of the state should not create a conflict of interest since such powers derive from CMU’s general competence and should not affect the performance of TSO’s functions considering that CMU acts as a collegial decision-making body.

3) Compliance with Unbundling requirement №3

Pursuant to subpara 3 of para 3 of Article 23 of the Law, “an individual or a legal person shall not simultaneously … appoint at least one official of the gas transmission system operator, and directly or indirectly exercise sole or joint control over at least one business entity (including a foreign one) carrying out production and/or supply of natural gas or exercise any right over at least one business entity carrying out production and/or supply of natural gas”.

The Proposal envisages that corporate governance of the TSO shall be based on the OECD Principles of Corporate Governance.

i. Which persons make nominations in MGU?

The corporate governance structure of MGU is presented in Annex 5.

a) General Shareholder’s Meetings (hereinafter – “GSM”)

Management of corporate rights of MGU will be performed by SPFU directly without holding of GSM. GSM decisions within its competence will be formalised in the form of SPFU decrees. Such decisions will have the status of GSM minutes.

The MGU Articles of Association will stipulate that GSM decisions shall be taken without any approvals from other state executive bodies except in cases provided by law. This clause will reflect Article 13 of the SPFU Law. A separate CMU act will provide that no intrusion into and obstruction of business activities of MGU shall be allowed on the part of state authorities, political parties and civil organizations, their officials and employees.

SPFU will exercise powers of GSM per the procedure prescribed in the MGU Articles of Association as well as in the legislation governing joint-stock companies.

The MGU Articles of Association shall refer only those issues within the exclusive competence of GSM under the laws of Ukraine to the competence of GSM. This exclusive competence includes:

- determination of main directions of activities of the company;
- amendments to the company’s articles of association;
- adoption of decisions on annulment of bought-back shares;

\textsuperscript{114} List of state property objects of strategic significance to the economy and defence of the state is approved by CMU upon submission from MEDT. See State Property Management Law, art.5(2)(24), 5-2(1)(12).
\textsuperscript{115} State Property Management Law, art.5(2)(23).
\textsuperscript{116} State Property Management Law, art.7(1)(1)(e).
\textsuperscript{117} State Property Management Law, art.11(16).
- amendments of the company’s type;
- adoption of decisions on placement of shares;
- adoption of decisions on increase/decrease of the company’s share capital;
- adoption of decisions on dilution or consolidation of shares;
- approval of regulations of GSM, the Supervisory Board, management body and of a revision commission (revision officer) of the company as well as amendments thereto;
- approval of other bylaws if provided by the company’s articles of association;
- approval of the company’s annual report;
- distribution of profits and losses of the company taking into account requirements of the law;
- adoption of decisions on the buy-back of shares except in cases of mandatory buy-back;
- adoption of decisions on the form of shares;
- approval of the amount of annual dividends taking into account requirements of the law;
- adoption of decisions regarding GSM’s agenda;
- appointment of members of the Supervisory Board, approval of civil law and employment contracts to be concluded with them, establishment of their remuneration, appointment of the person in charge of signing of contracts with the Supervisory Board;
- adoption of decisions on termination of the term of office of members of the Supervisory Board except in cases specified in the Law of Ukraine “On Joint-Stock Companies”;
- appointment of members of the revision commission (revision officer), adoption of a decision on prior termination of their terms of office;
- approval of conclusions of the revisions commission (revision officer);
- appointment of the counting commission, adoption of decisions on termination of its terms of office;
- adoption of decisions on substantial transactions if the market value of property, works and services which form the subject-matter of the transaction exceeds 25% of assets per the latest annual financial statements of the company;
- adoption of decisions on spinoff and termination of the company (with certain exceptions), on liquidation of the company, appointment of the liquidation commission, approval of the procedure and timeline of liquidation, procedure for allocation among shareholders of property left following settlements with creditors, approval of the liquidation balance sheet;
- adoption of decisions following consideration of the report of the Supervisory Board, of the management body, of the revision commission (revision officer);
- approval of principles (code) of corporate governance of the company;
- appointment of the commission on termination of the company.\textsuperscript{118}

It should be noted that GSM’s competence extends to all issues related to the activity of the company but shall be limited by those stated in the articles of association. At the same time, there are no legislative limitations on GSM’s competence to amend the articles of association of the company 100% of shares of which belong to the state.

\textit{b) Independent Nomination Committee (hereinafter – “INC“)}

To ensure selection of qualified persons to the Supervisory Board, namely of Independent Directors, the INC will be created.

The INC will consist of four members: one representing the shareholder, one representing the staff of the TSO, and two serving as independent members who will comply with

\textsuperscript{118} Law of Ukraine “On Joint-Stock Companies”, art.33(2).
independence criteria opposable to Independent Directors.

The INC shall be appointed by GSM. The INC Regulation shall be approved by GSM. GSM may approve instructions for INC as regards criteria for selection of candidates to the Supervisory Board. The MGU’s shareholder and/or other state authorities will have no right to intrude with the decision-making of INC members.

INC will:

- provide recommendations to GSM regarding candidate members to the Supervisory Board and the amount of their remuneration;
- prepare opinions on compliance of candidate Independent Directors with independence criteria;
- perform regular monitoring of compliance of Independent Directors with the independence criteria;
- assess activities of Independent Directors;
- perform other functions as determined by the INC Regulation.

c) Supervisory Board

GSM will appoint members of MGU’s Supervisory Board upon nominations from INC.

MGU’s Supervisory Board will consist of seven members. The majority of them will be Independent Directors complying with the independence criteria.\(^{119}\)

Members of MGU’s Supervisory Board will be appointed for the term determined by GSM unless otherwise provided by law.

MGU’s Supervisory Board shall be the body to protect rights of MGU’s shareholder and within its competence determined by law and the Articles of Association to control and govern activities of the Management Board. The following legislative requirements are opposable to MGU’s Supervisory Board:

- the Supervisory Board shall be established, liquidated, and organised per the procedure determined by CMU to be reviewed at least once per five years to account of the laws of Ukraine;\(^ {120}\)
- candidates proposed to SPFU for appointment as members of MGU’s Supervisory Board shall be selected per the procedure determined by CMU, and members of the Supervisory Board shall be appointed in accordance with the Law of Ukraine “On Joint-Stock Companies”, other laws governing activities of such companies;\(^ {121}\)
- Independent Directors of MGU shall meet the independence requirements listed in the law;\(^ {122}\)
- requirements to Independent Directors shall be approved by CMU.\(^ {123}\)

A member of MGU’s Supervisory Board may not be the founder, shareholder, director and/or member of the Supervisory Board of the enterprise or another business entity which carries out activities on the same or adjacent markets with MGU.\(^ {124}\)

\(^{119}\) This will correspond to the State Property Management Law, art.11-2(2) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).

\(^{120}\) State Property Management Law, art.11-2(1) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).

\(^{121}\) State Property Management Law, art.11-2(2) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).

\(^{122}\) State Property Management Law, art.11'(1) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).

\(^{123}\) State Property Management Law, art.11'(2) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).

\(^{124}\) State Property Management Law, art.11'(3) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
According to the law, a member of the Supervisory Board shall take decision on issues of the agenda based on its own judgement except in cases provided in the State Property Management Law.\textsuperscript{125} MGU’s Supervisory Board member will act in the interests of MGU rather than of a person or persons which nominated, approved or appointed them.

The exclusive competence of the Supervisory Board as prescribed by the law covers:

- approval of regulations governing issues of the company’s activities within its competence;
- preparation of GSM’s agenda, adoption of decisions on the date of their holding and on inclusion of proposals to the agenda except in cases of extra-ordinary GSM;
- adoption of decisions on holding of scheduled and extra-ordinary GSM according to the articles of association and in cases provided in the Law of Ukraine “On Joint-Stock Companies”;
- adoption of decisions on alienation of previously bought-back shares;
- adoption of decision on placement of securities other than shares;
- adoption of decisions on the buy-back of previously placed securities other than shares;
- approval of the market value of property in cases stipulated in the Law of Ukraine “On Joint-Stock Companies”;
- appointment and termination of the terms of office of the chairman and members of the management;
- approval of conditions of contracts to be concluded with members of the management, determination of their remuneration;
- adoption of decisions on suspension of the chairman or a member of the management and appointment of the person to temporarily perform powers of the chairman of the management;
- appointment and termination of the terms of office of the chairman and members of other bodies of the company;
- appointment of the registration commission except in cases specified in the Law of Ukraine “On Joint-Stock Companies”;
- appointment of the company’s auditor and determination of conditions of the contract to be concluded with it, determination of its remuneration;
- determination of the date of compilation of the list of persons eligible to receive dividends, of the procedure and timeline for payment of dividends within the maximum time period determined by the law;
- determination of the date of compilation of the list of shareholders to be notified of GSM according to the law and which are eligible to participate in GSM under the law;
- resolution of issues regarding participation in industrial and financial groups as well as in other associations, on establishment of other legal persons;
- resolution of issues within the competence of the Supervisory Board as provided in the law in case of termination as well as of merger, consolidation, separation, spinoff or transformation of the company;
- adoption of decisions on substantial transactions if the market value of property or services forming the subject-matter of the transaction constitutes 10 to 25 % of the value of assets per the latest annual financial statements of the company;
- determination of the likelihood of the company being recognized as insolvent as a result of assumption of an obligation or its performance, including as a result of payment of dividends and share buy-back;

\textsuperscript{125} State Property Management Law, art.11(3) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
- adoption of decisions on appointment of the appraiser of property of the company and approval of conditions of the contract to be concluded with it, determination of its remuneration;
- adoption of decisions on appointment (change) of the company’s registrar of holders of registered securities or of the depository of securities and approval of conditions of the contract to be concluded with it, determination of its remuneration;
- forwarding of proposals to shareholders on purchase of their shares by a person (jointly acting persons) which purchased the controlling stock of shares in accordance with the law;
- resolution of other issues within the exclusive competence of the Supervisory Board as determined by MGU’s Articles of Association.\(^{126}\)

MGU’s Articles of Association shall refer to the competence of the Supervisory Board the following:
- approval of the strategy and mission of MGU;
- approval of MGU’s business plan, including of the financial plan (budget) and of the investment programme;
- establishment of committees of the Supervisory Board, approval of their regulations, approval of the scope of issues to be transferred for their analysis and preparation;
- appointment and dismissal of directors of bodies and units of MGU per different directions controlled and accountable to the Supervisory Board.

Within MGU’s Supervisory Board the following permanent committees shall be established: the Nomination and Remuneration Committee, the Ethics Committee, the Audit Committee.

d) Management Board

Management of the current activities of MGU will be made by the Management Board which is a collective executive body of MGU. The Management Board shall act on the basis of the regulation to be approved by GSM. The Management Board shall be accountable to GSM and to the Supervisory Board. The Management Board, including its Chairman, will be elected by the Supervisory Board based on the submission from the Nomination and Remuneration Committee of the Supervisory Board.

The competence of the Management Board will include resolution of all issues related to the management of the current activities of MGU except for issues which belong to the exclusive competence of GSM, the Supervisory Board or to the competence of other bodies and units as provided in MGU’s Articles of Association.

Under the law members of MGU’s Management Board shall be prohibited from simultaneously serving on the Management Board and performing any commercial or other paid activity except for receiving of copyright remuneration, carrying out of scientific and teaching functions, and/or in case of approval of the relevant activity by the Supervisory Board.\(^{127}\)

\[ \text{ii. Whether these persons exercise control or rights over producers/suppliers of natural gas/electricity} \]

All appointments of MGU’s officials will be made by SPFU single-handedly or by collegial bodies established under MGU’s Articles of Association and shall not require approvals from other executive authorities.

\(^{126}\) Law of Ukraine “On Joint-Stock Companies”, art.52(2).
\(^{127}\) State Property Management Law, art.11\(^{(4)}\) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
As regards the absence of control or rights over producers/suppliers of natural gas/electricity with SPFU, please see above.

4) Compliance with Unbundling requirement №4

Pursuant to subpara 4 of para 3 of Article 23 of the Law, “an individual or a legal person shall not simultaneously … be an official of the gas transmission system operator and of at least one business entity (including a foreign one) carrying out production and/or supply of natural gas.”

The Proposal does not envisage the possibility for simultaneous holding of offices in MGU and in producers/suppliers of natural gas/electricity to be fixed in MGU’s Articles of Association and/or other documents. The relevant prohibition will also be provided in civil law and employment contracts to be concluded with members of the Supervisory Board and the Management Board of MGU.

V. Justification of the Proposal: requirement as to the ownership of the gas transmission system

1. The requirement as to the ownership of the gas transmission system by the TSO is stipulated in subpara a) of para 1 of Article 9 of Directive 2009/73/EC as well as in para 2 of Article 23 of the Law.

2. Under the law main pipelines shall mean a technological complex functioning as a single system which consists of a separate pipeline with all objects and constructions related thereto by means of a single technological process and several pipelines which perform transit, inter-state, inter-regional supplies of products of transport to consumers as well as other pipelines designed and constructed under state building requirements as regards main pipelines.¹²⁸

Main pipeline transport shall have strategic significance for the economy and defence and shall be state property.¹²⁹

Main gas pipelines and main pipeline transport servicing the needs of the state as a whole shall not be subject to privatization.¹³⁰ Under the law privatization shall mean paid alienation of state property, including of land plots belonging to the state on which a privatization object is located, in favor of individuals and legal persons qualifying as buyers under the Privatization Law with a view to enhance social and economic efficiency of production and attract funds for structure overhaul of the national economy.¹³¹ Alienation of fixed assets of state enterprises performing activities of transmission via main pipelines and storage in underground gas storages as well as of enterprises, institutions, and organizations established as a result of their reorganization, transfer of such assets from one balance sheet to another, into concession, lease, leasing, under lien, into management, injection into the share capital of other legal persons, performance of other deeds shall be prohibited with the exception of cases where as a result of such a deed the transfer of fixed assets of such enterprises to a budget entity, state enterprise or a joint-stock company 100% of shares of which belong to the state takes place.¹³²

Notwithstanding that, another law stipulates that real estate of state property object not subject to privatization may not be alienated, confiscated, transferred to the share capital of business entities, and in respect of such property actions may not be taken which lead to their alienation.¹³³ Importantly, the status of property not subject to privatization

¹³⁰ Law of Ukraine of 04.03.1992 №2163-XII “On Privatization of State Property”, art.5(2).
¹³¹ Privatization Law, art.1.
¹³³ State Property Management Law, art.11(9).
envisages that such property may not be pledged.\textsuperscript{134} In addition, foreclosure of property of companies with the state shareholding of at least 25% is prohibited "\textit{until the legislative improvement of the mechanism for forced sale of property}".\textsuperscript{135}

Main pipelines of Ukraine which constitute state property may not be leased except where they are transferred on a paid terminable basis without the right to alienate them for performance of functions of the TSO aimed at and for purposes of compliance with Ukraine’s undertakings from membership in the Energy Community.\textsuperscript{136}

3. Historically facilities of the gas transmission system of Ukraine (main gas pipelines) were accounted for on the balance sheet of the State Enterprise Production Unity Ukrgazprom. In the process of corporatization this state enterprise was transformed into JSC Ukrgazprom (hereinafter – “Ukrgazprom”). Pursuant to a decision of the State Committee on the Oil, Gas and Petroleum Product Industry of Ukraine main gas pipelines were retained on the balance sheet of Ukrgazprom as the state property not subject to privatization.

By CMU Resolution of 25.05.1998 №747 “On Establishment of NJSC Naftogaz of Ukraine” the list of property used to ensure transmission, storage and distribution of oil, petroleum products and natural gas which under the legislation shall not be subject of privatization and shall be transferred for Naftogaz’ use was approved in annex 3 to that resolution. This property was transferred to Naftogaz under the act of property transfer of 28.08.1998 signed with the State Committee on the Oil, Gas and Petroleum Product Industry of Ukraine and approved by SPFU.

Pursuant to CMU Resolution of 24.07.1998 №1173 “On separation of functions of production, transmission, storage, and sales of natural gas” functions of production, transmission, storage and sales of natural gas were separated by way of establishment of subsidiaries of Naftogaz. Thus, functions of transmission and storage of natural gas were transferred to Subsidiary Company Ukrtransgaz, which was established on the basis of gas transmission enterprises and structural subdivisions of Ukrgazprom.

By a joint decree of the State Committee of the Oil, Gas, Petroleum Product Industry of Ukraine and Naftogaz of 06.11.1998 №68/234 Ukrgazprom was terminated in connection with its reorganization by way of spinoff and merger to subsidiaries of Naftogaz determined as successors of all property rights and obligations of Ukrgazprom and of its reorganized enterprises. During the said reorganization of Ukrgazprom, main gas pipelines which were accounted on the balance sheet of Ukrgazprom were transferred to the balance sheet of Subsidiary Company Ukrtransgaz of NJSC Naftogaz of Ukraine.

At the moment main gas pipelines are accounted for on the balance sheet of PJSC Ukrtransgaz as state property not subject to privatization. Agreement №76 of 04.02.1999 on the use of state property not subject to privatization was concluded between SPFU and NJSC Naftogaz of Ukraine according to which NJSC Naftogaz of Ukraine assumed obligations regarding operational management and use of state property not subject to privatization and which was not contributed to the share capital of enterprises forming part of NJSC Naftogaz of Ukraine. Based on the said Agreement a mirror Agreement of 17.06.1999 №19/275 was concluded on the use of state property not subject to privatization between NJSC Naftogaz of Ukraine and Subsidiary Company Ukrtransgaz whereby functions of management and use of this property were transferred to Subsidiary Company Ukrtransgaz (of which PJSC Ukrtransgaz is a successor).

\textsuperscript{134} Law of Ukraine of 02.10.1992 №2654-XII “On Pledge”, art.4.
4. Under CMU Resolution of 14.04.2004 №467 “On Approval of the Statute of the Unified Register of State Property Objects” and of 30.11.2005 №1121 “On Approval of the Methodology for Performing Stock-Taking of State Property Objects” MECI performs stock-taking of state property objects used in natural gas transmission. In pursuance of the said resolutions and MECI Decree of 13.02.2012 №92 “On Stock-Taking of State Property Objects and Provisions of Information to the Unified Register of State Property Objects” MECI performs stock-taking of state property objects used in natural gas transmission. In pursuance of the said resolutions and MECI Decree of 13.02.2012 №92 “On Stock-Taking of State Property Objects and Provisions of Information to the Unified Register of State Property Objects” business entities on the balance sheets of which state property is accounted for which is managed through MECI shall annually and quarterly report to MECI. This information shall be inserted into the automatized system “Legal persons” maintained as part of the Unified Register of State Property Objects managed by SPFU.

5. The Proposal envisages that the gas transmission system shall be transferred to MGU as a contribution to its share capital.

According to the case law of the Commission, the requirement as to ownership of the gas transmission system shall be deemed as fulfilled if the person exercises rights of possession, use and disposal of the gas transmission system even though there are certain limitations on application of some of these property titles. In its opinion on certification of REN Rede Elétrica Nacional S.A. and REN Gasodutos S.A.137 the Commission states that rights of the concessionaire shall be deemed as equal to the rights of the owner, and therefore management of the gas transmission system based on a concession shall be sufficient for certification of the gas transmission system operator according to the OU unbundling model. In its opinion on certification of Companiei Naționale de Transport al Energiei Electrice “Transelectrica” S.A. the Commission invited the Romanian energy regulator to assess compliance of concession with the ownership requirement “taking into account, in particular, the ability of the concessionaire to use the assets covered by the concession agreement as a guarantee in acquiring financing on the capital markets and the right to compensation for investments made by the TSO into the said assets in the event of a termination of the concession agreement”.138

In view of the above, compliance with the ownership requirement as interpreted by the Commission should be ensured through a series of amendments into the Ukrainian laws, namely:

- amendments to the State Property Management Law as necessary to inject the gas transmission system into the share capital of the TSO;139

Such politically sensitive amendments would only be possible if they are directed at operationalization of the TSO which is a new company free from historical risks. Currently, claims of third parties (including NJSC Naftogaz of Ukraine) to PJSC Ukrtransgaz amount to circa 19-20 bcm of natural gas.

139 Despite that it is often considered that para 9 of Article 11 of the State Property Management Law forbids injections of the gas transmission system into the share capital of a company with the 100% state shareholding, this interpretation appears to be rather conservative and may be refuted based on a reasoned legal opinion. In particular, Article 7 of the Law of Ukraine “On the Pipeline Transport” specifically allows such a transfer. It should also be mentioned that the said provision of Article 7 of the Law of Ukraine “On the Pipeline Transport” entered into force later (13.04.2012) than the above-mentioned provision of the State Property Management Law (13.03.2012).
Injection of the gas transmission system into the share capital of the TSO appears to be the only viable option to avoid any future controversies over the scope of rights enjoyed by the TSO in respect of the gas transmission system. To ensure that the right to dispose of assets of the gas transmission system is not compromised, relevant clauses can be included in MGU's Articles of Association.

VI. Justification of the Proposal: availability of all necessary resources to carry out the TSO functions

The Proposal envisages that MGU shall possess all human, technical, financial and other necessary resources to perform functions and obligations of the gas transmission system operators under the Law. In order to enhance efficiency of the TSO organizational structure of MGU shall be developed based on the best practice of similar TSOs of the EU Member States.
B. TRANSITION TO THE TARGET TSO UNBUNDLING MODEL

<table>
<thead>
<tr>
<th>№</th>
<th>Measures</th>
<th>Responsible person</th>
<th>Timeframe</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Adoption of the decision on establishment of MGU as a JSC(^{141}) the sole founder and shareholder of which shall be NJSC Naftogaz of Ukraine by the Supervisory Board of NJSC Naftogaz of Ukraine(^{142})</td>
<td>NJSC Naftogaz of Ukraine</td>
<td>March – April 2016</td>
</tr>
<tr>
<td>2.</td>
<td>Measures envisaged in the Law of Ukraine “On Joint-Stock Companies” and the Regulation on the procedure for registration of share issue upon establishment of joint-stock companies approved by the National Securities and Stock Market Commission (hereinafter – <strong>NSSMC</strong>) of 27.05.2014 №692 as regards establishment of MGU as a JSC:</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2.1. registration of the share issue with NSSMC;</td>
<td>NJSC Naftogaz of Ukraine NSSFMC</td>
<td>March – July 2016</td>
</tr>
<tr>
<td></td>
<td>2.2. closed (private) offering of shares among MGU founders;</td>
<td>NJSC Naftogaz of Ukraine</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2.3. payment of the full value of shares by NJSC Naftogaz of Ukraine;</td>
<td>NJSC Naftogaz of Ukraine</td>
<td></td>
</tr>
</tbody>
</table>

\(^{140}\) Implementation of the Preparatory stage shall require necessary approvals and/or performance of other procedures per the obligations of NJSC Naftogaz of Ukraine owed to International Financial Institutions and private creditors.

\(^{141}\) Under Article 24(1) of the Law of Ukraine “On Joint-Stock Companies” (per the wording effective as of 01.05.2016) a public JSC shall undergo the procedure for listing, and its shares shall remain in at least one stock exchange register in Ukraine. This requirement shall apply to all public JSCs as of 01.01.2018. At the same time, due to requirements of Article 5 of the Law of Ukraine “On Privatization of State Property” shares of MGU may not be included in the stock exchange register. If amendments are not made to the Law of Ukraine “On Joint-Stock Companies” excluding the TSO from the scope of application of the said requirement, then it is proposed that MGU be established in the form of a private JSC.

\(^{142}\) Under para 70(9) the Articles of Association of NJSC Naftogaz of Ukraine decisions on participation of PJSC Naftogaz of Ukraine in companies, associations, on establishment of legal entities shall be within the exclusive competence of the Supervisory Board. In the absence of the Supervisory Board of NJSC Naftogaz of Ukraine, the said decision shall be taken by the GSM the functions of which are single-handedly performed by MEDT.

In addition, to speed up the establishment of a new legal entity, it may be considered to establish MGU as an LLC with its subsequent reorganization into a JSC with a view to, inter alia, implement the corporate governance action plan.
<table>
<thead>
<tr>
<th>2.4. adoption of the decision on approval by the constituent assembly of MGU of results of the closed (private) offering of shares, adoption of MGU’s Articles of Association and its internal regulations, selection of officials, as well as adoption of other decisions required by the law and MGU’s Articles of Association;</th>
<th>NJSC Naftogaz of Ukraine</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.5. registration of MGU and its Articles of Association with the state registration authorities;</td>
<td>MGU</td>
</tr>
<tr>
<td>2.6. procurement of the certificate of state registration of share issue.</td>
<td>MGU NSSMC</td>
</tr>
<tr>
<td>3. Implementation of the Corporate Governance Action Plan for MGU</td>
<td>MGU NJSC Naftogaz of Ukraine EBRD (upon consent)</td>
</tr>
<tr>
<td></td>
<td>April – July 2016</td>
</tr>
<tr>
<td>4. Development of the target operational model for the future TSO by MGU using its own personnel or consultants engaged with donors’ funding, including setting-up of operational processes and purchase of necessary IT-systems</td>
<td>MGU NJSC Naftogaz of Ukraine European Commission (upon consent) Energy Community Secretariat (upon consent)</td>
</tr>
<tr>
<td></td>
<td>April – October 2016</td>
</tr>
<tr>
<td>5. Start of performance of certain functions (transactions) of the TSO by MGU based on contracts with PJSC Ukrtransgaz</td>
<td>MGU</td>
</tr>
<tr>
<td></td>
<td>November 2016</td>
</tr>
<tr>
<td>6. Certification of MGU (in particular determination by NCSREU of conditions for receipt of the final decision on certification)</td>
<td>NCSREU MGU Energy Community Secretariat</td>
</tr>
<tr>
<td></td>
<td>01.06.2016 (or any other date as determined by NCSREU and the Energy Community Secretariat)</td>
</tr>
</tbody>
</table>
After amendments to the Contract TKГУ of 19.01.2009 between NJSC Naftogaz of Ukraine and PJSC Gazprom are made in the manner acceptable to Ukraine –

<table>
<thead>
<tr>
<th>Stage 1 – Fulfilment of the TSO unbundling requirements</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1.</strong> Transfer of 100% of shares of MGU to SPFU</td>
</tr>
<tr>
<td><strong>2.</strong> Stock-taking of state property used in natural gas transmission and placed on the balance sheet of PJSC Ukrtransgaz and compilation of the list of property to be transferred to the sphere of management of SPFU and to the share capital of MGU.</td>
</tr>
</tbody>
</table>

either by mutual consent of the parties or by virtue of an arbitral award:

| 7. | Amendments to the Privatization Law, the State Property Management Law, Laws of Ukraine “On Pipeline Transport”, “On Pledge”, “On Imposition of Moratorium against Forced Sale of Property” to enable the transfer of the gas transmission system to the share capital of MGU and realization of its rights as the owner. | VRU | May 2017 or earlier |

8. Adoption of the CMU Resolution “On restructuring of NJSC Naftogaz of Ukraine with the view to separate the natural gas transmission activity according to the requirements of the Law of Ukraine “On the Natural Gas Market” by which, in particular, to:

- approve transfer of 100% of shares in MGU to SPFU;
- ensure stock-taking of state property used in natural gas transmission and placed on the balance sheet of PJSC Ukrtransgaz;
- designate SPFU as the body responsible for management state property used in natural gas transmission;
- determine that the share capital of MGU shall be created using the state property used in natural gas transmission (injection in exchange of shares or issue of additional shares);
- ensure appraisal of state property used in natural gas transmission and accounted for on the balance-shtee of PJSC Ukrtransgaz;
- transfer from SPFU to other bodies state corporate rights in companies engaged in extraction (production) and/or distribution of natural gas and/or electricity and in which SPFU has rights in the meaning of the Law of Ukraine “On the Natural Gas Market” (except those state corporate rights which are subject to privatization);
- introduce changes to CMU’s acts necessary for independent operation of MGU, in particular to remove CMU’s intervention in the mandate of managing bodies of MGU. | CMU | May 2017 or earlier |

<p>| SPFU |
| MECI |
| NJSC Naftogaz of Ukraine |
| MGU |</p>
<table>
<thead>
<tr>
<th></th>
<th>Event Description</th>
<th>Responsible Parties</th>
<th>Timeline</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.</td>
<td>Transfer of state property used in natural gas transmission and accounted for on</td>
<td>SPFU, MGU, NJSC Naftogaz of Ukraine, PJSC Ukrtransgaz</td>
<td>May – June</td>
</tr>
<tr>
<td></td>
<td>the balance-sheet of PJSC Ukrtransgaz to the sphere of management of SPFU.</td>
<td></td>
<td>2017</td>
</tr>
<tr>
<td>4.</td>
<td>Appraisal of state property used in natural gas transmission to be transferred to</td>
<td>SPFU, MGU, NJSC Naftogaz of Ukraine, PJSC Ukrtransgaz</td>
<td>June 2017</td>
</tr>
<tr>
<td></td>
<td>the share capital of MGU.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Creation of the share capital of MGU by way of exchange of property used in</td>
<td>SPFU, MGU, NJSC Naftogaz of Ukraine, PJSC Ukrtransgaz</td>
<td>June – September 2017</td>
</tr>
<tr>
<td></td>
<td>natural gas transmission for shares (issue of additional shares).</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Termination of the Agreements on the use of state property not subject to</td>
<td>SPFU, MGU, NJSC Naftogaz of Ukraine, PJSC Ukrtransgaz</td>
<td>June – July 2017</td>
</tr>
<tr>
<td></td>
<td>privatization of 04.02.1999 №76 and of 17.06.1999 №19/275</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7.</td>
<td>Transfer of state property used in natural gas transmission from the balance</td>
<td>SPFU, NJSC Naftogaz of Ukraine, MGU, PJSC Ukrtransgaz</td>
<td>June – July 2017</td>
</tr>
<tr>
<td></td>
<td>sheet of PJSC Ukrtransgaz to that of MGU</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8.</td>
<td>Reappointment of management bodies of MGU</td>
<td>SPFU,</td>
<td>May – July 2017</td>
</tr>
</tbody>
</table>
Relevant amendments are already provided in the draft Law of Ukraine “On introduction of amendments to certain laws of Ukraine regarding creation of conditions for the natural gas market” (Registration № 3325, 15.10.2015).

Draft Law of Ukraine “On introduction of amendments to certain laws of Ukraine regarding improvement of corporate governance of National Joint-Stock Company Naftogaz of Ukraine, the gas transmission system operator and legal persons of which they acts as shareholders” has been developed as part of the corporate governance reform of National Joint Stock Company Naftogaz of Ukraine, its adoption by the Parliament is expected during the second phase of corporate governance reform of National Joint Stock Company Naftogaz of Ukraine.

### Phase 2 – Enhancing independence and effectiveness of MGU

<table>
<thead>
<tr>
<th></th>
<th>Procurement of licenses, certifications and all other permit documentation for the lawful start of natural gas transmission activities</th>
</tr>
</thead>
<tbody>
<tr>
<td>9.</td>
<td>SPFU</td>
</tr>
<tr>
<td></td>
<td>MGU</td>
</tr>
<tr>
<td></td>
<td>November 2016 – December 2017</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th><strong>Phase 2 – Enhancing independence and effectiveness of MGU</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Adoption of amendments to Article 44 to Law of Ukraine of 12.07.2001 № 2665-III “On Oil and Gas”(^{143}) and to the MECI Regulation approved by Decree of the President of Ukraine of 06.04.2011 № 382/2011 according to which the MECI currently determines and approves the operator of the Unified national gas transmission system of Ukraine</td>
</tr>
<tr>
<td></td>
<td>VRU</td>
</tr>
<tr>
<td></td>
<td>March – May 2016</td>
</tr>
</tbody>
</table>

| 2. | Adoption of amendments to the Commercial Code of Ukraine, the State Property Management Law, Law of Ukraine “On Joint-Stock Companies” in order to allow MGU to operate independently and without interference of state authorities and to introduce corporate governance principles for MGU on the part of the state as an owner in accordance to the OECD Guidelines on Corporate Governance of State-Owned Enterprises\(^{144}\) |
|   | MEDT |
|   | CMU |
|   | VRU |
|   | April – August 2016 |

| 3. | Adoption of the law on foundations of political non-interference into commercial activities of state enterprises in the oil and gas sector\(^{145}\) |
|   | MEDT |
|   | CMU |
|   | VRU |
|   | April – August 2016 |

\(^{143}\) Relevant amendments are already provided in the draft Law of Ukraine “On introduction of amendments to certain laws of Ukraine regarding creation of conditions for the natural gas market” (Registration № 3325, 15.10.2015)

\(^{144}\) Draft Law of Ukraine “On introduction of amendments to certain laws of Ukraine regarding improvement of corporate governance of National Joint-Stock Company Naftogaz of Ukraine, the gas transmission system operator and legal persons of which they acts as shareholders” has been developed as part of the corporate governance reform of National Joint Stock Company Naftogaz of Ukraine, its adoption by the Parliament is expected during the second phase of corporate governance reform of National Joint Stock Company Naftogaz of Ukraine.

\(^{145}\) Draft Law of Ukraine “On introduction of amendments to certain laws of Ukraine regarding improvement of corporate governance of National Joint-Stock Company Naftogaz of Ukraine, the gas transmission system operator and legal persons of which they acts as shareholders” has been developed as part of the corporate governance reform of National Joint Stock Company Naftogaz of Ukraine, its adoption by the Parliament is expected during the second phase of corporate governance reform of National Joint Stock Company Naftogaz of Ukraine.
Annex 1
Current and target ownership structure of the TSO

Current structure

State

MEDT

100%

NJSC Naftogaz of Ukraine

100%

PJSC Ukrtransgaz

GTS

Target structure

State

MEDT

100%

NJSC Naftogaz of Ukraine

100%

PJSC Ukrtransgaz

PJSC MGU

GTS
Annex 2
Privatization procedure under the laws of Ukraine

**SPFU**

### Determination of privatization objects

The Law provides for a list of objects not subject to privatization. SPFU defines and publishes the list of objects to be privatized. Authorized managing organs have the right to perform pre-privatization preparation of state enterprises and enterprises established in the process of corporatization prior to their transfer to SPFU.

### Pre-privatization preparation

Authorized managing organs on an annual basis submit to SPFU their proposals re: objects to be included in the list of objects to be privatized.

### Decision on privatization

Privatization may be initiated by:
- **SPFU**
- Authorized managing organs
- Buyers

SPFU adopts decision on privatization except decisions on privatization of Group D objects and objects of the fuel and energy complex.

CMU adopts decision on privatization of facilities of Group G and those in the oil and gas complex.

The timeline for privatization should not exceed 2 years as of the adoption of the decision on privatization.

### Audit of financial statements of the object

Experts and auditors are engaged by SPFU to carry out appraisal or audit services.

Within one month from adoption of the decision on privatization SPFU approves members of the privatization commission to develop a privatization plan of the object within the timelines set by SPFU which may not exceed 2 months.

In cases specified in the legislation on privatization an environmental audit shall be conducted.

### Plan of privatization / placement of shares

The draft plan of privatization provides:
- timelines and modes of privatization;
- starting price of the privatization object (volume of the share capital);
- recommended methods of payment;
- sizes of share lots according to the sales scope;
- measures for preservation of unified technological production process, avoidance of destruction of single property complexes, cycles, technologies;
- procedure for property use not included in the share capital of companies.

The draft shall be accompanied by the act of appraisal of property of the object approved by SPFU or by the report of appraisal of the object together with the approved opinion on its value.

CMU approves plans as regards:
- Group D objects and those of the fuel and energy complex.
- other modes defined by other laws on specifics of privatization in certain sectors.

### Sale of the object

Modes of privatization include:
- Auction sale;
- Competitive bidding sale;
- Sale of shares at an auction, competitive sale, on a stock exchange;
- Competitive sale of a single property complex or of a controlling stake;
- Buy-back;
- Sale of shares on international stock markets, including as depository receipts;
- other modes defined by other laws on specifics of privatization in certain sectors.

---

**SPFU**

Required stages of privatization

Possible stages of privatization
## Annex 3

**Privatization objects managed by SPFU**

<table>
<thead>
<tr>
<th>№</th>
<th>Code of the Unified State Register</th>
<th>Company name</th>
<th>State’s share in the share capital (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>30083966</td>
<td>PJSC Mykolayivska Cogeneration Plant</td>
<td>100</td>
</tr>
<tr>
<td>2.</td>
<td>00130820</td>
<td>PJSC Dniprodzerzhynska Cogeneration Plant</td>
<td>99,9277</td>
</tr>
<tr>
<td>3.</td>
<td>00131771</td>
<td>PJSC Khersonska Cogeneration Plant</td>
<td>99,8328</td>
</tr>
<tr>
<td>4.</td>
<td>05471158</td>
<td>PJSC Odeska Cogeneration Plant</td>
<td>99,9895</td>
</tr>
<tr>
<td>5.</td>
<td>22927045</td>
<td>PJSC Tsentrenergo</td>
<td>78,29</td>
</tr>
<tr>
<td>6.</td>
<td>22767506</td>
<td>PJSC Khmelnytskoblenergo</td>
<td>70,0089</td>
</tr>
<tr>
<td>7.</td>
<td>23399393</td>
<td>PJSC Mykolayivoblenergo</td>
<td>70</td>
</tr>
<tr>
<td>8.</td>
<td>00131954</td>
<td>JSC Kharkivoblenergo</td>
<td>65,0010</td>
</tr>
<tr>
<td>9.</td>
<td>00130926</td>
<td>OJSC Zaporizhzhyaoblenergo</td>
<td>60,2475</td>
</tr>
<tr>
<td>10.</td>
<td>00130725</td>
<td>OJSC Ternopiloblenergo</td>
<td>50,9990</td>
</tr>
<tr>
<td>11.</td>
<td>22800735</td>
<td>PJSC Cherkasyoblenergo</td>
<td>46</td>
</tr>
<tr>
<td>12.</td>
<td>00130872</td>
<td>PJSC DTEK Dniproenergo</td>
<td>25</td>
</tr>
<tr>
<td>13.</td>
<td>00131268</td>
<td>PJSC DTEK Donetskoblenergo</td>
<td>25</td>
</tr>
<tr>
<td>14.</td>
<td>00131305</td>
<td>PJSC Kyivenergo</td>
<td>25</td>
</tr>
<tr>
<td>15.</td>
<td>23269555</td>
<td>PJSC DTEK Zakhidenergo</td>
<td>25</td>
</tr>
<tr>
<td>16.</td>
<td>23293513</td>
<td>PJSC Sumyoblenergo</td>
<td>25</td>
</tr>
<tr>
<td>17.</td>
<td>23343582</td>
<td>PJSC Donbasenergo</td>
<td>25</td>
</tr>
<tr>
<td>18.</td>
<td>23359034</td>
<td>PJSC DTEK Dniprooblenergo</td>
<td>25</td>
</tr>
<tr>
<td>19.</td>
<td>00131713</td>
<td>PJSC Odesaoblenergo</td>
<td>25</td>
</tr>
</tbody>
</table>

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146 SPFU Decree of 30.12.2015 №2064 «On approval of the list of Group C, D objects to be sold in 2016». 42
## Annex 4
Principal powers of CMU in respect of state property objects (in the context of MGU activities)

<table>
<thead>
<tr>
<th>CMU powers under laws of Ukraine</th>
<th>Realization of CMU powers in secondary legislation</th>
<th>If amendments are necessary? If yes, please specify</th>
</tr>
</thead>
<tbody>
<tr>
<td>CMU shall determine executive bodies and state collegial bodies to perform functions of state property management (including of state corporate rights)(^{147})</td>
<td>These powers concern CMU’s general competence regarding management of state property.</td>
<td>No</td>
</tr>
<tr>
<td>CMU shall establish the procedure for the transfer of state property objects to managing subjects(^ {148})</td>
<td>The CMU Regulation(^ {149}) concerns CMU’s general competence regarding management of state property.</td>
<td>No</td>
</tr>
<tr>
<td>CMU shall determine the procedure for management of corporate rights by SPFU(^ {150})</td>
<td>Under the CMU Procedure,(^ {151}) CMU approves voting instructions for state representatives in MGU’s Supervisory Board meetings regarding the following agenda items: amendments to the statute; increase or reduction of the share capital; alienation and / or pledge of assets or property; approval of annual financial statements; distribution of profits; Amendments are necessary to this Procedure to remove MGU from its scope of application (by analogy with NJSC Naftogaz of Ukraine and its subsidiaries).</td>
<td></td>
</tr>
</tbody>
</table>

\(^{147}\) State Property Management Law, art.5(2)(1).
\(^{148}\) State Property Management Law, art.5(2)(2).
\(^{149}\) Regulation on the procedure for transfer of state property objects approved by CMU Resolution of 21.09.1998 №1482.
\(^{150}\) State Property Management Law, art.7(1)(3)(а).
\(^{151}\) Procedure for issue and approval of voting instructions for state representatives for General Shareholders’ Meeting and meetings of the Supervisory Board of a company with the state shareholding approved by CMU Resolution of 30.10.2014 №678.
<table>
<thead>
<tr>
<th><strong>CMU shall initiate ad-hoc revisions and inspections related to the use of state property objects and shall establish the procedure for such revisions/inspections</strong>&lt;sup&gt;152&lt;/sup&gt;</th>
<th><strong>The relevant act of secondary legislation has not been identified.</strong></th>
<th><strong>-</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>CMU shall establish the procedure of control over performance of state property management functions</strong>&lt;sup&gt;153&lt;/sup&gt;</td>
<td><strong>The CMU Procedure&lt;sup&gt;154&lt;/sup&gt; concerns the general competence of MEDT related to monitoring of state property management. It specifies that control over performance of state property management functions shall be carried out by way of monitoring of efficiency of state property management the aim of which is collection, accumulation and analysis of information on performance of state property management functions by managing subjects.</strong></td>
<td><strong>No</strong></td>
</tr>
<tr>
<td><strong>CMU shall establish the procedure of competitive selection of directors of business entities of the state sector of economy</strong>&lt;sup&gt;155&lt;/sup&gt;</td>
<td><strong>According to the CMU Procedure,&lt;sup&gt;156&lt;/sup&gt; SPFU will decide on the need to hold competitive selection of the Chairman of the Management Board of newly established companies; acquisition or alienation of corporate rights in companies; appointment and suspension of the Chairman and members of the Management Board, appointment of the person to temporarily act as the Chairman of the Management Board.</strong></td>
<td><strong>Amendments are necessary to this Procedure to remove MGU from its scope of application (by</strong></td>
</tr>
</tbody>
</table>

<sup>152</sup> State Property Management Law, art.5(2)(16).
<sup>153</sup> State Property Management Law, art.5(2)(18)(a).
<sup>154</sup> Procedure of control over performance of state property management functions approved by CMU Resolution of 19.06.2007 №832.
<sup>155</sup> State Property Management Law, art.5(2)(18)(r).
<sup>156</sup> Procedure of competitive selection of directors of business entities of the state sector of economy approved by CMU Resolution of 03.09.2008 №777.
established MGU to be held pursuant to this Procedure. However, this procedure shall be applied for selection of the next Chairman. In addition, in any event, the contract with MGU’s Chairman of the Management Board will be concluded by SPFU in the manner and per the form established by CMU.\(^{157}\)

| CMU shall establish the procedure of remuneration of directors of state enterprises\(^{158}\) | The CMU Resolution\(^{159}\) shall not apply to MGU as it will not be established in the legal form of a state enterprise and shall not qualify as an open joint-stock company established in the process of privatization (corporatization) of a state enterprise. | No |
| CMU shall establish the procedure of stock-taking of state property objects\(^{160}\) | According to the CMU Methodology\(^{161}\) stock-taking of state property shall be conducted by the relevant managing subject, i.e. SPFU. | No |
| CMU shall establish the procedure of disposal of assets of state business entities\(^{162}\) | The relevant act of secondary legislation has not been identified. | - |
| CMU shall establish the procedure of conclusion of joint activity agreements, commission, agency and property | The CMU Procedure\(^{164}\) stipulates that CMU approves conclusion of joint activity agreements, commission, agency and property management agreements upon If necessary, amendments may be introduced into the Procedure. | |

\(^{157}\) CMU Resolutions of 19.03.1993 №203 and of 02.08.1995 №597.  
\(^{158}\) State Property Management Law, art.5(2)(18)(r).  
\(^{159}\) CMU Resolution of 19.05.1999 №859.  
\(^{160}\) State Property Management Law, art.5(2)(18)(з).  
\(^{161}\) Methodology of stock-taking of state property approved by CMU Resolution of 30.11.2005 №1121.  
\(^{162}\) State Property Management Law, art.5(2)(18)(і).
<table>
<thead>
<tr>
<th>Management agreements by business entities with state shareholding exceeding than 50%[^163]</th>
<th>Submission of the managing subject agreed with MEDT, the Ministry of Finance of Ukraine, SPFU and the Ministry of Justice of Ukraine.</th>
</tr>
</thead>
<tbody>
<tr>
<td>CMU shall approve annual financial plans of state enterprises which are natural monopolies[^165] and establish the procedure of incurring expenditure in case of non-approval (rejection) of annual financial plans in due course[^166]</td>
<td>The CMU Procedure[^167] stipulates that in the event of non-approval (rejection) of annual financial plans business entities of the state sector of economy may incur expenditure directly related to production and sale of goods (works, services) with exception of: capital expenditures (unless decisions on them have been made by CMU), purchase and rent of cars, marketing, information and consulting services, insurance (excluding expenditure on state social security, mandatory insurance and insurance according to international treaties), representation expenses, production and distribution of advertising, charity, sponsorship and other assistance, provision for doubtful debts, as well as they may not sell or dispose of state property. The requirements of this Procedure shall not apply to NJSC Naftogaz of Ukraine and to companies where NJSC Naftogaz of Ukraine is a shareholder as of implementation of the internal controls system of NJSC Naftogaz of Ukraine in accordance with the Corporate Governance Action Plan for NJSC Naftogaz of Ukraine. If necessary, amendments may be made to the law of Ukraine to exclude approval of MGU’s financial plans by CMU. Amendments are necessary to this Procedure to remove MGU from its scope of application (by analogy with NJSC Naftogaz of Ukraine).</td>
</tr>
</tbody>
</table>

[^164]: Procedure of conclusion of joint activity agreements, commission, agency and property management agreements by state enterprises, institutions and organizations as well as by business entities with state shareholding exceeding 50% approved by CMU Resolution of 11.04.2012 №296.

[^163]: State Property Management Law, art.5(2)(18)(n).

[^165]: Commercial Code of Ukraine, art.89(5); State Property Management Law, art.5(2)(20).

[^166]: State Property Management Law, art.5(2)(18)(p).

[^167]: Procedure of incurring expenditure by business entities of the state sector of economy in case of non-approval (rejection) of annual financial plans in due course approved by CMU Resolution of 03.10.2012 №899.
<table>
<thead>
<tr>
<th><strong>CMU shall ensure control over efficiency of state property management</strong>&lt;sup&gt;168&lt;/sup&gt;</th>
<th><strong>CMU establishes mandatory criteria for selection of audit firms to audit financial statements or consolidated financial statements of a business entity of the state sector of economy.</strong>&lt;sup&gt;169&lt;/sup&gt; In general, these criteria stipulate conditions for the quality of service provider during procurement of audit services.</th>
<th>No</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>CMU shall determine the methodology for approval of financial plans of state business associations, enterprises, institutions and organizations and calculation of budget revenues from management of state corporate rights</strong>&lt;sup&gt;170&lt;/sup&gt;</td>
<td>The relevant act of secondary legislation has not been identified.</td>
<td>-</td>
</tr>
<tr>
<td><strong>CMU shall determine the criteria according to which establishment of a supervisory board is mandatory in state unitary enterprises and, account taken of laws of Ukraine, in companies within the state shareholding exceeding 50%</strong>&lt;sup&gt;171&lt;/sup&gt;</td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>-</td>
</tr>
<tr>
<td><strong>CMU shall determine the criteria of selection of the independent auditor and the criteria for determining state unitary enterprises and companies with the state shareholding exceeding 50% financial statement (including consolidated financial statement) of which shall be subject to mandatory audit by the independent auditor depending on the balance</strong></td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>While drafting these documents, requirements of independence and unbundling of the TSO shall be taken into consideration.</td>
</tr>
</tbody>
</table>

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<sup>168</sup> State Property Management Law, art.5(2)(19).

<sup>169</sup> Criteria according to which audit firms are engaged to audit financial statements or consolidated financial statements of certain business entities of the state sector of economy approved by CMU Resolution of 04.06.2015 №390.

<sup>170</sup> CMU Law, art.24(2).

<sup>171</sup> State Property Management Law, art.5(2)(16-1) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016.
<table>
<thead>
<tr>
<th>Sheet value of assets of such state unitary enterprises or companies&lt;sup&gt;172&lt;/sup&gt;</th>
<th>Relevant acts of secondary legislation have not yet been approved.</th>
<th>While drafting these documents, requirements of independence and unbundling of the TSO shall be taken into consideration.</th>
</tr>
</thead>
<tbody>
<tr>
<td>CMU shall adopt requirements to independent members of supervisory boards of state unitary enterprises and companies with the state shareholding exceeding 50%&lt;sup&gt;173&lt;/sup&gt;</td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>While drafting these documents, requirements of independence and unbundling of the TSO shall be taken into consideration.</td>
</tr>
<tr>
<td>CMU shall determine the procedure of competitive selection of the independent member of the Supervisory Board of state unitary enterprises and their appointment and of competitive selection of candidates of independent members of the Supervisory Board of a company with the state shareholding exceeding 50% to be nominated by managing subjects for appointment to positions of independent Supervisory Board members&lt;sup&gt;174&lt;/sup&gt;</td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>While drafting these documents, requirements of independence and unbundling of the TSO shall be taken into consideration.</td>
</tr>
<tr>
<td>CMU shall determine the procedure of disclosure of information on activities of state unitary enterprises and companies with the state shareholding exceeding 50% as well as of companies 50% and more shares of which belong to companies with the state shareholding of 100%&lt;sup&gt;175&lt;/sup&gt;</td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>-</td>
</tr>
<tr>
<td>CMU shall determine the procedure of</td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>While drafting these documents,</td>
</tr>
</tbody>
</table>

<sup>172</sup> State Property Management Law, art.5 (2)(17-1) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).

<sup>173</sup> State Property Management Law, art.5 (2)(17-2) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).

<sup>174</sup> State Property Management Law, art.5 (2)(18)(т) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).

<sup>175</sup> State Property Management Law, art.5(2)(18)(y) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
<table>
<thead>
<tr>
<th>Determination and approval of candidates of state representatives to be appointed to supervisory boards of state unitary enterprises and to take part in the General Shareholders' Meeting and be appointed to the Supervisory Board of companies with the state shareholding exceeding 50% (^{176})</th>
<th>been approved.</th>
<th>Requirements of independence and unbundling of the TSO shall be taken into consideration.</th>
</tr>
</thead>
<tbody>
<tr>
<td>CMU shall determine the procedure of determination of the procedure and rules for liability insurance, remunerations and compensations of Supervisory Board members in state unitary enterprises and companies with the state shareholding exceeding 50% (^{177})</td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>-</td>
</tr>
<tr>
<td>CMU shall determine the procedure of determination of clear objectives of state unitary enterprises and companies with the state shareholding exceeding 50% (^{178})</td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>While drafting these documents, requirements of independence and unbundling of the TSO shall be taken into consideration.</td>
</tr>
<tr>
<td>CMU shall determine the procedure of compilation and maintenance of contracts concluded with directors of business entities of the state sector of economy (^{179})</td>
<td>Relevant acts of secondary legislation have not yet been approved.</td>
<td>-</td>
</tr>
</tbody>
</table>

\(^{176}\) State Property Management Law, art.5(2)(18)(ф) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
\(^{177}\) State Property Management Law, art.5 (2)(18)(x) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
\(^{178}\) State Property Management Law, art.5(2)(18)(ц) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
\(^{179}\) State Property Management Law, art.5(2)(18)(ч) (per the wording of Draft Law №3062 adopted by VRU in the second reading and as a whole on 18.02.2016).
Annex 5
Target corporate governance structure of MGU

- **General Shareholders’ Meeting**
  (the function will be performed by SPFU directly with holding GSM)
  - appoints
  - Independent Nomination Committee
    consists of 4 persons: one representing the shareholder, one representing the staff of the TSO, two independent members
  - Supervisory Board
    (consists of 7 members the majority of which are independent)
    - proposes candidates of Supervisory Board members
    - Management Board
      - accountable to
  - Nomination and Remuneration Committee of the Supervisory Board
    - proposes candidates of Management members
Annex 6
Influence of state authorities on MGU under the laws of Ukraine

CMU
- fully or partially repeals SPFU acts in case of non-compliance with the Constitution and laws of Ukraine, acts of the President of Ukraine and CMU acts
- Prime-minister of Ukraine issues binding orders to direct, coordinate and control SPFU’s activities
- approves decisions on reorganization and liquidation as well as conditions of privatization, restructuring and reorganization of MGU
- approves annual financial plans
- within the competence provided in the law adopts legislation related to state property objects management

SPFU

MECI
- within the competence provided in the law issues binding decrees

MEDT
- within the competence provided in the law issues binding decrees

State Audit Service
- performs state financial audit on an annual and regular basis (depending on whether the regime of financial control of individual transactions applies)

GSM

Supervisory Board

Management

MGU
Considering that cogeneration plants and municipal heating companies perform the critical function of production of heat for centralised heating and hot water supply to population and with the view to avoid social pressure it is necessary to use all the best efforts to avoid termination of gas supply to the said enterprises till the end of the heating period of 2015/2016.

Minister (signature) V. Demchyshyn

Ramazanov 594-66-34

[Stamp reads: Ministry of Energy and the Coal Industry of Ukraine, No.01/31-1574 of 15.02.2016]
[Stamp reads: NJSC Naftogaz of Ukraine, No.104/5-16 of 15.02.2016]
On natural gas transmission

Changes in the functioning of the natural gas market in Ukraine led to implementation of new approaches to booking of natural gas transmission services through the gas transmission system of Ukraine. Thus, to obtain transmission services (services of physical transmission of natural gas through the gas transmission system) the transmission service customer shall submit to the TSO a monthly nomination for entry and/or exit points in respect of natural gas volumes planned for transmission with the possibility to adjust it further but no later than on the 25th day of the reporting month.

However, currently in the absence of stable electricity consumption and due to the reduction of the consumption share of the largest energy-intensive companies the daily unevenness of electricity consumption increases significantly. In this respect, the demand for capacity of energy units of cogeneration plants for performing operational balancing of electricity in the unified energy system of Ukraine is constantly changing. Such uneven functioning of energy units of cogeneration plants prevents effective planning of the required natural gas volumes for ensuring operations of cogeneration plants, which causes the need to constantly adjust the monthly gas nomination.

[Stamp reads: Ministry of Energy and the Coal Industry of Ukraine, No.01/31-2834 of 16.03.2016]
[Stamp reads: NJSC Naftogaz of Ukraine, No.185/5-16 of 17.03.2016]
Moreover, there is an issue with booking the monthly capacity of exit points of the gas transmission system by generating companies of cogeneration plants. In case of exceeding of planned capacities additional volumes are charged at a higher tariff; in case of underutilization of the planned volumes prepayment is not refundable, i.e. it is paid for the service that is not obtained.

Taking into account the specifics of operations of generating companies of cogeneration plants and with the view to improve the situation related to planning of natural gas volumes for transmission, it is proposed to consider the possibility to submit nominations for transmission of gas used for heat and electricity generation on a 10-day basis also allowing to make adjustments up to two days before the end of the reporting period and subject to payment of the monthly capacity of exit points of the gas transmission system of Ukraine by generating companies of cogeneration plants according to the actually consumed volumes of gas.

Minister (signature) V. Demchyshyn