Attachment I. Memorandum of Economic and Financial Policies

I. Background, Recent Economic Developments, and Outlook

Context

1. **Russia's unprovoked, illegal, and unjustified invasion of our country continues to bring enormous human, social, and economic costs.** Civilian casualties keep rising, around a quarter of the population has been displaced, and missile strikes countrywide continue including devastating attacks on our infrastructure, in particular electricity generation capacity. Despite all the destruction, suffering and challenges, our people continue to show remarkable courage and resilience, while macroeconomic, financial, and external stability have been preserved. Nevertheless, we continue to face major challenges: the fiscal deficit remains very high, entailing large external and domestic financing needs. Protecting core functions of the state under tight financing constraints force us to continue navigating difficult policy trade-offs.

2. **The Extended Fund Facility (EFF) arrangement provides a strong anchor for our economic policies, and we continue to sustain strong performance under the program.** The approval of the extended arrangement in March 2023 helped mobilize an external financing package from our international partners that now totals US$121.9 billion over the program period (2023Q2–27Q1). In these very difficult times, the program has helped infuse greater predictability into our macroeconomic management and remains a strong anchor for our economic policies. We remain highly committed to our program objectives; our robust implementation of major components of the program thus far is a testament to this. The welcome approval of external financing by the European Union (see ¶3) and the United States (comprising US$61 billion of supplemental appropriations for military and financial support), has eased concerns about near-term liquidity strains and signals the commitment of our international partners to our stability, reform, and recovery.

3. **The approval of the EU's Ukraine Facility has been a major step forward, which, coupled with efforts to achieve our strategic goal of EU accession, will reinforce long-term growth and stability.** In May 2024, the European Council approved the €50 billion Ukraine Plan for 2024–27, which will be critical to support our budgetary needs, recovery, reconstruction, and modernization efforts. Reforms to achieve EU accession will strengthen our economy and institutions, as they are essential to creating conditions for increased investment and growth going forward. Our candidate status implies that the choice of the regulatory regime defined by the EU acquis will frame our recovery and reconstruction process. Progressive integration into the European internal market, already underway within the Association Agreement and Deep and Comprehensive Free Trade Agreement, should enhance trade and stimulate revenue and technology transfer to the Ukrainian economy, thereby helping sustain the recovery.

Economic Outlook

4. The economic recovery in 2023 was stronger than expected, with resilient growth continuing into 2024Q1.

- Economic activity in 2023 was robust with growth of 5.3 percent, as households and firms continued to adapt to the war circumstances, FX market stability was maintained, including after the transition to the managed flexibility of the exchange rate, and the disinflationary trend continued. The resilience of the energy sector in 2023 was a key factor, although the sector faces renewed pressure from large-scale Russian attacks that started in late March 2024. The labor market has shown signs of stabilization amid lower net migrant outflows though strains from labor shortages remain considerable.

- Growth is expected to remain resilient between 2.5 and 3.5 percent in 2024; the recovery has slowed due to the impact of the energy attacks and an expected decrease in harvests, offsetting the expected strengthening in exports from the new Black Sea corridor and robust consumption growth. Inflation has continued to decelerate faster than expected from its peak of 26.6 percent y/y in end-2022 to 3.3 percent y/y in May, below the target range, driven by declining raw food prices from last year's strong harvests, compressed prices for processed food and some services, and easing external inflationary pressures. Inflation is expected to edge up in 2024 to around 8 percent due to pressures from business labor costs, further recovery in consumer demand, pass-through from the past currency depreciation and the fading impact of temporary factors (such as last year's large harvests and this year's mild winter) that helped contain inflation at the beginning of the year.

- For 2024, the current account deficit is expected to rise to US$10.6 billion (from US$9.2 billion in 2023) and remain broadly stable, reflecting (i) an improved trade balance, thanks to increased use of the Black Sea corridor; (ii) lower travel services imports (as cash withdrawals and spending by Ukrainians abroad declined), and (iii) higher FX outflows due to the recent easing of some FX controls. On balance, reserves are expected to end the year at US$41.8 billion (113.7 percent of the ARA metric).

- Under the managed flexibility exchange rate regime, the exchange rate is increasingly adjusting to market conditions, supported by FX interventions given the structural deficit, against a backdrop of a deepening FX market. The exchange rate has depreciated through end-April 2024 by a cumulative 8.4 percent since the transition. The spread between the official and cash rates has remained low, including following the easing of some FX controls amid increased confidence.

- Credit growth is recovering, broadly supported by government-backed subsidized lending initiatives (including the 5-7-9 program for SMEs and eOselya for mortgages), credit guarantee schemes, improved business activity and declining interest rates. The official non-performing loan ratio remains elevated at 36.1 percent amid a high provisioning ratio for NPLs (83.6 percent) in March 2024. Deposits continue to grow at a robust rate (23 percent, y/y in March).

5. The economy could rebound more quickly, particularly if the security situation improves sooner than expected. Several factors could support a stronger recovery, primarily from a decline in security risks that enables a quicker return of migrants and faster recovery in sentiment, along with a revitalization in economic activity from a swifter resolution of war-related supply disruptions and more durable access to seaports and other supply routes. Our efforts to raise resources for critical recovery and repair projects, including in the energy sector, would also support stronger growth. From a medium-term perspective, our economic growth could be accelerated by forceful implementation of structural reforms, including in the context of the EU integration, significant investments in reconstruction, including private investment inflows, as well as a faster return of migrants.

6. In spite of the recent strong growth, risks to the outlook remain tilted to the downside, amid exceptionally high uncertainty. Security risks could persist for longer than expected, putting pressures on our fiscal position, and leading to the emergence of additional budget needs. A prolonged or more intense war would weigh on firm and household sentiment, as well as exchange rate and inflation expectations and dampen the pace of return by migrants, worsening labor market mismatches. Export transit routes could be significantly interrupted, there could be further damage to energy infrastructure, or past supply chain disruptions could resurface, weighing on production costs and firm profitability. While near-term external financing risks have diminished following the approval of US aid and the EU Ukraine Facility, the risk of shortfalls or delays could materialize, exacerbating financing constraints and requiring difficult policy trade-offs. Moreover, in the event of such risks materializing, the needed higher domestic financing may become difficult to mobilize.

II. Macroeconomic and Structural Policies for 2024–27

A. Overview

7. The ultimate goals of the Ukrainian government's economic program—supported by the IMF—is to restore fiscal and debt sustainability and maintain external and financial stability, while promoting long-term growth in the context of post-war reconstruction and our path to EU accession. Our economic program continues to focus on a two-phased approach which includes both restoring stability while advancing necessary structural reforms in parallel, with the intention of broadening and deepening reforms once the war tapers off.

- Our current primary focus is to maintain macroeconomic, external, and financial stability, in order to strengthen Ukraine's capacity on its way to victory. Our program involves policies to ensure a robust budget implementation in 2024 coupled with a strong medium-term fiscal framework that would anchor fiscal policy and the assessment of financing gaps. The managed flexibility of the exchange rate strengthens the resilience of the Ukrainian economy and FX market, promotes better adaptation to domestic and external shocks, and reduces the risks of accumulating FX imbalances. At the same time and despite the war, we are implementing well-targeted structural measures covering public finances, the financial sector, monetary and exchange rate policies, governance, anti-corruption, and the energy sector to prepare the ground for Ukraine's post-war growth. Importantly, social spending is being safeguarded to the extent possible.

- Once the war has tapered off, we will build on the significant progress so far and shift our focus to more expansive structural reforms to entrench macroeconomic stability, support recovery and early reconstruction, promote economic growth, and thereby restore medium-term external viability. As conditions allow, Ukraine will revert to pre-war policy frameworks. Progress toward EU accession will be a major anchor for our policies; we have committed to undertake a wide range of measures in support of this under the Ukraine Facility.

8. We acknowledge IMF staff analysis on an updated downside scenario, and we are fully committed to swiftly taking all necessary measures to ensure program success and a stable economy.

- Since the start of the war, we have repeatedly and decisively taken measures to respond to shocks as they have materialized, carefully balancing the need for a prompt and effective response with social considerations. Building on this track record, we would respond decisively to a potential downside scenario, to ensure that public institutions function effectively while taking measures as needed to preserve economic and financial stability, and also maintain debt sustainability on a forward-looking basis. Under the updated downside scenario, as illustrated in IMF staff analysis, we stand ready to take additional feasible fiscal measures, including identifying tax policy measures that can be implemented swiftly and effectively or spending measures building on efficiency gains. In particular, we would be guided by the National Revenue Strategy (NRS), a cornerstone of our efforts to strengthen revenue mobilization. In parallel, we will also identify additional domestic financing as needed to ensure that financing gaps are swiftly closed, without compromising economic and financial stability or debt sustainability. We also stand ready to deploy our foreign reserves, adjust our monetary policy stance, and recalibrate FX controls, to maintain stability as needed. These are very difficult balancing acts, and we welcome the fact that our partners stand ready to provide additional financial resources sufficient to close financing gaps and preserve debt sustainability under the downside scenario; we are strongly committed to play our part to ensure the burden of adjustment is shared.

- We are equally focused on identifying policies that can help us achieve high and sustained growth rates, including via illustrative upside scenarios that motivate reform priorities towards EU accession. Our medium-and long-term growth post-war will crucially depend on catalyzing high and sustained investment levels, supporting inward migration, rebuilding human capital, and fostering an enabling business environment that could propel total factor productivity (TFP) growth to help converge to European income levels. In this regard, establishing frameworks for post-war reconstruction, which would enable us to absorb substantial official resources and also catalyze private capital, including foreign direct investment, could have a decisive impact. Reforms required to achieve the strategic goal of EU accession coupled with progressive integration into the European internal market through the Association Agreement and Deep and

Comprehensive Free Trade Agreement would be critical components of such a strategy. Implementing these wide-ranging policies and reforms will require our steadfast commitment for an extended period.

B. Fiscal Policy

9. Financing constraints necessitated a prudent approach to budget execution in the first quarter of 2024. Until significant external disbursements began arriving in mid-March, we needed to rely on policy measures and domestic resources to keep expenditures within the available envelope. Our efforts included restraining expenditures, front-loading revenues (including reaping the benefit of the extraordinary one-time tax on 2023 bank profits), mobilizing domestic financing, and drawing down our buffers. While our liquidity situation has improved substantially in recent months thanks to donor support, we have continued with our strategy of prudent budget execution.

10. As a result of these efforts, we achieved all the end-March 2024 fiscal targets, as follows:

- Reflecting tight control over budget implementation, the end-March non-defense cash primary balance of the general government excluding grants was UAH 241.9 billion (at program exchange rates), exceeding the program's floor of UAH 135.0 billion (***Quantitative Performance Criterion***).

- Likewise, the overall balance excluding grants was UAH -211.0 billion (at program exchange rates), exceeding the floor of UAH -344.5 billion (***Indicative Target***).

- Our tax revenues (excluding social security contributions) were UAH 508.0 billion through end-March, comfortably exceeding the floor of UAH 426.3 billion (***Quantitative Performance Criterion***), despite the impact of the blockades along the western border.

- The issuance of government guarantees was UAH 5.9 billion, and well below the ceiling of UAH 49.9 billion (***Quantitative Performance Criterion***).

- The accumulation of overdue accounts payable (domestic arrears) was UAH 1.5 billion as of end-March, below the ceiling of UAH 2.0 billion (***Indicative Target***).

- Social spending outlays amounted to UAH 142.1 billion at end-March, exceeding the floor of UAH 130.0 billion (***Indicative Target***).

11. The 2024 budget remains the anchor for our fiscal policy intentions this year, capturing our major policy intentions and initiatives, as follows:

- *Expenditures*: The budget prioritizes national defense and contains an allocation consistent with a full year of war operations, while other expenditures will continue to be prioritized. We are continuing to provide adequate resources for the social safety net, including to address the needs of war veterans and vulnerable layers of the population. The floor on spending on social programs ***(Indicative Target)*** represents our commitment to safeguard this spending. The annual pension indexation from March 1, 2024 of 7.96 percent has been carried out in line with the legislation, and is consistent with the deficit projection.

- *Revenues*: In addition to the extraordinary one-time bank profit tax, we are also implementing revenue policies set out in the budget, including the revised allocation of personal income taxes between the state and local budgets.

- *Balance*: We continue to target an overall balance excluding grants of UAH -1,562 billion or around -21 percent of GDP. This deficit is financed primarily through budget support from international donors, and is consistent with our efforts to return to fiscal and debt sustainability. Our progress in budget implementation will continue to be monitored by the floor on the non-defense primary balance of the general government excluding grants ***(Quantitative Performance Criterion)*** and the floor on the overall cash balance of the general government excluding grants ***(Indicative Target)***.

12. We recognize that risks are exceptionally high and rising and will therefore resist additional budgetary pressures that could jeopardize our hard-won stability. On the revenues side, we will continue to refrain from introducing tax amnesties for the duration of the program, and from any tax policy and administrative measures that may erode the tax revenue base. Furthermore, any tax-related measures that are needed to support imports related to national defense and security will be targeted, timebound, controlled, and subject to oversight. As regards expenditures, we will resist pressures on non-core spending categories, recognizing the already high contributions from international donors and partners, and prioritize national defense. Further, we will only revise spending categories in consultation with IMF staff and after identifying either new financing sources or compensating fiscal measures. We will continue to exercise strong commitment controls and maintain strict oversight of budget execution by key spending units.

13. We are prepared to take fiscal measures as needed to ensure stability, contain risks, and advance EU accession objectives. On the latter, following CMU approval, draft legislation has been registered in Parliament to gradually align tobacco and fuel product excise taxes with EU requirements (over 2024H2–2028). Draft legislation to introduce excises on sugary drinks has also been submitted. We aim to secure swift adoption of these laws. Work is also underway to develop legislation on medical cannabis taxation and introduce advance payments on CIT for fuel stations. We also recognize that improving enforcement is essential, including to avoid leakages and ensure equity, and will strive to improve excise tax administration, including for tobacco. Specifically, as envisaged in the NRS, we are developing a track and trace system, in cooperation with the Ministry of Digital Transformation, and plan to make it operational by January 1, 2026. Given the balance of risks, we will stand ready to take feasible measures to respond to potential shocks. To this end, the working group, which first met last February to identify potential temporary revenue measures for 2024, is continuing its work. We also intend to mobilize additional domestic financing if necessary.

14. The budget for 2025 will reflect our efforts to secure sustainability and will be prepared according to the standard timeline. We expect next year to remain challenging, with substantial expenditure pressures that correspond to our defense, reconstruction, and development priorities. We recognize that while external partners will continue to be an important source of financing, we will need to step up our efforts to generate revenues, while expenditures will need to be carefully prioritized. These efforts will help ensure that the budget is financeable and consistent with sustainability. As regards the process, consistent with the Budget Code, the Cabinet of Ministers of Ukraine will approve the Budget Declaration for 2025–2027 in June, which will then be submitted to Parliament. This document, our first medium-term budget declaration since restoring the Budget Code, is an important milestone in strengthening our medium-term budget framework (see ¶29) and will form the basis for the preparation of the 2025 Budget. We remain committed to adhering to the standard schedule, to ensure careful preparation and timely adoption.

15. Over the medium term, we remain committed to policies that are consistent with fiscal and debt sustainability. The return to sustainability involves three components. First, we will continue implementing fiscal adjustment over the coming years to deliver a medium-term primary surplus. Post-war priorities for recovery and reconstruction, social protection, and maintaining defense readiness require reform efforts to focus on tax policy and administration. We aim to mobilize 3-4 percent of GDP in additional revenues during 2024–27. Second, we will carefully evaluate the financing mix and for external financial support will continue to seek highly concessional terms where possible. Third, we will work to complete a treatment of external public debt that brings public debt and gross financing needs back down to manageable levels and in line with program parameters (see ¶38).

16. Relentless attacks on our energy infrastructure have pushed our reconstruction needs beyond those estimated in the third Rapid Damage and Needs Assessment (RDNA-3). This report, published on February 15, 2024, estimated reconstruction needs of US$486 billion over the next 10 years. Addressing the largest needs in housing, transport, and commerce and industry will be vital to delivering essential public services, restoring the economy's productive capacity, and providing adequate social protection. Repair and recovery on these fronts will also help promote the return of those who were forced to flee the country. In considering initiatives in this area, we will ensure that these activities are consistent with a return to fiscal and debt sustainability. To this end, we will carefully evaluate the financing mix, and will seek financing on highly concessional terms. Additionally, we will make sure that the mechanisms used for reconstruction financing are consistent with the principles of integrated public investment management to ensure that critical reconstruction projects fit into the medium-term budget framework (see ¶29).

C. Financing Strategy

17. Timely and predictable external financing on appropriately concessional terms is an essential pillar of our financing strategy. We remain very grateful for the substantial budget support from our donors, which has risen to US$45.1 billion since the start of the program, of which US$11.8 billion was disbursed over January-May 2024; for the rest of the year, we expect an additional US$26.1 billion of external budget support. Over the next 12 months of the IMF-supported program (July 2024–June 2025), firm financing assurances are in place thanks to large official sector multilateral and bilateral commitments. Continued support from the EU, IFIs, and bilateral donors in the amounts, terms, and timing envisaged are vital to maintain economic and financial stability. Consistent with this requirement, looking beyond June 2025, key partners have assured us of their continued support, which provides good prospects for ensuring the program will remain fully financed over the program period.

18. We recognize the need to further strengthen our efforts to sustain net domestic financing over the program period, contributing to efforts to maintain stability. Our strategy will involve increasing the issuance of domestic government securities in the primary market with an objective of obtaining net positive financing in 2024.

- As of end-May 2024, we have mobilized net domestic bond financing of UAH 46.1 billion or almost US$1.2 billion, resulting in an implied rollover rate of 132 percent so far this year. We have continued with the progress we began last year in matching issuance yields and maturities to market demand, and in lengthening the maturity of our issuances. About UAH 3.3 billion were issued in the form of designated benchmark bonds that banks may use to meet reserve requirements.

- Given the substantial liquidity available and expected in the banking system, we remain committed to identifying and implementing ways to increase bank financing, including studying the flow of liquidity into the banking system, including on a bank-by-bank and bank-group basis, in order to develop targeted strategies that encourage increased uptake of government bonds, supported by the joint Working Group under the auspices of the Financial Stability Council (FSC), established in April 2023. With an appropriate mix of approaches, such measures could contribute to positive net domestic financing over the course of the program. In this regard, the smooth functioning of secondary market trading of government bonds on stock exchanges is important, and we aim to ensure the continuation of such trading on the respective stock exchanges to support efficient price discovery and liquidity of the government bond market. Additionally, discussions are proceeding between the MOF and NBU to agree on ways to achieve savings on other domestic debt.

Successful placement of domestic securities coupled with timely external financing on appropriately concessional terms will enable us to execute the budget as planned, avoid arrears, and continue to avoid monetary financing. It will also ensure that the budget is financed in a manner consistent with safeguarding macroeconomic and financial stability and consistent with attaining debt sustainability.

19. In addition to seeking an external debt restructuring (¶39), we will ensure our debt management strategy is consistent with our objectives under the program. Following the debt treatment on external commercial claims, which is moving forward, there will be important impacts on the overall public debt burden and its structure. To reflect these developments, we plan to publish an update to the Medium-Term Debt Strategy (MTDS) by end-2024. We are also committed to strengthening the capacity of the Debt Management Agency, including by increasing staffing and training. We will continue to support the development of the domestic debt market, including through medium-term efforts to maintain the attractiveness of locally-issued instruments, diversify the set of investors (including encouraging the participation of non-residents), and cautiously restore international capital market access, thereby enabling the bond market to play an active role in reconstruction.

20. We are determined to strengthen treasury cash and liquidity management. The ongoing war and recent uncertainty around the timing of external disbursements has led to volatility in our budget execution. These developments, along with our continuous efforts to strengthen budget execution and commitment control, have prompted us to strengthen liquidity forecasting and cash management to help lower the volatility and transaction costs of treasury resource management. To this end, with the help of FAD TA, we have conducted a diagnostic assessment of treasury cash and liquidity management based on an examination of international best practices with regard to the roles of finance ministries, treasuries, central banks, and debt management agencies. We are reviewing the findings of the diagnostic assessment to improve the predictability of cash and liquidity management and may seek further TA.

D. Fiscal Structural Reforms

22. Despite the uncertainty and risks, we are moving forward with our structural reform agenda to support EU accession and achievement of development goals. In the area of public finance we will focus on: (i) raising adequate revenues to help meet reconstruction and social spending needs, guided by the objective of enhancing the efficiency, fairness and simplicity of the tax system, including through the home-grown multi-year National Revenue Strategy (NRS); (ii) preparing our public investment and public financial management for the post-war era by strengthening public investment processes, the project management cycle, and commitment controls; (iii) reforming and strengthening the pension system and social safety net, (iv) enhancing fiscal transparency and management of fiscal risks; and (v) ensuring fiscal sustainability and the predictability of budget policy by restoring the role of the medium-term budget framework (MTBF).

Revenue Mobilization

23. Our efforts to increase revenues through tax policy and administrative reforms are guided by the NRS. The NRS, adopted in December 2023, aims to establish a fair and competitive tax framework to generate revenues sufficient to safeguard our post-war development goals while maintaining fiscal and debt sustainability. Informed by IMF FAD TA, the NRS provides guidance for coordination among government agencies, donors, the private sector and civil society on tax policies and administration, led by the MOF. As our focus now shifts to NRS implementation, we have developed detailed implementation plans with specific timetables for tax administration, customs, and tax policy reforms. Importantly, we will continue to abstain from any tax policy and administrative measures that may adversely affect the tax revenue base, and as such we will refrain from introducing new categories of taxpayers in the existing preferential regimes.

24. Near-term tax policy measures focus on raising revenues from excises, further alignment with the EU acquis, and streamlining tax privileges. We recently submitted legislation to increase excise rates, a first step in a gradual increase to EU minimum levels over the medium term (see also ¶13). In line with the NRS, we are also planning to better target and rationalize tax exemptions, minimize revenue losses and avoid compromising equity and economic efficiency. To this end, we had initially committed to conducting an assessment of the effectiveness of tax privileges, including their cost to the budget. After further consultations, we are now considering a phased approach, which will allow for greater depth and continuity in the analysis. Accordingly, in consultation with IMF FAD TA, we will first develop and adopt a formal assessment methodology for tax privileges and guidelines specifying (i) the number of topics on tax privileges to be evaluated in an annual cycle, (ii) a standardized evaluation template, and (iii) the publication process of underlying assessments **(*Structural Benchmark,* end-July 2024, proposed to be modified and reset to end-September 2024*)*.** Subsequently, this methodology will be phased in and gradually applied to all relevant topics, targeting the most significant tax expenditures first, and leading to a regular evaluation cycle covering all topics over a number of years.

25. Over the next few years, we will undertake important tax policy reforms, guided by the NRS, to meet post-war needs. In addition to streamlining tax exemptions, we will strengthen revenue mobilization by:

- (i) developing a comprehensive package of measures for the post-war period to reform the taxation of carbon emissions, based on a concept of environmental protection; (ii) analyzing and assessing the taxation of extractive industries; and (iii) defining the principles of taxation of virtual assets, aligned with EU rules, in particular with regard to information exchange and initiatives of the OECD Global Forum. Work in several of these areas has already begun and will be supported by TA from the IMF FAD and other international development partners.

- In the future, when conditions are ready, we will also consider reforms to make the tax system more equitable (e.g., through a more progressive personal income tax (PIT)). However, as outlined in the NRS, such PIT reforms require administrative reforms, including to safeguard the confidentiality of tax data in the STS systems.

- We are also developing legislative amendments to implement rules to combat tax evasion practices that take into account the requirements of the EU Anti-Tax Avoidance Directive (EU ATAD) and the best international practices for preventing tax evasion and ensure effective protection of the tax base from erosion and profit shifting.

26. Near-term reform efforts at the State Tax Service (STS) focus on building public trust in the STS and developing modern compliance risk management practices:

- Taxpayer survey results from 2022 have underscored the need to improve public perceptions of the STS through improved taxpayer services and anticorruption reforms. Currently we are working on eliminating problems identified in the survey. With support from the World Bank, a similar survey, by an independent company, has started in April 2024, with results to be published within two weeks after receipt by the STS, no later than August 2024.

- We will approve a long-term Digital Development Plan for the STS in accordance with the NRS's implementation plan (by the end of 2024). It will include measures for the gradual consolidation of IT platforms and information resources, and their administration by an independent administrator.

- We will take measures to ensure the confidentiality and protection of data in the STS systems (including information received from taxpayers and tax agents). To enhance the confidentiality of tax data held by STS, by end-2024 we will develop the concept of using anonymized data (data masking) on taxpayers by tax authorities (see NRS section 4.2.3), until the risk of tax non-compliance is detected. These changes to our systems will be operational by end-2026.

- To improve our risk-based approach to tax administration, we will develop a methodology to operationalize the tax risk management system. For this purpose, we will adopt a comprehensive compliance improvement plan (Overall Compliance Improvement Plan) on the identification, analysis, assessment, and mitigation of risks by major types of tax risks. By end-June 2024, we will launch a pilot of the new compliance risk management system, which requires a resolution by CMU.

- We are also working on: (i) organizational restructuring that will reflect the results of the functional review (by end-2024) to better align the STS's organizational structure with the principle of functionally organized tax administration and support modern Compliance Risk Management practices of functional principle; (ii) determining the criteria for assessing the impact and efficiency of the STS Anti-Corruption Program; (iii) implementing IT solutions for SAF-T UA (electronic format for large taxpayer data submission , an NRS envisaged measure that is being implemented within the EU support framework); (iv) improving the efficiency of information exchange with foreign competent authorities (including obtaining positive assessment from the OECD Global Forum on Information Security Management Maturity).

27. Near-term reform efforts at the State Customs Service (SCS) focus on areas critical for reducing corruption risks:

- We have adopted legislation that reinstates post-clearance customs audits, effective end-May 2024, to complement the reinstatement of tax audits and close potential loopholes in managing compliance processes.

- We have adopted legislation to criminalize large-scale customs fraud and smuggling, effective January 1st, 2024, for excisable goods and July 1st, 2024, for all other goods. We have also submitted legislation to modernize the framework to address administrative liability for violations of customs regulations, to be adopted by end-2024.

- We have submitted to Parliament significant revisions to the Customs Code to align the legislation with international best practice. The reform will (i) simplify procedures, (ii) clarify the treatment of customs debt, (iii) establish the legal basis for dismissing customs officers, including the role of integrity checks in a framework for periodic re-attestation (verification of their qualifications and integrity), (iv) set up a disciplinary committee, (v) introduce the hiring of customs personnel on contractual basis, (vi) ensure alignment with EU legislation and regulations, and (vii) ensure that, given its central role in government finances, the SCS remains subordinated to and accountable to the MOF. We intend to establish a merit-based and transparent process for leadership selection, with integrity checks and with meaningful participation of experts with international experience, which is consistent with the relevant legislation. The law will also continue to prevent the re-hiring of personnel previously dismissed from the civil service for ethics violations. We are currently considering amendments to the initial proposal and will continue to consult with the IMF and other international partners. We aim to adopt amendments to the Customs Code, in line with best practice, by end-October 2024 (***proposed Structural Benchmark,*** **end-October 2024**).

- We will launch an initiative to determine the criteria for assessing the impact of the SCS Anti-Corruption Program, by end-September 2024. This assessment will be supported by regular (biannual) independent surveys of traders on the perception of integrity level in customs. Moreover, we are working on: (i) reforms of HR and compensation policies; (ii) improving operational management of customs from its headquarters, including the development of centers of excellence for different functional tasks; and (iii) moving the verification/checking of customs documents from border crossings to inland offices.

28. Economic Security Bureau of Ukraine (ESBU). Given the importance of strengthening compliance controls and detecting major financial and economic crimes, there is a need to bolster analytical support for identifying tax evasion. To this end, we will adopt a new ESBU law (***end-June Structural Benchmark***) that establishes a clear mandate and scope for investigative powers for the ESBU consistent with good practice by focusing on major economic crimes and strengthening its analytical capacity (complemented by efforts to ensure the capacity of the STS and SCS to effectively address violations in the tax and customs spheres). The ESBU's activities will be directed and coordinated by the CMU, while noting the ESBU's focus on major economic crimes. The existing delineation between the investigative powers of the ESBU and the National Anti-corruption Bureau of Ukraine (NABU) will be maintained. In addition, the law establishes a legal basis for the operation of the ESBU in order to (i) develop an open, transparent and competitive process for selection of management and staff; (ii) strengthen requirements for the selection commission for the ESBU head, including a decisive and crucial vote for independent experts with international experience; (iii) set up of a disciplinary committee; (iv) introduce a contract system for employees; and (v) develop a mechanism of attestation based on high-level principles in the law and procedures approved by the new ESBU head; the attestation of managers will be prioritized and completed within a reasonable period after the appointment of the new ESBU head.

Restoring the Medium-term Budget Framework

29. We will continue enhancing expenditure planning and the medium-term budget framework (MTBF). With the help of IMF TA, we will undertake a diagnostic review of pre-war MTBF policies and practices relative to best practices **(*Structural Benchmark*, end-October 2024)**. To this end, we have undertaken the first set of gap analyses, which have identified key areas of focus in our work. In this context, as a first step, we have started with preparation of the budget declaration for 2025-2027 and have sent a letter to key spending units requesting them to share with MOF key factors feeding into the estimation of baseline costs of public services for this period. This is an essential input into enhancing the credibility of fiscal forecasts and assessing the affordability of existing policies. Based on this diagnostic review, we will take a sequenced approach to strengthening the medium-term budget planning and expanding the coverage of the MTBF to include budgets of the local governments and social funds. In this regard, we recently submitted to the Parliament legislation (draft law No. 11131) to restore medium-term budget planning for local budgets. Key steps towards aligning the MTBF with international practices and EU requirements are also among the priorities. Looking ahead, we expect to have continuous IMF TA support to enhance the estimation of the baseline expenditures in the instructions for the formulation of the 2026-2028 Budget declaration and 2026 Budget.

Pensions and Social Spending

30. With the help of World Bank TA, we are preparing modifications to the pensions system and mechanisms to support vulnerable layers of the population:

- **Pensions.** We plan to work on a comprehensive conceptual framework to improve the pension system and are reviewing the possibility of introducing a second pillar of the pension scheme, when conditions are in place. We reiterate that any proposed legal amendments that would increase pension expenditures need to be accompanied by a medium-term fiscal and debt sustainability analysis, and a clear identification of the necessary resources in the amendments to the Pension Fund of Ukraine budget. We will refrain from: (i) introducing new special pensions or privileges; (ii) providing further discretionary benefit increases; and (iii) modifications that would lead to a lowering of the legally defined retirement age.

- **Mechanisms to support vulnerable groups.** We are working on further enhancement of targeting and means testing of benefits to vulnerable groups of population. With the support of the World Bank, including through a programmatic loan, we are working on draft legislation to consolidate different types of social entitlements. More specifically, we are exploring the options for integrating various social assistance programs under a single unified package based on individual needs regardless of a recipient's status (e.g., IDP or non-IDP). In this context, we also have increased the income threshold for eligibility under the Guaranteed Minimum Income (GMI) program by 10 percent.

Fiscal Transparency and Risks

31. Measures to enhance fiscal transparency and address fiscal risks remain an important part of our program. Specifically:

- By including a Fiscal Risk Statement (FRS) in the 2024 budget, we achieved significant progress in strengthening our risk analysis. Going forward we will include a consolidated view of financial performance analysis and stress testing across major SOEs. We are also taking steps to strengthen the policies and practices for feeding the FRS analysis into the annual budget preparation, strengthening the integration of fiscal risks at all stages of the budget cycle. As a first step, we have issued a letter to line ministries and key spending units requesting them to start identifying key fiscal risks. The information received on key fiscal risks will be included in the medium-term budget declaration for 2025–2027.

- Based on recent IMF TA on risk assessment and SOE stress testing, we will continue strengthening SOE stress testing under different scenarios. We will identify major public companies severely affected by the war and prepare an assessment of their potential fiscal and quasi-fiscal costs **(*Structural Benchmark,* end-September 2024**). We have already requested IMF TA to support our work and are working on defining the scope and the timeline of the assessment.

- To strengthen the link between the fiscal risks assessment and the predictability of government spending, we will develop methodological guidance for assessing fiscal risks in key spending areas and contingent liabilities, including PPPs, guarantees, and SOEs. By integrating these assessments more robustly into the early stages of the budget cycle, fiscal risk analyses can better inform budgetary and fiscal decisions. In this process, we will reach out to MOE and other line ministries to develop methodological guidance in their respective areas of responsibility and establish stronger links between the fiscal risks assessment and government spending predictability.

- With the help of ongoing IMF TA, the MOF will continue the development of risk-based fees for guarantees and prepare amendments to the existing decree. The upcoming IMF TA mission is expected in July-August 2024.

- In collaboration with MOE, the MOF will publish a list of PPPs and prepare a review of the associated risks and potential impact on the 2025 Budget and onwards by end-September 2024**.**

32. We are implementing reforms to reduce the deficit and limit fiscal risks from the BDF's 5-7-9 loan program. In line with the BDF concept note developed by MOF in consultation with MOE (***Structural Benchmark,* end-March 2024, met**), we have reduced bank margins by 300-500 basis points and lowered the maximum size of working capital loans to non-priority sectors from UAH150 million to UAH5 million. An earlier backlog of bank compensations has been resolved. We are now working on the remaining measures to limit the program's deficit in 2024 and eliminate it in 2025, including (i) reinstating state aid rules and (ii) further targeting the lower end of medium-sized enterprises by end-June 2024. Meanwhile, implementing ESG criteria (to the extent possible by end-2024) will improve the quality of the program and further limit its size.

33. The MOF remains responsible for overseeing the BDF. We have developed a coordination mechanism with clearly defined roles for the MOE and the MOF. While the MOE will maintain its role of identifying priority sectors for SME support, the MOF will control and monitor spending under the program. This adequately balances SME support objectives against fiscal risks and ensures that the established directions and bank lending limits are respected. The appropriations for the 5-7-9 program in the 2025 Budget will be consistent with the parameters of the program. We will also ensure that the 5-7-9 program remains solely within the BDF, preventing its delegation to (or replication by) other entities.

34. Our reforms of the 5-7-9 program are accompanied by measures to strengthen the BDF's effectiveness and sustainability. The MOF, in collaboration with international partners, has commissioned an independent assessment of the BDF (to be completed by end-2024) and its support programs, with the goal of refining their operational design to effectively serve only those SMEs that encounter substantial barriers to funding and of informing the future role of the BDF. Moreover, the World Bank will carry out a policy effectiveness review of the 5-7-9 program in 2024. To ensure legal certainty and attract a wide range of qualified candidates for the BDF supervisory board, we recently passed a law to align the asset declaration obligations of the BDF's foreign independent supervisory board members with those of SOBs. To further strengthen the governance and financial self-sustainability of the BDF, we are committed to:

- Increasing BDF's fees from 0.15 percent to 0.5 percent and shifting responsibility for paying such fees from the government to banks participating in the 5-7-9 program (by end-September 2024).
- Establishing a BDF supervisory board with majority of independent candidates (by end-September 2024).
- Preparing a draft law to clarify the mandate and ensure the independence of the supervisory board, as outlined in our BDF concept note (by end-year 2024).

35. To limit fiscal risks, any government lending facilities or development finance institutions will strictly adhere to international best practice. We will ensure that any legislation along these lines conforms to international best practice. Specifically, we will ensure that any proposal internalizes the need for appropriate oversight (including by the competent authorities), a business model that ensures long-term financial sustainability to mitigate fiscal risks, and incorporates sound risk management frameworks and corporate governance standards, to provide insulation from political interference. We will consult with IMF staff and other international partners before launching any such programs.

36. We will continue to enhance transparency in the management and spending of budgetary funds and special accounts:

- ***Fund for the Liquidation of the Consequences of the Armed Aggression.*** The Fund served its purpose well in the context of Budget 2023, supporting the restoration of destroyed and damaged property in the amount of UAH 38.1 billion. In 2024, the Fund will continue serving its purpose as stated in the Article 28 of the 2024 State Budget Law. The sources for the Fund's operations are expected to comprise the unspent balance of about UAH 24 billion as of end-2023.

- ***Special accounts.*** In April 2023 we amended the Budget Code to ensure transparency of sources, usage and reporting of funds on special accounts. Starting mid-2023, the MOF publishes information about sources and usage of funds in special accounts donated by private individuals and legal entities. We are committed to continuing transparency and accountability of these accounts.

Strengthening Public Investment Management

37. We have begun to implement the roadmap, developed in 2023, to reform our public investment management (PIM) which lays out an ambitious agenda. The roadmap will gradually address identified weaknesses in the areas of (i) strategic planning, (ii) integrating public investment into the MTBF, (iii) procedures for preparing, appraising, selecting, and implementing projects, (iv) institutional capacity, and (v) monitoring and evaluating implementation. As a first step to implement the roadmap, we recently established the Strategic Investment Council (SIC), which will play a central role in defining the project pipeline. By end-September 2024, the SIC will consider the list of public investment projects for the 2025 budget. With the help of IMF TA and/or other partners, we will further operationalize the roadmap, including through a government decree with a specific action plan and a timeline that provides clear linkages between the MTBF and national reconstruction priorities, specifying a gatekeeper role for the MOF, which implies a central role for MOF in all stages of public investment management **(*Structural Benchmark,* end-December 2024*)***. We will amend the Budget Code (by end-2024) to establish clear institutional links between the MTBF, PIM, and reconstruction priorities, thus bolstering the MOF's institutional role as a gatekeeper of public investment and mitigating risks to debt sustainability. Coordination will be strengthened between the MOF, MOE, Ministry of Infrastructure, and other line ministries, who remain responsible for project execution. Meanwhile, we will continue working on strengthening public investment management policies consistent with best practices of MTBF and PIM (¶29), following the principles of budget unity, coherence, and predictability.

E. External Debt Strategy

38. To help restore debt sustainability on a forward-looking basis, we publicly announced our intention to proceed with a debt treatment of our external public debt on March 24, 2023. Our strategy seeks to help close financing gaps during the program period, reduce gross financing needs to manageable levels, including after the program, and to place public debt on a sustainable path. Our strategy is also designed to help create the necessary conditions for private sector participation in the post-war reconstruction of Ukraine and takes into account the importance of preserving financial stability. To this end, we hired external financial advisors and are committed to a credible process with transparency for information and communication. We continue to discuss our strategy with private creditors and seek their feedback. Our goal remains to restore public debt sustainability and ensure that our program is fully financed throughout its duration, including in a downside scenario.

39. The debt treatment comprises the following elements:

- *Official bilateral debt.* Creditors in the Group of Creditors of Ukraine have committed to a two-step process involving an extension of the debt standstill, coupled with a separate assurance to deliver a final debt treatment sufficient to restore debt sustainability before the final review of the IMF-supported program. The first stage—an extension of the standstill until 2027—was formally concluded in December 2023. We will seek treatments on comparable terms with other official creditors.

- *External commercial debt*. Our goal remains to reach agreement on a debt restructuring with our international bondholders and other participating commercial creditors by the time the current standstill ends in August 2024. To this end, and to ensure compatibility with relevant Fund policies:

  (i) We are currently working with our legal and financial advisors, in discussions with bondholders, to reach an agreement consistent with the program's debt sustainability targets under the latest baseline scenario;

- We are committed to undertake a further treatment of external commercial claims as needed to restore debt sustainability, in line with program parameters. We note that the exceptionally high uncertainty now prevailing means that it is difficult to pin down a future scenario. If the scenario prevailing at the penultimate review of the program (or once conditions of exceptionally high uncertainty abate if that occurs earlier) is worse than that on which the present restructuring is based, then a further treatment will be necessary. The further treatment would be expected to take place once conditions of exceptionally high uncertainty abate, or at the latest by the penultimate review of the program. We continue to retain legal and financial advisors to assist us in this process and are undertaking consultations with creditors about an eventual further treatment, including sharing information about the potential range of outcomes. Given the time it could take to get to the point where an offer could be launched, we are committed to continuing regular consultations with creditors, including sharing of updated information as it becomes available.

40. To support our goal of safeguarding debt sustainability, we will continue to strictly limit the issuance of guarantees (*Quantitative Performance Criterion*). This limit is consistent with reinstatement of the articles of the Budget Code. Adequate space will be provided to facilitate guarantees on loans from International Financial Institutions (IFIs) and foreign governments for projects, including those for recovery and reconstruction.

F. Monetary and Exchange Rate Policies

41. Our monetary and exchange rate policies aim to safeguard price and external stability and ensure an adequate level of international reserves. Guided by our Strategy we are adapting our monetary and exchange rate policies in view of evolving macroeconomic conditions and outlook, including cautiously continuing with FX liberalization.

Monetary Policy

42. We will maintain an appropriate monetary policy stance to support price stability, anchor inflation expectations, and enhance FX market stability. In view of rapid disinflation combined with a favorable inflation trajectory, we continued the easing cycle by cutting the key policy rate (KPR) by 150 bps this year, at a faster pace than envisaged at the beginning of the year. Inflation remaining close to the target, improved inflation expectations, and the successful transition to greater exchange rate flexibility have strengthened the role of inflation as the nominal anchor of monetary policy. Moreover, inflation control has been enhanced by the gradual restoration of monetary transmission channels, including by the KPR regaining its effectiveness in fulfilling its role as a monetary instrument, due to the impact of measures undertaken by the NBU. Overall, consistent with our Strategy and subject to its conditions, we will continue a gradual transition toward a full-fledged inflation targeting regime. Our strong commitment to achieving and supporting price stability in the medium term is crucial in guiding inflation expectations. Our interim regime deviates from the pre-war due to the managed flexibility of the exchange rate, a vital policy instrument due to a high uncertainty. The flexibility inherent in our inflation targeting regime, which accommodates short-term deviations from the inflation target in response to shocks, should facilitate the adjustment of the Ukrainian economy to shocks while maintaining control over expectations. To this end, we plan to steer monetary policy towards sustaining moderate inflation throughout 2024, followed by its return toward the target of 5 percent over the NBU's forecast horizon. With inflation expected to remain in control over the policy horizon under the baseline, we see further scope for the easing cycle to continue, albeit more gradually than in the previous quarters, and subject to the balance of risks to the inflation and economic outlook on the NBU's forecast horizon. The NBU intends to adapt its monetary policy if the balance of risks to inflation and the economic outlook changes significantly over the forecast horizon. Overall, in line with our Strategy, we intend to maintain sufficiently positive real interest rates to support price and external stability.

43. To ensure appropriate attractiveness of hryvnia-denominated instruments and strengthen monetary transmission, we will continue to adjust the operational design of our monetary policy framework as well as take steps to manage the banking system's structural liquidity position. In October 2023, we shifted from a corridor to a floor system, aligning the KPR with the main overnight CD instrument, thereby enhancing the KPR's role. We have also maintained the 3-month CD (access to which is linked to hryvnia term deposit growth), which has supported real returns and volumes of such deposits, enhancing FX stability and bank funding. We continue to make technical adjustments to the operational design to better enable alignment with the appropriate stance and enhance monetary policy transmission, and supporting external stability and reserves. Recently, this has included adjusting the eligibility for 3-month CDs, reducing the spread between the rates on 3-month CDs and overnight CDs, and reducing the spread between the KPR and the refinancing rate. We will continue to monitor the impact on banks' behavior and the transmission of monetary policy as further changes are introduced, ensuring these are carefully calibrated while preserving hryvnia assets' attractiveness and monetary stability. Over time, consistent with the evolution of liquidity conditions, we may consider the introduction of instruments beyond an overnight maturity to achieve, among other objectives, an increase in the average maturity of our sterilization operations, while considering the implications for the primary government bond market.

Exchange Rate Policies

44. **Effective operationalization of the managed flexibility exchange rate regime has enhanced the FX market's capacity for self-balancing, and strengthens the exchange rate's role as a shock absorber while safeguarding reserves**. The exchange rate, while supported by FX interventions, fluctuates in both directions in response to market conditions, reflecting the effects of domestic and external shocks. Trading activity in the FX market has increased significantly, accompanied by a notable increase in its depth: since the transition to managed flexibility, transactions excluding the NBU's participation have more than tripled, and their share more than doubled. The spread between exchange rates on the cash and official exchange rates remained compressed within 2 percent in February-April 2024, thus aligning different FX market segments. In general, these developments help to reduce the FX market's sensitivity to short-term volatility and strengthen its ability to self-balance. Allowing the exchange rate to adjust to domestic and external shocks will enhance the resilience of the Ukrainian economy and FX market. We continue to monitor the FX market closely and to calibrate our FX intervention policy in order to ensure fulfilment of the program's objective of price and external stability, including consistency with the program NIR targets. Avoiding excessive exchange rate volatility under the managed flexibility framework will further help keep inflation and exchange rate expectations under control, thereby preserving confidence in the hryvnia and helping steer inflation toward the target over the NBU's forecast horizon. We will also continue to facilitate the functioning of the FX cash market to ensure a low and stable spread, in line with our Strategy, including by easing access to noncash FX and increasing cash FX supply depending on market conditions.

45. **We intend to maintain adequate FX reserves through the course of the program to safeguard external stability.** FX reserves remained robust in 2024Q1, given weaker than expected net FX demand in the early part of the year due to fiscal restraint, stronger than expected net exports, and lower private outflows, allowing us to comfortably meet our end-March ***Quantitative Performance Criterion*** on net international reserves. Notwithstanding these positive developments, we are requesting an adjustment of the floor on the NIR QPC for end-June 2024, primarily due to shifted timing of expected financing from the US. On the other hand, the new end-September and end-December 2024 PCs are set at a higher level than IT projections under the previous review to reflect improvements in external sector performance and the shifted timing of external financing, as well as our continued commitment to external sustainability.

46. **We continue to carefully adjust FX controls to support the economic recovery, while maintaining FX market stability and addressing national and international security considerations**. In line with our Strategy, we have cautiously eased FX controls, including most recently by easing restrictions on service imports, dividend repatriation, and external loan repayments, alongside facilitating international leasing and increasing fund transfer limits for

specific entities. These reforms are aimed at improving the investment environment, facilitating debt management, and promoting capital inflows into Ukraine, while considering assessments on macroeconomic conditions and outlook, and also ensuring consistency with the overall policy mix. We will continue to remain vigilant, proceeding with the FX liberalization roadmap under our Strategy to safeguard macroeconomic stability. To ensure the effectiveness of our liberalization efforts, we will continue to closely monitor the situation, including via bank-level data, to identify and address potential circumvention.

47. Our FX Strategy will continue to guide our decisions to gradually relax FX restrictions, as conditions allow. In March 2024, the NBU amended the necessary legislations in order to ensure the discretionary right of the NBU to approve FX permits for exemptions to the general rules on cross-border transactions set by Resolution #18. Our decisions to approve such individual permits will be consistent with the FX Strategy and the goal of safeguarding macroeconomic, financial, and external stability, and will be made in cases of exceptional importance to the state in wartime. On the issue of adjusting settlement periods for export and import transactions, we will work with relevant stakeholders to devise suitable solutions that balance facilitating business activity while ensuring the steady flow of export earnings, a vital element for the smooth functioning of the FX market, which is in turn crucial for successfully implementing currency liberalization measures.

48. No multiple currency practices (MCPs) have been identified since the Third Review. We commit to ensuring that that as we continue with our exchange rate transition and FX liberalization, multiple currency practices do not arise inadvertently.

NBU Independence and Governance

49. We remain committed to avoiding monetary financing. If unexpected critical needs arise or external disbursements are delayed, we will first explore additional measures, such as drawing down excess government deposits or tapping the government debt market. We will request monetary financing from the NBU only as a last resort and in strictly limited amounts, underpinned by a framework that has been mutually agreed between the MOF and NBU in consultation with the IMF, and for which a draft NBU resolution is underway. We will also avoid indirect forms of monetary financing that are outside the core functions of the NBU, such as through the directed provision of liquidity to banks for the purchase of government securities on the primary market. Direct financing of off-budget programs by the NBU will be avoided altogether. We have avoided, and remain committed to, avoiding monetary financing. Due to technical reasons, a fluctuation in accounts payable unrelated to budget execution caused a minor miss of the indicative target on the ceiling on general government direct borrowing from the NBU. The issue has since been resolved.

50. We remain fully committed to upholding the independence and institutional effectiveness of the NBU. A strong and independent NBU remains critical to achieving macroeconomic stability and will support the eventual transition back to an inflation targeting framework with a floating exchange rate.

- *Governance arrangements*. We will ensure strong governance arrangements within the NBU. We have further enhanced the MoU between the NBU and the MOF for servicing the government's obligations to the Fund by the NBU through the introduction of additional agreements and necessary contracts, as well as rigorous monitoring of the status of settlements between the MOF and the NBU.

- *Financial autonomy*. We will continue adhering to our profit retention rules and ensure that the distribution of NBU profits to the state budget takes place in line with procedures established by the NBU Law. We commit to refrain from using NBU profit for earmarked spending and will direct this revenue category to the General Fund of the State Budget. Finally, we recognize that costs incurred from monetary policy implementation via liquidity absorption (interest expenses on NBU CDs) are both necessary and justified to support macroeconomic stability in line with our mandate. These costs have now decreased in line with the recent monetary easing.

51. As part of our efforts to achieve our strategic goal of EU accession, we will continue to improve the conceptual framework and content of the NBU's financial reporting. We aim to provide reliable and relevant presentation of information, taking into account the purpose and unique features of the central bank's operations. With the help of technical assistance from the IMF and other partners, we will study the experiences of European national central banks, the legal framework for accounting and financial reporting in the European System of Central Banks (ESCB), and assess the NBU's readiness to transition to financial reporting in line with ESCB standards.

52. We intend to carefully unwind the unconventional measures undertaken to support price and external stability in wartime. Urgent wartime challenges have necessitated the use of several nonstandard measures by the NBU to support macroeconomic stability. We will strive to ensure that such measures are well-targeted, clearly communicated and time bound. For example, as the structural liquidity surplus unwinds, we will adjust the design of our monetary policy operational framework to better align with economic conditions, including assessing the merits of reverting to a corridor system. When conditions permit, we are committed to phasing out war-time measures. This will strengthen our monetary policy toolkit, safeguard NBU credibility and independence, and thereby support our goals to eventually return to a full-fledged inflation targeting framework with a floating exchange rate regime.

G. Financial Sector

53. Our wide-ranging emergency measures have preserved financial stability. We will continue to closely monitor developments in the financial sector and make adjustments as necessary. Despite the severe impact of the war, the majority of bank branches remain operational, online banking services are fully available to all clients with internet connectivity, the non-cash payment system is functioning normally, and liquidity is robust for most banks. To ensure the continuity of the banking network, we introduced "Power Banking" in late 2022, a network of over 2,000 bank branches across the country that are capable of providing banking services to clients even during prolonged blackouts. The licenses of eight small banks (around 4 percent of system net assets as of December-2023) have been revoked under Martial Law and one bank (also around 4 percent of system assets) was nationalized.

54. Recognizing the importance of a well-informed approach to supervision, the NBU continues to undertake detailed bank diagnostics. These are critical to ensure prudent and consistent valuation of banks' assets, informing triage and the modalities of eventual balance sheet cleanup.

- The NBU completed a resilience assessment of banks comprising 90 percent of system assets in December 2023. This asset valuation and solvency assessment found minor capital needs in five banks which have mostly been addressed. Four banks submitted capital management plans to close the approximately UAH 10 billion (US$260 million) gap as of end-2023 in two stages by March 2026. The findings of the NBU's 2023 banking system resilience assessment have been fully reflected in banks' regulatory ratios and financial statements. Starting in 2025, the NBU plans to resume annual resilience assessments, which will include asset quality reviews and stress testing under baseline and adverse scenarios and involve external auditors. We will prepare a prioritized interagency NPL resolution action plan by end-June 2024, which will be informed by the NBU resilience assessment.

- In line with the Terms of Reference adopted by the NBU in January 2023, we will: (i) complete an independent asset quality review (AQR) once conditions have stabilized; and (ii) carry out a subsequent bank viability assessment. The current prohibition on bank capital distributions will remain in place until after the independent AQR findings have been fully reflected in banks' regulatory ratios and financial statements.

55. We are determined to take the necessary steps to continue to preserve financial stability and limit the potential fiscal cost of any interventions. Our priorities will focus on continued preservation of financial stability whilst ensuring financial and operational readiness to respond adeptly to shocks. The NBU and Deposit Guarantee Fund (DGF) have prepared contingency plans to respond to further potential high-impact events in their respective areas, in consultation with key stakeholders and IMF staff. The Financial Stability Council has approved those plans related to preparation for potential adverse rulings from the constitutional challenges against the DGF Law and an updated contingency plan to prepare for litigation risks concerning past bank resolution decisions. We will continue to monitor developments and update these plans as needed.

56. The DGF, MOF and NBU will prepare a bank rehabilitation framework in consultation with IMF staff (*Structural Benchmark*, end-December 2024). It will include: (i) measures to strengthen operational readiness, including regularly updated bank recovery and contingency plans; (ii) improving procedures to apply resolution tools for insolvent banks and early intervention measures, including temporary administration for anti-crisis management to close key outstanding gaps by end-December 2024; (iii) revive the work of the NBU-DGF coordination committee to improve information sharing between the NBU and DGF to foster cooperation and functioning of the two institutions; and (iv) review of financial backstop mechanisms and any improvements needed to the DGF's financial position. In addition, the NBU will align its frameworks for counterparty eligibility in monetary policy operations with international best practice and their coordination with lender-of-last-resort operations with international best practice. The framework preserves the progress under past reforms and takes into account the longer-term goals related to EU accession.

57. We will refrain from making any changes to the allocation of roles and responsibilities of financial safety net stakeholders during Martial Law. The current financial safety net design is heavily shaped by reforms undertaken under past Fund-supported programs and has served Ukraine well during crisis times. The DGF plays an important role in Ukraine's financial safety net by safeguarding deposits and addressing insolvent banks. We recognize that maintaining its current role in the financial safety net is therefore essential. In consultation with IFIs, (i) we will appoint a new Managing Director when the position becomes vacant in July 2024; and (ii) a subcommittee of the Financial Stability Council will review DGF governance arrangements, including of the Administrative Board, internal controls, and the procedures for the appointment of the Managing Director, and prepare legislative proposals to close gaps relative to good practice by end-March 2025. The new appointment procedures will include the engagement of an independent HR firm to assist with the selection process and introduce a nomination committee comprised of voting representatives and IFIs as observers.

58. Our decisions will be consistent with our overall strategy to reduce state ownership in the banking sector. Any decision that has the potential to increase state ownership in the banking sector will be taken in consultation with IMF staff and be strictly limited to matters related to preserving financial stability and national security decisions during the Martial Law period. All systemic banks with majority state ownership will fall under the responsibility of the MOF, and any non-systemic banks that come under state ownership will not be recapitalized using fiscal resources and will be transferred to the DGF for resolution upon breach of prudential requirements **(*Continuous Structural Benchmark*)**. We are considering how to include our vision for state-owned banks and financial institutions in our Financial Sector Strategy. In the immediate future, the key steps are as follows:

- Preparing and implementing a framework to inform decisions on any additional banks that come under state control, which aims to preserve value, ensure effective operational management, and reach decisions on the future of such banks.

- We will continue to undertake analysis on the state of the banking system and wartime developments and needs. Informed by the NBU resilience assessment, we developed capital management plans and adjusted the business plans of SOBs needing capital increase to meet the requirements. Once the independent AQR is concluded, we will use its results to update the general SOB strategy and subsequently, strategies for individual banks with majority public ownership, including with respect to privatization (in line with our Financial Sector Strategy).

- In preparation for privatization of banks with majority public ownership, we prepared a draft law on SOB privatization in consultation with IFIs and will submit it to Parliament by end-September 2024. We are also preparing two systemic state-owned banks for sale, Sense Bank and Ukrgasbank. We are planning to appoint an internationally recognized financial advisor by end-September 2024 using a transparent procedure and in consultation with IFIs.

- The Ministry of Economy will develop strategies for the Ukrainian Financial Housing Company and Export Credit Agency in consultation with the Ministry of Finance by end-November 2024 to align with the general targets of financial sector development.

59. We will take further steps to align financial and credit market infrastructure with international good practice.

- *Financial reporting*. We will restore the legislative obligations to submit financial statements and audit reports for financial institutions for the 2023 financial year and for business entities located outside the occupied territories for the 2024 financial year. In anticipation of this change, the NBU has fully restored prudential reporting requirements for NBFIs. To improve the quality of financial reporting in the non-banking financial services market, we will restore by end-September 2024 the requirements for mandatory quality control of services provided by audit companies, including the verification of audit reports prepared to comply with the requirements of the law.

- *Bank capital rules.* In recognition of the importance of preparing for EU accession, the NBU issued a regulation to align banks' regulatory capital structure with the EU Capital Requirements Directive and Regulation in December 2023. With the continued support of the World Bank, we will close key gaps in minimum capital requirements by end-June 2025 and other gaps thereafter. The implementation of the new requirements will be phased to facilitate banks integrating them into their business plans. The NBU will continue monitoring prevailing economic conditions and relax controls and reinstate pre-war regulations when it is safe to do so and based on banks' adherence to the new capital requirements aligned with EU standards.

- *Property valuations law*. In recognition of the need for prudent (fair) valuation of real estate and bank collateral for all economic entities and public authorities, the State Property Fund (SPF) will close the gaps with international standards in consultation with the NBU, NSSMC and IFIs, and: (i) by end-August 2024, in coordination with the World Bank, will develop provisions that will improve the draft amendments to the law registered in Parliament "On Valuation of Property, Property Rights and Professional Valuation Activities in Ukraine" (#7386) that closes the gaps with international valuation standards, and (ii) by end-December 2024, propose an implementation roadmap that includes transitional arrangements, details of supportive regulation and/or guidance, steps to strengthen the valuers' profession including additional training requirements for valuation of financial assets (banking assets, insurance assets and collateral), and creation of a register of valuations for financial assets.

- *Immovable property databases and indices*. In March 2024, the NBU and Ministry of Justice prepared a detailed proposal in consultation with key stakeholders to increase the transparency of the real estate market for participants (including international investors), strengthen systemic risk analysis and mitigation, and bank collateral valuations. This proposal includes conditions, details, and timelines for introducing: (i) a publicly accessible database of real estate transaction prices with detailed metadata including structural parameters of primary and secondary market; and (ii) residential and commercial property price indexes. Based on this proposal, the Ministry of Justice and the NBU will continue to implement reforms within the timeframe planned in the proposal to launch databases and publish the indices in 2025.

- *Virtual assets*. Virtual assets pose risks to price stability, the effectiveness of monetary transmission, and tax revenue in the absence of a strong legal framework. The NBU and NSSMC will prepare an update of the legislation with input from IMF technical assistance and in consultation with IMF staff by end-December 2024 to align with international best practice while considering economic development goals and mitigating price and financial stability risks.

- *Non-performing exposures*. The NBU, in consultation with IFIs, aligned the definition of non-performing exposures with Article 47a (non-performing exposures) and Article 178 (Default of an obligor) of Regulation EU 575/2013 of the European Parliament and the EU Council of 26 June 2013. The amendments will come into force from January 1st, 2025, and will strengthen monitoring by supervisors and banks.

- *NBU's status as a secured creditor*. We will strengthen the NBU's status as a secured creditor in line with the IMF's Safeguards Assessment Report. We will submit to Parliament by end-December 2024, law amendments that reflect the NBU and the DGF's coordinated position and that aim at strengthening the NBU's status as a secured creditor of banks by improving the mechanisms for extraordinary satisfaction of the NBU's claims through collateral, management, and sale of collateral.

60. We are fully committed to further strengthening banking supervision.

- *Recent developments*. We took the following actions in 2023: (i) separated the related-parties unit from banking supervision; and (ii) strengthened Supervisory Committee decision-making by implementing "supervisory panels" as a consulting body to the Committee that provides additional independent review by relevant subject matter experts; and (iii) in recognition of the critical importance of onsite inspections, we have resumed scheduled inspections for both banking and non-banking institutions, while ensuring NBU discretion on matters related to staff safety. We will undertake a survey of the effectiveness of the new supervisory panels by end-September 2024 in consultation with IMF staff.

- *Transition to risk-based supervision*. The NBU will prepare and implement a supervisory risk assessment methodology to inform supervisory engagement priorities (***Structural Benchmark*, end-December 2024**). We will apply this methodology to all banks and prepare a supervisory action plan by end-December 2024. We will also adjust the organizational structure for bank supervision to leverage efficiencies as we transition to a risk-based approach; continue to develop expertise for effective supervision, in particular, for supervision of information and communications technology risks as part of operational risk; and further improve the professional capacity of bank supervision, which will include the development of professional profiles needed and a multi-year training program for new hires.

- *AML and Banking Supervision*. The NBU will continue strengthening risk-based AML/CFT supervision of banks, payment service providers and non-bank financial institutions, particularly in relation to corruption, tax crimes and illegal gambling. By end-December 2024, we will amend Article 32 of the AML/CFT law and corresponding amendments to Article 73 of the Banking Law to ensure that the penalties for AML/CFT violations by entities regulated and supervised by the NBU are effective, dissuasive, and proportionate, in line with the FATF standards. The financial sanctions applied to such entities will be established by the laws of Ukraine and the regulatory legal acts of the National Bank of Ukraine.

- *Supervision of banking hybrid business models*. We recognize the growing importance of banks' hybrid business models, specifically Banking-as-a-Service, a model in which banks integrate their digital banking services directly into the products of other non-bank businesses. The NBU in consultation with the IMF will propose a supervisory framework that will incorporate the specific risks of such business models based on international best practices by end-August 2024.

- *Transfer of bank ownership*. We commit to ensuring that any future transfers of bank ownership, including following seizures during Martial Law, can only take place with due regard to the Law of Ukraine on Banks and Banking and following formal notification, review, and approval of the process by the NBU.

61. We will strengthen the legal, regulatory, and supervisory framework for non-bank financial institutions (NBFIs) and financial markets.

- *Legal framework*. In December 2021–July 2023 we passed legislation on Financial Services and Financial Companies (#1953), Insurance (#1909) and Credit Unions (#3254). Most provisions of these laws came into force in January 2024 and the NBU has prepared implementing regulations. Rules for insurance intermediaries apply from January 2025, and Solvency II will apply from January 2027. The NBU and DGF plan to initiate the development of a deposit insurance framework for credit unions and a guarantee framework for life insurance companies after Martial Law is lifted, and once the regulations required for enforcing the new laws are put into effect.

- *Capital and reporting requirements*. To further strengthen the NBFI market, the NBU increased capital requirements for financial companies in December 2023 and has provided a six-month transition period for existing entities to align their operations with the new requirements. The NBU will also prepare a supervisory risk assessment methodology by end-September 2024 that distinguishes between the types of NBFIs with the aim to transition to a risk-based supervision approach for NBFIs. The NSSMC will prepare draft regulation for financial intermediaries by end-December 2024, which will bring their capital requirements in line with the EU acquis.

- *Payments market*. Draft law (#11043) that will strengthen regulatory requirements for market participants has passed the Parliamentary committee stage and is ready for the first reading. It aims to align with the EU payment services directive (PSD2, 2015/2366) and international good practice. We will aim to adopt the law by end-September 2024. To prioritize supervisory activities of payment service providers we will in consultation with IFIs: (i) prepare a concept note for a supervisory risk assessment methodology by end-August 2024 and implement the methodology by end-December 2024; (ii) develop the reporting system; (iii) strengthen supervision capacity through hiring specialists and building analytical competence; (iv) prepare a concept note by end-June 2024 on regulatory requirements for person to person (p2p) and other such electronic payments with the aim of identifying and restricting abnormal behavior and implement the reforms as quickly as possible; and (v) develop a concept note by end-August 2024 on the establishment of a public register to record card holder and merchant violations, and its potential use by market participants and government agencies such as cyber police, SSU, ESBU, and SFSU. We will implement supporting regulation by end-December 2024.

- *Capital market regulation and harmonization with IOSCO principles*. Law (#3585) on the National Securities and Stock Market Commission (NSSMC) which enhances the NSSMC's powers, independence and institutional capacity, and its cross-border and domestic cooperation mandate was enacted in April 2024. The law considers the mandate of other regulators, and we will move swiftly to align with IOSCO principles by conducting the screening process to become a signatory of IOSCO's multilateral MoU by end-December 2024 with full implementation of the other provisions of the law by end-December 2025. The NSSMC will take steps to enhance the operational efficiency of NBU's capital controls in consultation with the NBU, including through regulatory harmonization and aligning capital flow restrictions for securities accounts with those applied to bank accounts by end-December 2024.

- *Related parties*. The NBU will extend the powers of its related-parties supervision unit to NBFIs by end-August 2024. This will include increasing the resources of the unit, and designing a new internal database and tools for effective related-parties identification. The NBU, in consultation with IFIs, will propose draft amendments to the Law on Banks and Banking by end-July 2024 to take into account supervisory observations in the recognition of related parties.

- *Insurance transparency*. We adopted a regulation in February 2024 that requires auditors to confirm that insurers have acceptable assets and to assess their value for the 2023 financial year. We will also assess the feasibility of updating the disclosure requirements for insurance and reinsurance brokers by end-December 2025.

62. In recognition of its important catalytic role in post-war economic recovery, we will take steps to enhance credit and financial market infrastructure:

- *Capital market infrastructure.* Mechanisms are needed for foreign investors to directly access marketable debt instruments beyond government securities. The NBU, NSSMC and MOF in consultation with IMF and other IFIs have proposed priority actions for enhancing the capital market infrastructure. In a first phase, the NSSMC will approve the NBU regulation allowing the NBU to extend the NBU Clearstream link by end-July 2024 to facilitate access of foreign capital to municipal bonds and other Ukraine reconstruction-related debt instruments. In a second phase, the NSSMC, National Depositary (NDU), and NBU with IMF technical assistance will target establishment of a direct link between the Central Securities Depository (CSD) and foreign CSDs by end-July 2025 to expand foreign investors' access to a broader range of instruments and markets. The NBU, NSSMC, and MOF will by end-August 2024 propose further measures aimed at enhancing capital market infrastructure.

- *War risk insurance system*. The NBU, together with the Ministry of Economy and Ministry of Finance, will prepare an initial draft law establishing a fully functional war insurance system by end-June 2024.

- *Financial inclusion.* The ongoing war is adversely impacting access to financial services for both households and enterprises in the areas close to the armed conflict zone, in the liberated territories, as well as for certain groups of the population. The war is also restricting IFIs' ability to comprehensively assess financial inclusion developments and priorities. We will collate fresh data using a best efforts approach and update our financial inclusion strategy in consultation with IFIs by end-July 2024. We will encourage financial institutions to do more to meet the needs of vulnerable clients and to reintegrate de-occupied territories. The NBU will prepare by end-July 2024 a legislative draft proposal for a specialized and restricted banking license which aims to quickly tackle growing financial inclusion challenges by leveraging on existing infrastructure. These specialized banks will: (i) be subject to the full extent of the Law of Ukraine on Banks and Banking; (ii) participate in the Ukraine deposit insurance scheme; (iii) have limits imposed on lending and funding operations. The proposal will be prepared in consultation with key stakeholders and IFIs, and with due regard to international good practice.

- *Lending development strategy*. We have prepared a strategy to support bank lending in consultation with IFIs that aims to provide a unified policy approach to support fresh credit. It is focused on targeting subsidized lending instruments to key priority sectors during the war and further developing credit infrastructure to support banks' risk management and lending decisions. We aim to submit to the FSC for approval in June 2024. NBU regulation and supervision will continue to apply to institutions that provide financial services to a large volume of clients and any authorities or agencies mandated with improving the lending infrastructure will adhere to the approved strategy.

- *Responsible consumer lending*. To strengthen borrowers' rights, improve information exchange, and encourage responsible lending, we submitted to parliament in February a draft law on improving state regulation and the functioning of credit bureaus. We will take the necessary steps to facilitate the adoption of the law by Parliament by end-September 2024. We will also enhance the supervision of credit bureaus by establishing requirements for ownership and internal controls within six months of the law being adopted by the parliament and signed by the President.

- *Monetary derivative instruments*. To hedge foreign exchange and interest rate risks and improve monetary transmission, the NBU in consultation with IFIs, including via technical assistance, will prepare a concept note by end-October 2024 that will set out the steps, conditions and timing needed to introduce and develop the derivative financial instruments (including forwards) market.

63. Finally, we will continue our efforts to recover value from former shareholders of failed banks. We reconfirm our commitment to continue efforts to recover value from assets of failed banks and to abstain from any interference with the current asset recovery strategies of the largest bank nationalized in 2016 and of the DGF.

H. Governance and Anti-Corruption

Governance of Reconstruction

64. Our strategy for post-war reconstruction will meet the highest standards of transparency and accountability. In coordination with international partners, we plan to take full advantage of digital technologies in implementation of the full cycle of public investment projects, providing timely information to transparently track and analyze related projects throughout the whole project cycle from planning to implementation, including procurement processes and expenditures. We will achieve this through developing a single digital ecosystem for PIM based on the updated Ministry of Economy's Prozorro digital procurement system, the Ministry of Finance's IT systems for planning and execution monitoring of state and local budgets and IFI projects, the Ministry of Infrastructure's Digital Restoration EcoSystem for Accountable Management (DREAM) and other relevant systems and registries. We will also explore the scope to publish the breakdown of costs for public construction projects to ensure transparency following the public procurement process. Comprehensive audits of the use of reconstruction funds, performance audits of selected individual projects (including project costs, deliverables and outputs), and timely publication of audit reports will also be key features of the reconstruction strategy. Our strategy will integrate and implement mechanisms to prevent and identify corruption risks, and cases will be referred, as appropriate, for follow-up by the anti-corruption institutions. In line with their memorandum of understanding, the NABU and the State Agency for Restoration and Development will continue cooperation efforts and exchange of information to prevent and detect corruption.

65. We will undertake efforts to enhance the institutional independence and effectiveness of key audit institutions to ensure that public funds, particularly for reconstruction and recovery, are used for their intended purposes and any misuse is prevented or detected. In this respect, a law will be enacted by end-December 2024 to enhance the independence (organizational, functional and financial), mandate and effectiveness of the Accounting Chamber of Ukraine (ACU) to fulfill its constitutional oversight function over public expenditures in line with standards of the

International Organization of Supreme Audit Institutions, and audit all public funds (including budgets of local government agencies, SOEs and off-budget funding). In particular, the law will: (i) enhance its independence including strengthening the selection process for ACU members for an open, transparent, credible and competitive procedure; (ii) enable the ACU to select the scope of the audit free from any direction or interference and to have full and timely access to all relevant information and databases to perform its audit functions; (iii) empower the ACU to exercise external audit function on all public funds (including funds or budgets of local government agencies, SOEs and off-budget funding); and (iv) establish formal procedures in the legislature for reviewing and monitoring external audit reports and following up on audit recommendations with commensurate financial and technical resources. More broadly, we will continue to safeguard the financial independence of the ACU, consistent with its role and constitutional independence.

Anti-Corruption and Rule of Law

66. Our reform agenda on anti-corruption aims at effectively combatting corruption, sustaining public confidence in the rule of law, and advancing towards our goal of EU membership. We remain firmly committed to preserving independent, competent, and trustworthy institutions to combat high-level corruption. We will preserve the hard-won advances on building an independent and effective anti-corruption infrastructure and prevent any backtracking from progress made.

67. We remain committed to strengthening the effectiveness of anti-corruption institutions.

- To strengthen effective procedures for corruption investigations, further amendments to the Criminal Procedural Code will be enacted, including (i) to enable the Prosecutor General to delegate to the SAPO the management of extraditions and mutual legal assistance requests in relation to corruption investigations, (ii) remove the mandatory dismissal of pre-trial investigations due to the lapse of time limits of pre-trial investigation after notice of suspicion, and (iii) upon expiration of the time limits and motion of the defendant or affected parties, give the investigating judge authority to compel in a timely manner the prosecutors to decide on the pre-trial investigation (either close the proceeding or complete the pre-trial investigation), or reject the motion, with the aim of appropriately balancing the objectives of prompt and comprehensive investigations of criminal offenses and protection of rights of parties in criminal proceedings **(*Proposed Structural Benchmark,* end-October 2024).**

- As provided for in the law, the external audit of the NABU's effectiveness with participation of three independent experts with international experience will be completed and its report published **(*Structural Benchmark,* end-September 2024)**. The Cabinet of Ministers have engaged with international partners on the nomination of independent experts for the planned NABU's external audit, and will, as necessary, provide further support to this external audit commission, once the external auditors are nominated and appointed. To effectively implement the law empowering the NABU to intercept communications (wiretapping), we will develop an implementation plan in the post-Martial Law period to provide resources, equipment and technological solutions for the NABU to independently intercept communications of landlines and mobile devices. Discussions between the NABU and law enforcement agencies are ongoing on the development of the implementation plan. Consistent with our broader reform plans for the forensic expert system for criminal law enforcement, we will ensure that the NABU by end-October 2024 has access to independent and competent forensic experts, to enable it to effectively conduct its investigative mandate, including investigating complex corruption schemes. We will also enact by end-November a law to enhance corporate criminal liability (applicable to private and public legal entities either resident or non-resident in Ukraine) with international standards to support the country's efforts towards accession to the OECD Anti-Bribery Convention.

- We have initiated the process for nominating and appointing new members of the Public Council of International Experts (PCIE), which will vet candidates to the 24 new vacancies to the High Anti-Corruption Court (HACC) both at the first instance (15 vacancies) and appellate (9 vacancies) levels. We will prolong the mandate of the PCIE by another year, given its expiry in October 2024, as more time is needed to finish the ongoing selection process of new HACC judges. We will ensure the open and competitive selection for these new vacancies and adequately provision for their staffing and office needs. Final appointments to the HACC will be completed by end-September. To enhance its efficiency and facilitate hearings, amendments to the procedural code were enacted in May 2024 (shortly after the end-April target date) to rationalize matters or issues to be heard at the first instance by one HACC judge or by a panel of three HACC judges based on the severity of the penalty **(*Structural Benchmark,* end-April 2024, not met, implemented with delay)**. In this regard, we will also assess the potential impact on judicial efficiencies and resources to all criminal courts by the inclusion of a list of high-level public officials, whose cases would automatically be heard by a panel of judges (regardless of the penalty), and implement corrective measures, as warranted.

68. The NBU is ensuring that risk-based implementation of AML tools helps prevent, detect, and deter the laundering of proceeds of corruption. Following the legal amendments to the definition of politically exposed persons (PEPs), the NBU is proceeding to conduct a thematic inspection of the selected financial institutions' compliance with enhanced customer due diligence on PEPs by end-June 2024. By end-August 2024, the NBU with IMF capacity development support will issue guidance for financial institutions and other covered non-bank institutions, consistent with the FATF standards, on the application of a risk-based approach regarding PEPs, which will include relevant case examples. In this regard, we are committed to invest in building the capacity of new and existing NBU staff to improve organizational performance, remain flexible and respond rapidly to changes and challenges in the AML/CFT framework. We will also improve the effectiveness of the beneficial ownership regime to enhance transparency in public procurement, detect conflicts of interest through transparent ownership structures, and prevent the misuse of companies. In this regard, the Ministry of Justice will further simplify procedures and update software by end-September to facilitate submission by companies of their beneficial ownership information, which continues to be publicly available in the Unified State Register of Legal Entities, Entrepreneurs and Public Associations. By end-December 2024, we will also enhance processes for obtaining adequate, accurate and up-to-date beneficial ownership information and designate a competent authority to conduct risk-based verification of the information.

69. We are committed to advancing the rule of law and judicial reforms. Following the dissolution of the Kyiv District Administrative Court in December 2022, we will enact a law to establish the High Administrative Court of Ukraine (with first instance and appellate chambers) that will hear administrative cases against national state agencies (e.g., NBU, NABU, NACP) by judges who have been properly vetted for professional competence and integrity with decisive and crucial vote of independent experts with international experience in the PCIE **(*Structural Benchmark,* end-July 2024, proposed to be reset to end-December 2024)**. In particular, the new court will have authority over cases belonging to the competence of the liquidated Kyiv District Administrative Court in relation to the appeal of acts of national state agencies the power of which extend to the entire territory of Ukraine, in addition to the administrative cases against procedures of selection commissions and external audit commission that include participation of independent experts (such as NACP, NABU, and SAPO).

Corporate Governance in SOBs and SOEs

70. We will continue to strengthen the governance of state-owned banks (SOBs). We remain committed to upholding the spirit of corporate governance reforms in SOBs and ensuring their operation on a professional and commercial basis, without political interference on operational matters. We appointed a fresh slate of independent supervisory board members to the SOBs in the first half of 2023 and the NBU applied its fit and proper assessment framework to selected candidates. Upon completion of the selection process in this cycle, we have assessed the effectiveness of the new procedures and will make some minor adjustments to procedures in consultation with IFI stakeholders. We will also implement a procedure for conducting performance assessments for all SOBs in 2024. The first such performance assessment will be conducted for each of the banks in early 2025. In August 2025, the MOF will publish the key findings of its first annual assessment, together with the CMU's proposed actions to address the findings.

71. We will continue to strengthen SOE corporate governance.

- We are working on implementing law #3587-IX (formerly draft law #5593-D), which entered into force in March 2024 to bring the SOE corporate governance framework broadly into line with OECD Guidelines on Corporate Governance of SOEs, while also mitigating fiscal risks. This includes, in particular, secondary legislation to operationalize SOEs' financial planning process, including financial indicators designed with the help of IMF TA that are consistent with the gatekeeper role of the MOF from a budget financing and PFM perspective to limit quasi-fiscal risks and safeguard debt sustainability. The implementation of #3587-IX will also include a revamped nomination process and effective independent evaluation procedure for SOE supervisory boards, consistent with OECD standards.

- We remain strongly committed to energy corporate governance reforms, including to ensure an independent evaluation of the GTSO supervisory board one year after its appointment. We are currently developing a framework procedure for supervisory board assessment and commit to launch an independent evaluation of the supervisory boards of Naftogaz and Ukrenergo in October 2024 and to conclude it by end-December 2024.

72. We are exploring options, in close consultation with international partners, to strengthen SOE management through the existing SOE corporate governance reform agenda. Drawing on best practices and putting it into the context of the ongoing SOE corporate governance reforms, we will clearly define the scope and mandate of options for strengthening SOE management, such as centralized modes, including defining the roles and mandates of key government institutions engaged in management of SOEs, such as the MOF, MOE, CMU, and the State Property Fund (SPFU). To start with, we continue to adhere to the following SOE reform agenda after adoption of #3587-IX (as discussed in ¶71) and policy sequencing in close consultation with international partners, which are all essential preconditions for strengthening SOE management, including: (i) implementing related secondary legislation for #3587-IX, including establishing a methodology for and subsequently conducting regular independent evaluations of SOE supervisory boards; (ii) as an interim step, assessing the financial conditions and fiscal risks of the SOEs in the state ownership policy by end-July 2024; and (iii) producing a comprehensive state ownership, dividend policy and privatization strategy ***(Structural Benchmark,* end-October 2024*)***. More broadly, we will also assess the financial viability of key SOEs as an input to developing a framework to deal with quasi-fiscal costs, including legacy Public Service Obligations (PSOs).

73. The SOE state ownership policy, which will serve as a critical input and pre-condition into the triage and privatization strategy of SOEs, will include the following elements:

- Long-term priorities of SOE state ownership; SOE public policy objectives and rationales for SOEs in state ownership (subject to regular reviews); the state's role in the governance of SOEs and its implementation (including roles and responsibilities of involved government agencies).
- Criteria of financial viability of SOEs, financial assessment of SOEs (including contingent liabilities, debts and risks to public finances); critical gatekeeper role of Ministry of Finance to safeguard public finances and debt sustainability (via tracking financial viability of SOEs and fiscal risk analysis).
- Dividend policy (e.g., rationale, sectoral policy, impact on public finances, and post-war strategy) and remuneration policy for Board members and managers.

Energy Sector Reforms

74. Our immediate priority is to contain the adverse impact of the war on the energy sector. We remain strongly committed to implementing, once conditions allow, a timely and ambitious energy reform agenda to address long-standing structural problems in the energy sector that have been exacerbated by the war.

- Recent large-scale attacks on our energy infrastructure and electricity generation have destroyed around a half of our generating capacity, especially thermal and hydroelectric power, with damage exceeding US$1 billion during the spring. We are working swiftly to repair the damage and to ensure sufficient electricity provision to households and firms across the country. We will also aim to make our energy system more resilient to future attacks, including through decentralized energy generation in a conducive market and regulatory environment. Affected companies will mostly rely on their working capital to conduct the repairs, while we are grateful for donor support, including on equipment. We may need additional financial assistance by donors to support decentralized electricity generation support programs. Meanwhile, we have increased the electricity tariffs for households by up to 64 percent as of June 1, 2024, bringing tariffs closer to cost recovery levels and adjusting incentives for electricity usage during the heating season.

- Potential reform measures, once conditions allow, include additional gradual tariff increases (subject to a new tariff methodology and social considerations during the war), securing external financing, and providing transparent and exceptional direct budget support to energy SOEs pending available budgetary resources. Once the war winds down, the reform agenda in the energy sector will, inter alia, require restoring and enhancing competition in wholesale and retail gas markets. Furthermore, ensuring the sustainability of the system and reducing quasi-fiscal liabilities will necessitate a gradual increase in gas and electricity tariffs towards cost recovery, while allocating adequate and well-targeted resources to protect vulnerable households. The CMU will adopt a roadmap for the gradual liberalization of gas and electricity markets, with a time-bound implementation plan for the post Martial Law period. The roadmap will be based on technical analysis of the financial condition of the sector, in coordination with the European Commission.

- Restrained domestic consumption and growing domestic production limited the need for gas imports during the past heating season. For the next heating season in 2024/25, we do not plan additional gas imports for domestic consumption, including due to Naftogaz's expanded production capacity, but up to 3 bcm of additional gas for storing by non-residents for EU country needs could occur under the baseline. Naftogaz has secured additional financing for gas imports through the EBRD and bilateral donors. If Naftogaz faces a liquidity shortfall, we will assess the amount of PSO compensation in 2024 based on actual documentary proven expenditures of Naftogaz verified by the State Audit Service and other stakeholders. The relevant calculations will be finalized by end-August 2024. The potential spending pressure from gas imports and PSO compensation will be accommodated through an adjustor on fiscal balance targets, subject to the above assessment, the findings of the stock of arrears of District Heating Companies (DHCs) based on a desk audit (see below), available financing, and capped at UAH 60 billion (about 1 percent of GDP).

- The updated strategies of the GTSO and transmission industry appropriately reflect the new operating environment by seeking to rightsize the system and identifying alternative sources of gas supply. This will be critical for the GTSO to prepare financially and operationally for the zerotransit scenario when the transit contract expires at end-2024. In particular, we will adopt draft law #6133 by end-June that allows for a special regime of operations for GTSO to reduce its operational expenditures and maintenance for non-critical gas transmission purposes.

- Consistent with our commitments to the EU and other international partners, we will ensure the independence of the National Energy and Utilities Regulatory Commission (NEURC), which plays an important role in efforts to integrate the Ukrainian energy market with the EU, to attract needed FDI and advance the envisaged decentralization of power generation, and thus help make the energy system more resilient to missile attacks. Specifically, in order to align the Law of Ukraine 'On the NEURC' with European legislation to ensure NEURC's functional independence, we will adopt amendments to the law #3354-IX by end-December 2024 to exempt regulatory decisions by NEURC from the state registration procedure and also to implement Article 5 of the Law of Ukraine 'On the NEURC' prohibiting state bodies from interfering with NEURC's activities. We will ensure the appointment of NEURC's Commissioners by end-September 2024 based on the results of the competition carried out in line with the norms of the Law of Ukraine 'On the NEURC.'

- District Heating Companies (DHCs) have accumulated a significant stock of arrears to Naftogaz before and since the start of the war, as a result of accumulated tariff differentials and the impact of the war. We will tackle this issue comprehensively once war-related pressures on the budget subside by developing a new tariff methodology. In the interim, we will analyze the debts and financial conditions of DHCs through a desk review, by a reputable audit firm, which will analyze the debts before and after February 2022 (***Structural Benchmark,*** **end-June 2024, proposed to be modified and reset to October 2024**). This will help clarify the stock of arrears and the financial situation of DHCs, including the drivers of the arrears' accumulation, ahead of the 2024/25 heating season.

I. Program Monitoring

75. Program implementation in 2024 will be monitored through quarterly reviews via quantitative performance criteria, indicative targets, and structural benchmarks. We commit to provide to IMF staff all the data needed for adequate monitoring of the program, including as detailed in the attached TMU. The complete schedule of reviews is presented in the companion staff report, and quantitative conditionality is detailed in Table 1. The program will also be monitored through the continuous performance criterion (PC) on the non-accumulation of external payments arrears and standard continuous PCs. Structural Benchmarks described in this MEFP are summarized in Table 2. The fifth, sixth, and seventh reviews are expected to take place on or after September 1, 2024, December 1, 2024, and March 1, 2025, respectively, based on quantitative performance criteria for end-June 2024, end-September 2024, and end-December 2024, respectively, and corresponding structural benchmarks.

Table 1. Ukraine: Quantitative Performance Criteria and Indicative Targets

(end of period; millions of Ukrainian hryvnia, unless indicated otherwise)

	Mar 2024					Jun 2024		Sep 2024		Dec 2024		Mar 2025		Jun 2025
	QPC	Adjustor	Adjusted QPC	Actual	Status	QPC	Proposed Rev. QPC	IT	Proposed QPC	IT	Proposed QPC	IT	Proposed rev. IT	Proposed IT
I. Quantitative Performance Criteria 1/ 2/														
Floor on the non-defense cash primary balance of the general government, excluding budget support grants (- implies a deficit) 2/	135,000	0	135,000	241,901	Met	250,000	250,000	368,313	368,313	415,410	415,410	330,000	310,000	660,000
Floor on tax revenues (excluding Social Security Contributions)	426,300	…	426,300	507,992	Met	880,400	880,400	1,398,600	1,398,600	2,042,250	2,042,250	485,000	485,000	850,000
Ceiling on publicly guaranteed debt	47,900	5,879	53,779	5,879	Met	47,900	47,900	47,900	47,900	47,900	47,900	53,626	53,626	53,626
Floor on net international reserves (in millions of U.S. dollars) 3/	28,400	-134	28,266	31,408	Met	26,800	25,300	27,900	28,800	24,900	26,300	26,000	23,800	24,800
II. Indicative Targets 1/ 2/														
Floor on the cash balance of the general government, excluding budget support grants (- implies a deficit)	-344,485	0	-344,485	-211,020	Met	-725,996	-725,996	-1,123,107	-1,123,107	-1,557,208	-1,557,208	-215,000	-215,000	-370,000
Ceiling on general government arrears	2,000	…	2,000	1,514	Met	2,000	2,000	1,800	1,800	1,600	1,600	1,600	1,600	1,600
Floor on social spending	130,000	…	130,000	142,139	Met	262,500	262,500	390,000	390,000	537,800	537,800	135,000	130,000	250,000
Ceiling on general government borrowing from the NBU 4/ 5/	-9,500	0	-9,500	-9,392	Not met	-2,884	-2,884	0	0	0	0	-984	-984	-4,100
III. Continuous performance criterion 1/ 2/														
Ceiling on non-accumulation of new external debt payments arrears by the general government	0	…	0	0	Met	0	0	0	0	0	0	0	0	0
IV. Memorandum items														
External project financing (in millions of U.S. dollars)	476	…	…	186	…	861	251	1,200	605	1,497	1,496	326	142	426
External budget financing (in millions of U.S. dollars) 6/	9,267	…	…	9,210	…	16,825	12,936	25,654	25,745	32,414	32,565	5,183	4,236	10,794
Budget support grants (in millions of U.S. dollars)	1,017	…	…	980	…	4,942	1,050	10,474	10,506	12,082	12,114	1,735	429	965
Budget support loans (in millions of U.S. dollars) 6/	8,250	…	…	8,230	…	11,883	11,887	15,180	15,239	20,332	20,451	3,447	3,807	9,830
Interest payments	49,500	…	…	44,966	…	161,780	161,780	284,320	284,320	429,820	429,820	117,831	67,000	190,600
NBU profit transfers to the government	30,000	…	…	0	…	38,000	38,000	38,000	38,000	38,000	38,000	0	0	34,400
Government bonds for the purposes of bank recapitalization and DGF financing	0	…	…	0	…	0	0	0	0	0	0	0	0	0
Spending from receipts resulting from sales of confiscated Russian assets and transfers of bank accounts	0	…	…	0	…	0	0	0	0	23,743	23,743	0	0	0
Spending on gas purchases, PSO compensation and transfer to GTSO	0	…	…	0	…	0	0	60,000	60,000	60,000	60,000	0	0	0
Cash balance of the general government, excluding budget support grants, treasury report at current exchange rates (- implies a deficit; in billions of Ukrainian hryvnia)	-262.4	…	…	-221.2	…	-671.7	-671.7	-1,046.6	-1,046.6	-1,562.1	-1,562.1	-212.2	-181.8	-363.6

Sources: Ukranian authorities and IMF staff estimates and projections.

1/ Definitions and adjustors are specificied in the Technical Memorandum of Understanding (TMU).

2/ Targets and projections for 2024, and 2025 are cumulative flows from January 1, 2024, and 2025, respectively.

3/ Calculated using program accounting exchange rates as specified in the TMU.

4/ From end of previous quarter.

5/ For June, 2024 onwards, calculated using the projected redemptions of government bonds as of May 15, 2024.

6/ Excludes prospective IMF disbursements under the EFF.

Table 2. Ukraine: Structural Benchmarks (modified/new SBs in bold text; purple indicates new timing)

	Structural Benchmark	Sector	Timing	Status
1	Enact the second supplementary Budget 2023	Fiscal	End-April 2023	Met
2	Submit to Parliament a draft law to restore and strengthen Article 52 of the Budget Code to minimize ad hoc amendments to the budget law	Fiscal	End-May 2023	Met
3	Prepare an action plan, including to address the weaknesses identified in taxpayers' perception survey, as an input into National Revenue Strategy roadmap	Fiscal	End-May 2023	Met
4	Submit to Parliament a draft law which will reinstate articles of Budget Code that establish limits on issuance of public guarantee with clear criteria for such provision (including for priority sectors)	Fiscal	End-May 2023	Met
5	Enact amendments to the Budget Code and related regulatory framework to enhance transparency and accountability of the special accounts and consolidate them within general government as a special fund of the State Budget	Fiscal	End-May 2023	Met
6	Prepare a conditions-based strategy to move to a more flexible exchange rate, ease FX controls and transition to inflation targeting	Monetary and Exchange Rate	End-June 2023	Met
7	Adopt the draft law on tax policy and administration prepared under the PMB	Fiscal	End-July 2023	Not Met (implemented with delay)
8	Transfer the GTSO shareholding directly to the Ministry of Energy and adopt the new charter	Energy/ Corporate Governance	End-July 2023	Not Met (implemented with delay)
9	Enact the law to restore asset declaration of public officials not directly involved in the mobilization and war efforts and reinstating the NACP's function to examine and verify them	Governance/ Anti-Corruption	End-July 2023	Not Met (implemented with delay)
10	Enact the articles of the Budget Code that allow preparation of the medium-term budget framework, elaboration of the debt strategy, and ringfencing risks from guarantees.	Fiscal	End-September 2023	Met
11	Present in the 2024 budget declaration projections for major revenue and spending categories and sources of deficit financing for 2025-2026, and a fiscal risks statement including details on energy and critical infrastructure SOEs	Fiscal	End-September 2023	Met
12	Amend the AML/CFT Law to re-establish enhanced due diligence measures on politically exposed persons consistent with the risk-based approach consistent with the FATF standards.	Governance/ Anti-Corruption	End-September 2023	Not Met (implemented with delay)

Table 3. Ukraine: Structural Benchmarks (continued)

	Structural Benchmark	Sector	Timing	Status
13	Strengthen bank governance and oversight by: (i) separating the related-parties-unit from banking supervision; (ii) implementing "supervisory panels" as a consulting body to the Supervisory Committee; and (iii) resume scheduled inspections for both banking and non-banking institutions, while ensuring NBU discretion on matters related to staff safety	Financial Sector	End-September 2023	Met
14	MOF, with STS and SCS, to prepare an action plan, including short-term and medium-term measures covering key reform areas identified by the upcoming diagnostic, that would feed into broader NRS.	Fiscal	End-October 2023	Met
15	Update and publish the Medium-Term Debt Management Strategy to align it with the program objectives	Fiscal	End-October 2023	Met
16	Simplify the asset declaration system through linking with other databases and registers consistent with the public officials' legal obligations to make truthful and timely submissions	Governance/ Anti-Corruption	End-October 2023	Met
17	Select and appoint a supervisory board for the GTSO	Energy/ Corporate Governance	End-October 2023	Met
18	Review the current PIM procedures and develop a roadmap of measures so that: (i) all public investment projects follow unified PIM approaches, including PPPs; (ii) investment projects are selected on a competitive basis, with transparent selection criteria, and consistent with the medium-term budget framework; (iii) stronger powers are provided to MOF, including a clear gatekeeping role during the different stages of the investment project cycle.	Fiscal	End-December 2023	Met
19	Adopt the National Revenue Strategy	Fiscal	End-December 2023	**Met**
20	Adopt legislation to enhance the institutional autonomy and effectiveness of the SAPO by being designated as a separate legal entity, and specifically, on the selection procedures, capacity to regulate organizational activities, mechanisms for discipline and accountability, and autonomy under the criminal procedural code	Governance/ Anti-Corruption	End-December 2023	**Met**
21	Based on findings of the revenue working group, prepare short-term revenue measures (tax and non-tax) with yields of at least 0.5 percent of GDP ready to be included in budget 2024	Fiscal	End-February 2024	**Met**

Table 3. Ukraine: Table of Structural Benchmarks (continued)				
	Structural Benchmark	**Sector**	**Timing**	**Status**
22	Develop a concept note on the 5-7-9 program with proposals to target small and medium enterprises by phasing out the eligibility of large companies, enhance monitoring, and maintain adequate safeguards.	Fiscal	End-March 2024	**Met**
23	Adopt a new law (consistent with ¶28 of the MEFP) on the ESBU that has a clear mandate and scope for investigative powers consistent with good practice by focusing on major economic crimes; establishing legal basis for operation of the ESBU in terms of the selection of management and staff. The law will respect the existing delineation between the investigative powers of the ESBU and the National Anti-corruption Bureau of Ukraine (NABU).	Fiscal	End-June 2024	
24	**Develop a methodology to assess the effectiveness of tax privileges, including their cost to the budget, in order to have a unified reform approach**	Fiscal	***End-September 2024***	***Modify and reset from end-July 2024***
25	Identify major public companies severely affected by the war and prepare a review of potential fiscal and quasi-fiscal costs	Fiscal	End-September 2024	
26	With the help of IMF TA, produce a diagnostic review of pre-war MTBF policies and practices relative to best practices.	Fiscal	End-October 2024	
27	**Adopt amendments to the Customs Code (consistent with ¶27 of the MEFP), in line with international best practice.**	Fiscal	**End-October 2024**	
28	Based on the outcomes of a roadmap on development of PIM procedures, adopt a government decree with an action plan and timeline that provides clear linkages between MTBF and capital expenditures, including reconstruction priorities, and specifying the gatekeeper role of the MOF.	Fiscal	End-December 2024	
29	All systemic banks with majority state ownership will fall under the responsibility of the MOF, and any non-systemic banks that come under state ownership will not be recapitalized using fiscal resources and will be transferred to the DGF for resolution upon breach of prudential requirements.	Financial Sector	Continuous	
30	Prepare a bank rehabilitation framework in consultation with the DGF and IMF staff	Financial Sector	End-December 2024	
31	Implement a supervisory risk assessment methodology to inform supervisory engagement priorities	Financial Sector	End-December 2024	
32	**Analyze the debts and assess financial conditions of District Heating Companies (DHCs) through a desk review by a reputable audit firm, including by separating arrears until and after February 2022.**	Energy	***End-October 2024***	***Modify and reset from end-June 2024***

33	Enact amendments to the procedural code to rationalize matters or issues to be heard at the first instance by one anti-corruption judge or by a panel of three anti-corruption judges.	Governance/ Anti-Corruption	End-April 2024	**Not Met (implemented with delay)**
34	Complete an external audit of the National Anti-Corruption Bureau of Ukraine's effectiveness with participation of three independent experts with international experience and publish its report.	Governance/ Anti-Corruption	End-September 2024	
35	**Amend the Criminal Procedural Code to enable the Specialized Anti-Corruption Prosecutor's Office to manage extradition and mutual legal assistance request and rationalize consequences from expiration of time limits for pre-trial investigations (including for corruption cases) in line with MEFP, ¶67, 1st bullet.**	**Governance/ Anti-Corruption**	**End-October 2024**	
36	**Enact a law to establish a new court that will hear administrative cases against national state agencies (e.g., NBU, NABU, NACP) by judges who have been properly vetted for professional competence and integrity.**	Governance/ Anti-Corruption	***End-December 2024***	***Reset from end-July 2024***
37	Produce a SOE state ownership policy, dividend policy and privatization strategy	SOE Corporate Governance	End-October 2024	