CEE Bankwatch Network

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Applying best practices from EU funds to the reconstruction of Ukraine

Photo: Kurekaoru

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The reconstruction of Ukraine: background

CEE Bankwatch Network and its member group organisations in central and eastern Europe have been involved in the monitoring of EU funds since the early 2000s. As a result, Bankwatch has seen cases when EU funds have really made a difference and had a significant impact at a national level. Some of these experiences can show us how Ukraine's own funds and EU or international financial instruments dedicated to Ukraine's post-war reconstruction should be developed and used.

The scale of destruction caused by Russia's aggression to Ukraine's housing, industry, energy and social infrastructure, as well as its nature, environment and economy, is incredible. According to a joint report by the World Bank, the Ukrainian government and the European Commission, an estimated USD 349 billion was

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needed for recovery as of 1 June 2022,[1] with this figure sure to increase until the end of the war. With this in mind, joint efforts to coordinate donations and properly plan Ukraine's reconstruction must start before the end of the war.

In May 2022, the European Commission committed[2] to creating the Rebuild Ukraine Platform to coordinate financial institutions and donor organisations, as well establishing the new RebuildUkraine Facility. This was welcomed as a great step forward in financing the reconstruction effort and aligning Ukraine's economy with that of the EU.[3]

In June 2022, the European Council awarded Ukraine EU membership candidate status, ensuring that the future post-war reconstruction 'will be linked to the implementation of reforms and anti-corruption measures consistent with its European path'.[4] This process will continue the parties' close political and economic relations based on the association agreement with its deep and comprehensive free trade area. The financing of Ukraine's reconstruction will have to be aligned with the goals of the European Green Deal, the economic development programme that aims to make Europe climate-neutral by 2050. Led by the Ukrainian authorities, the reconstruction will take place in close partnership with the European Union and other key partners, such as G7 and G20 partners and other third countries, as well as international financial institutions and international organisations.[5]

The Ukrainian government has set up its National Council for Recovery[6] to prepare for post-war recovery and development from 2022 to 2032. The first national plans were presented in early July,[7,8] but these lacked priorities; a holistic vision for the country's development; and inclusive, bottom-up participation.[9] Moreover, crucial regional reconstruction plans are yet to be developed,[10] so the bottom-up approach and regional development needs must feed into the national reconstruction plan. Meanwhile, Ukrainian civil society

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[1] World Bank, European Commission, Government of Ukraine and the European Commission, *Ukraine Rapid Damage and Needs Assessment*, *World Bank*, August 2022.

[2] European Council, European Council conclusions on Ukraine, 30 May 2022, *European Council and Council of the European Union*, 31 May 2022.

[3] János Allenbach-Ammann, 'EU Commission proposes Ukraine reconstruction platform', *Euractiv*, 19 May 2022.

[4] European Council, European Council conclusions on Ukraine, 30 May 2022.

[5] European Commission, Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions: Ukraine Relief And Reconstruction, *European Commission,* 18 May 2022.

[6] Secretariat of the Cabinet of Ministers of Ukraine, About the National Council for the Recovery of Ukraine from the War, *Government Portal of Ukraine*, accessed 14 December 2022.

[7] Homepage, *Ukraine Recovery Conference*, accessed 14 December 2022.

[8] Recovery plan, *Ukraine Recovery Conference*, July 2022.

[9] Ecoaction, 'Analysis of Ukraine's Post-War Recovery Plan Blueprint and Ecoaction's Recommendations', *Ecoaction*, 15 July 2022.

[10] Про внесення змін до деяких законодавчих актів України щодо засад державної регіональної політики та політики відновлення регіонів і територій, Закон України, 9 July 2022.

organisations have developed green principles[11] for environmentally sustainable economic[12] and social reconstruction, which must be realised using the best available technologies and practices.

The proposed RebuildUkraine reconstruction plan[13] will bring together the Ukrainian government, the European Union and its Member States, the European Investment Bank and its international partners, other bilateral and multilateral partners (the World Bank Trust Fund and the International Monetary Fund administered account), and other international financial institutions. The RebuildUkraine Facility would be the main legal instrument for the European Union's support, through a mix of grants and loans, to the RebuildUkraine reconstruction plan. This would be embedded in the EU budget. It would build on the experience attained from financing investments and reforms under the Recovery and Resilience Facility inside the EU,[14] then adapt them to the unprecedented challenges of reconstructing Ukraine.

Source: European Commission[15]

[11] Ecoaction, 'Green Reconstruction of Ukraine: Position of Civil Society', *Ecoaction*, 5 May 2022.

[12] Ecoaction, 'Putting the green reconstruction of Ukraine into action: Requirements for programme design and policy', *Ecoaction*, 15 September 2022.

[13] European Commission, Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions: Ukraine Relief And Reconstruction.

[14] Ibid.

[15] Ibid.

While the structure of the financial platform is still under development, the proposal for the platform states that the European Commission will host the secretariat to help coordinate the donor community.[16] It will be important to ensure that the platform not only brings donors together, but also sets common rules and standards for stakeholder engagement, transparency and accountability. Moreover, the overall proposing, programming, implementing and overseeing cycle for the funds and projects must be laid out clearly, which will not only ensure that the reconstruction is done in an organised way, but will also ensure that future EU and national funding programmes in Ukraine are properly implemented.

Regional development in Ukraine

Map 1: New system of Ukraine's administrative territorial structure (at the level of districts, *hromadas*) as a result of decentralisation,[17] adopted 12 June 2020 by the Cabinet of Ministers

1,470 *hromadas* (total)
410 city-type
433 urban-type
627 rural-type

From 2014 to 2020, a decentralisation reform was implemented in Ukraine with the aim of enhancing regional development and local democracy. It resulted in the creation of 1,470 hromadas. Cities and hromadas should have a say in defining national priorities, and they should also implement specific solutions adapted to their own realities, vision for development and the opinions of the community itself. The number of these administrative territorial units, as shown on the map and listed in the table, adds another layer of complexity to the reconstruction efforts. Source: Ministry of Development of Communities and Territories of Ukraine; map from OpenStreetMap contributors via WebGIS

[16] Reuters, 'World must not waste time but swiftly start work on Ukraine's reconstruction', *Reuters*, 25 October 2022.

[17] *Hromada* is the term used for a special territorial unit in Ukraine created through the 2015-2020 process of voluntary mergers of territorial communities as a part of decentralization reform.

From 2014 to 2020, a decentralisation reform was implemented in Ukraine with the aim of enhancing regional development and local democracy.[18, 19] It was considered extremely successful[20] and helpful for regions in resisting the shocks caused by the Russian invasion in February,[21] when the central government's attention and resources were very limited. The decentralisation reform should serve as an asset so that effective regional development will go smoothly during the country's reconstruction.

The newly adopted legislation on the state regional policy includes changes[22] that aim 'to create conditions for the dynamic, balanced development of Ukraine and its regions, to ensure their social and economic unity, to raise the standard of living of the population, to create safe conditions, to ensure state-guaranteed social standards for every citizen regardless of his place of residence'. It is foreseen that there will be four functional types of territories: 1) recovery areas; 2) regional poles of growth; 3) territories with special conditions for development; and 4) areas of sustainable development with differentiated development support measures.[23]

The new legislation on state regional policy planning[24, 25] describes the strategic documents required for development at such levels: 1) a state strategy on regional development for Ukraine; 2) regional strategies for development; and 3) strategies for development of territorial divisions. Attention should be paid to regional development agencies, which will be the key implementers of such programmes. Regional development is seen as 'the process of social, economic, ecological, humanitarian and other positive changes in the regions'.

EU funding programmes and good practices

The European Union supports the economies of its 27 Member States through the EU budget, also known as the Multiannual Financial Framework (MFF). The MFF complements countries' national budgets in policy areas that are carried out at the European level, and currently amounts to EUR 1 074.3 billion from 2021 to 2027. In addition to the MFF, in 2020, European institutions agreed to support the Member States hit hardest by the COVID-19 pandemic by creating a recovery package with a further EUR 750 billion at the disposal of countries between 2021 and 2026.

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[18] Lucas Ford, 'Understanding Ukraine's Decentralisation Reform', *VoxUkraine*, 22 June 2020.

[19] Пресцентр ініціативи "Децентралізація", Viacheslav Nehoda at the CDDG meeting: A new Action Plan of the Council of Europe for Ukraine focused on local self-government development is coming ', Децентралізація, 28 November 2022.

[20] Ministry of Development of Communities and Territories of Ukraine, Моніторинг Реформи Місцевого Самоврядування Та Територіальної Організації Влади, presentation, Децентралізація, 10 January 2022.

[21] Пресцентр ініціативи "Децентралізація", Roger Myerson: The reform of local self-government became one of the main factors that strengthened the resolve of Ukrainians to fight for their country,' Децентралізація, 24 November 2022.

[22] Про внесення змін до деяких законодавчих актів України щодо засад державної регіональної політики та політики відновлення регіонів і територій.

[23] Ibid.

[24] Ibid.

[25] Ibid.

As part of the EU budget, the RebuildUkraine Facility will support the reconstruction of Ukraine through the development of Ukraine's regions, municipalities and territorial divisions. In order to improve the quality of the facility, elements like public participation and climate conditionality within cohesion policy funds (including the Just Transition Fund) and the Recovery and Resilience Facility (RRF) should be taken into consideration and be applied to the case of Ukraine's reconstruction.

Cohesion policy funds

The EU cohesion policy aims to strengthen 'economic, social and territorial cohesion in the European Union' and to 'correct imbalances between countries and regions'.[26] The EU supports these objectives through the following funds:

- The European Regional Development Fund (ERDF), which invests in social and economic development;
- The Cohesion Fund (CF), which invests in environmental protection and transport in less prosperous EU countries;
- The European Social Fund Plus (ESF+), which supports job growth and creates a fair and socially inclusive society;
- The Just Transition Fund (JTF), which supports the regions most affected by the transition towards climate neutrality.

All of these are examples of European structural and investment funds, which are regulated by the Common Provision Regulation.[27] In the current programming period from 2021 to 2027 (and the investments foreseen in this period), the cohesion policy has a budget of EUR 392 billion to finance regions and countries.

In order to receive the funds, ***Member States need to prepare and submit*** two sets of documents outlining priorities and specific investment needs: ***partnership agreements*** and ***operational programmes.*** Partnership agreements define the **strategy and investment priorities** of the Member States, and operational programmes are the **detailed plans** of how the country intends to spend the money during the seven years, and they can be either **regional or national.** The programming lasts for seven years, during which Member States regularly present progress made in the implementation of investment proposals to the European Commission.

Since the Russian invasion of Ukraine, the European Commission has used Cohesion Policy money to support EU Member States in welcoming Ukrainian refugees through the 'Flexible Assistance to Territories' (FAST-CARE)

[26] European Parliament, Fact sheets on the European Union: Economic, social and territorial cohesion, *European Parliament*, accessed 14 December 2022.

[27] European Parliament and Council of the European Union, Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021 laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, the Just Transition Fund and the European Maritime, Fisheries and Aquaculture Fund and financial rules for those and for the Asylum, Migration and Integration Fund, the Internal Security Fund and the Instrument for Financial Support for Border Management and Visa Policy, *Official Journal of the European Union* L 231/159, *EUR-Lex*, 30 June 2021.

programme. FAST-CARE extends the support already provided under the Cohesion's Action for Refugees in Europe (CARE), which prioritises equal access to healthcare and more resilient health systems, as well as sustainable solutions for climate change adaptation and disaster risk prevention.[28]

- **Conditionality and climate**

Regional policies play a fundamental role in achieving the targets of the European Green Deal: accounting for one-third of the total EU budget, cohesion policy funds can provide a significant boost to the energy transition. Climate policies are among the five policy objectives set for the current 2021-2027 programming period. Three of the European structural and investment funds are designed to **support green targets: the ERDF, the Cohesion Fund and the newly introduced Just Transition Fund.**

The ERDF and the Cohesion Fund must respectively devote **30 per cent and 37 per cent of their budgets to climate objectives.**[29] This means specifically covering areas such as energy efficiency, climate change adaptation, renewable energy, circular economy and sustainable development. In addition to this, the cohesion policy contributes to tackling the loss of biodiversity in line with the targets set under the MFF.[30]

In order to be eligible to receive the money, Member States must propose investments that comply with **specific requirements called 'enabling conditions'**,[31] laid down in annex IV of the Common Provision Regulation. All programmes must also be subjected to a strategic environmental assessment evaluating the likely environmental effects of investments.[32] Furthermore, the 'do no significant harm' principle was introduced for the first time to the current cohesion policy; although it is not mandatory for countries to provide a 'do no significant harm' assessment to the European Commission (as happens for the recovery and resilience plans), the principle ensures further compliance with the climate objectives.

In the previous programming period (2014 to 2020), important projects contributing to the European Green Deal's targets were achieved thanks to cohesion policy money. For example, the opening of the first large-scale park of 1,720 solar collectors in Salaspils, Latvia in 2019 is considered best practice for decarbonising district heating systems and deploying solar thermal energy. This project received EUR 2.73 million (out of the total EUR 8.78 needed to complete the project) through cohesion co-funding under the thematic objective 'Promoting energy efficiency and local RES [renewable energy sources] in district heating'.

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[28] European Commission, Ukraine: Cohesion Policy steps up support to address the consequences of Russia's aggression in Ukraine with the 'Flexible Assistance to Territories', *European Commission*, 29 June 2022.

[29] European Parliament, Cohesion policy and climate change, *European Parliament*, 11 March 2021.

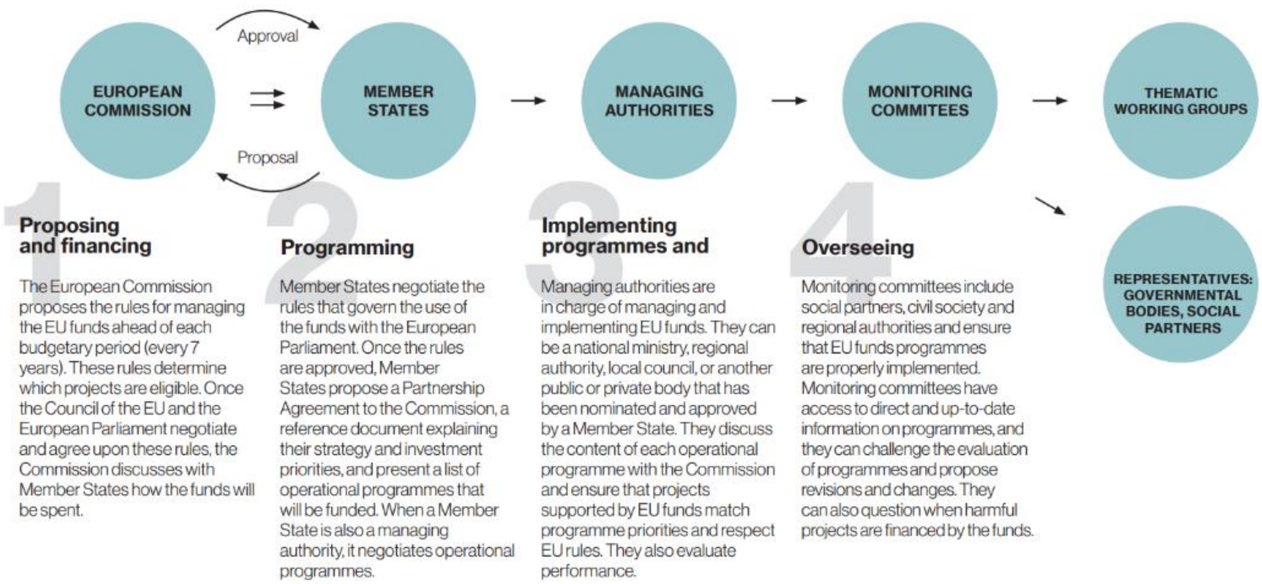
[30] Common Provision Regulation: '[t]he Funds should contribute to mainstream biodiversity action in the Union policies and to the achievement of the overall ambition of providing 7,5 % of annual spending under the multiannual financial framework (MFF) to biodiversity objectives in the year 2024 and 10 % of annual spending under the MFF to biodiversity objectives in 2026 and 2027, while considering the existing overlaps between climate and biodiversity goals.'

[31] Annex IV of the Common Provision Regulation with enabling conditions. European Parliament and Council of the European Union, Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021.

[32] United Nations Economic Commission for Europe, *Protocol on Strategic Environmental Assessment (SEA) to the Convention on Environmental Impact Assessment in a Transboundary Context*,' *United Nations Economic Commission for Europe*, accessed 14 December 2022.

- **Public participation and stakeholder engagement**

Partnership is one of the cornerstones of the EU's regional policy. Regional and local governments, civil society organisations and socioeconomic actors contribute to shaping the cohesion policy and play a central role in the programming of the European structural and investment funds.



Source: CEE Bankwatch Network, 2019[33]

The involvement of civil society is regulated by the partnership principle, which was strengthened by the institutions in 2014 when the European Code of Conduct on Partnership[34] was introduced and attached to the Common Provision Regulation, becoming mandatory for all the Member States. The code of conduct defines how governments and managing authorities must engage with stakeholders during the preparation, implementation and monitoring of partnership agreements and operational programmes in order to create a structured and open space for exchange with partners. For example, articles 2, 3 and 4 include criteria to identify the relevant partners to consult with. Articles 10 and 11 set the rules of membership and procedures for the monitoring committees, the bodies whose objective it is to oversee the implementation of operational programmes once they are approved.

Although compliance with the code of conduct can be improved even in the current programming period,[35] this document remains an essential tool to guarantee that partners are involved in the process. In the previous and current programming period, it is indeed possible to observe good examples of partnership implementation in central and eastern Europe.

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[33] CEE Bankwatch Network, *Financing the European Green Deal*, *CEE Bankwatch Network*, September 2022.

[34] European Commission, Commission Delegated Regulation (EU) No 240/2014 of 7 January 2014 on the European code of conduct on partnership in the framework of the European Structural and Investment Funds, *Official Journal of the European Union* L 74/1, *EUR-Lex*, 7 January 2014.

[35] Francesca Canali, 'More stakeholder participation needed in preparation of new cohesion programmes', *CEE Bankwatch Network*, 29 July 2021.

For example, in **Slovakia**, civil society experts started participating in the programming and monitoring of EU funds with proper recognition, systematisation, networking and financial support during the previous programming period. The Partnership project in Slovakia has created coordination capacities and supported activities with national authorities such as connecting ministries with experts and regional stakeholders, participatory monitoring and improvements in the nomination mechanism for civil society representatives in the EU system.[36]

As for the current programming period, the process has been very much delayed and the preparation of partnership agreements and operational programmes will end at the beginning of 2023, long after the initial deadline. Nevertheless, some improvements in the quality of consultations were observed even during the preparation phase, as was the case in **Poland.** For the first time, Poland's managing authorities hosted reverse public hearings, a type of public hearing where authorities respond to inputs from consultations and regular public hearings. This new practice in Poland has been welcomed by the partners, who agree that the quality of consultations has improved.

The Recovery and Resilience Facility

The RRF[37] was presented in 2020 and put forward as the main EU instrument for responding to the outbreak of the COVID-19 pandemic and its consequences on European countries. It officially came into force in February 2021, providing up to EUR 672.5 billion in loans and grants covering reforms and investments until the end of 2026.

Due to the unprecedented amount of funding made available from the RRF, this facility is considered an expression of the EU's solidarity and unity[38] for supporting post-pandemic economic reconstruction in the 27 EU Member States, all of which were severely hit by the COVID-19 crisis. It is expected[39] that the RRF will serve as the model for funding Ukraine's reconstruction, although at the time of writing, the details of the process have not yet been disclosed.

- **Conditionality and climate**

In order to receive funding from the RRF, each Member State had to prepare a **recovery and resilience plan outlining the reforms and investments** they were planning to implement with this money. Although the first deadline for the submission of the recovery plans to the European Commission was the end of April 2021, there were many delays in the process and some countries only received the green light from institutions recently.[40] In order to receive the RRF money, countries had to propose reforms and investments that would comply with

[36] CEE Bankwatch Network, *Financing the European Green Deal*.

[37] European Commission, Recovery and Resilience Facility, *European Commission*, accessed 14 December 2022.

[38] European Greens, Recovery and Resilience Facility - for a true green and just transition, *European Greens*, adopted 25-29 May 2021.

[39] European Commission, Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions: Ukraine Relief And Reconstruction.

[40] With the exception of Hungary and Poland, whose plans are still under negotiation with the European Commission due to rule of law concerns.

a series of conditions laid down in the regulation. Regarding climate issues, each recovery plan had to include a minimum of 37 per cent of its expenditure on the green transition.[41]

The European Commission adjudged that all recovery plans reached the 37 per cent green target, with some countries even exceeding it.[42] However, using other methodologies to assess the plans, such as the one developed under the Green Recovery Tracker,[43] we can see that this is not always the case and that many countries in all regions of Europe still need to improve their plans.[44] Nevertheless, there were some countries where both methodologies showed that the target was achieved, such as Finland, Germany and Hungary.

In addition to the 37 per cent earmarking, the reforms and investments proposed in the recovery plans also must comply with the 'do no significant harm' principle. This principle was first developed under the EU Taxonomy Regulation as a principle to identify economic activities that are sustainable. In order to be defined as such, a measure must significantly contribute to one of the six environmental objectives listed in article 17 of the regulation, while not causing harm to any of the others.

With regards to the application of the 'do no significant harm' principle in the recovery plans, the European Commission specified the rules in a technical guidance that was adopted in February 2021. It advises that no measure included in the recovery and resilience plans should cause significant harm to any of the six environmental objectives described in article 17 of the taxonomy. If this condition was not met, the European Commission was not supposed to endorse the recovery plan and the country should not have included that specific measure.

Unfortunately, we cannot assess with certainty that this is what happened in most cases. Furthermore, the way the principle was designed under the RRF still left the door open for fossil-based heating systems, in particular gas boilers. Nevertheless, although the quality of the application of the 'do no significant harm' principle can certainly be improved by better implementation, this tool can still play an important role in preventing harmful investments from being financed with EU money.

- **Public participation and stakeholder engagement**

The RRF provides weak and general provisions on stakeholder engagement and consultations. In the regulation, the European Commission simply encourages Member States to consult with partners, but consultations are not mandatory and the partnership principle is neither mentioned nor applied. The lack of strong wording on the necessity to include stakeholders in a structured way severely affected the preparation of the recovery plans, which often happened behind closed doors and without the proper involvement of civil society.[45] In some

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[41] European Commission, Recovery and Resilience Scoreboard: green transition, *European Commission*, accessed 14 December 2022.

[42] European Commission, Recovery and Resilience Facility - Performance, *European Commission*, accessed 14 December 2022.

[43] Wuppertal Institute and E3G, Green Recovery Tracker homepage, *Green Recovery Tracker*, accessed 14 December 2022.

[44] CAN Europe and CEE Bankwatch Network, *Reaching for a Green Recovery*, *CEE Bankwatch Network*, February 2022.

[45] CEE Bankwatch Network, 'Secrecy surrounding €672 billion in EU recovery funding jeopardises building back better', *CEE Bankwatch Network*, 9 February 2021.

countries, stakeholders have had limited opportunities to propose concrete measures or even be aware of final plans until their submission or final approval by European institutions.

Despite the very weak provisions, some countries in central and eastern Europe performed better than others in terms of involving stakeholders in discussions.

In **Bulgaria**, preparing the plans took longer than in the rest of Europe (due to constant changes of government), which gave civil society organisations more time to influence the plan. Eventually, having a say on the proposed investments and measures allowed them to remove some very harmful measures from the final plan submitted to the European Commission (i.e. Maritsa East 2[46]).

In **Estonia**, the government appointed a monitoring committee to check the implementation of the plan. Since the partnership principle does not apply to the RRF, Member States were not obliged to set up monitoring committees like they are for funds associated with the cohesion policy. Nevertheless, in some countries, including Estonia, pressure from civil society led to the formation of such committees, whose job is to carefully scrutinise the implementation of the plan.

Recommendations for funding Ukraine's reconstruction

The RebuildUkraine strategic reconstruction plan should ensure the implementation of a 'rebuild better' strategy and lead the country on its path to EU membership. As such, the quality of projects, programmes and initiatives should be in line with EU standards. The focus on economic development should be balanced and sustainable and may have long-term positive implications on post-war reconstruction.

The implementation of the **EU cohesion policy** could be one of the examples we look to during Ukraine's reconstruction, as this policy is designed to address imbalances between countries and regions. In Ukraine, lessons from the cohesion policy might be useful in addressing the disproportionate impacts of the Russian invasion on certain regions in the light of the latest regional development legislation changes.

It is important to incorporate some features of the cohesion policy in the financial programming and strategies for Ukraine's development and reconstruction:

- The partnership principle is one of the cornerstones, emphasising the role of partners as per the European Code of Conduct on Partnership.
- Programmes must be subject to a strategic environmental assessment consistent with the national energy and climate plan and reflect the 55 per cent emission reduction target for 2030.
- The ERDF and the Cohesion Fund must respectively devote at least 30 per cent and 37 per cent of their budget to climate objectives; at the same time, the Just Transition Fund requires the preparation of Territorial Just Transition Plans to support regional transitions.

[46] Rory Forster, 'In Bulgaria, a cautionary tale for the energy transition as country abandons coal to gas switch', *CEE Bankwatch Network*, 21 January 2022.

- The thematic enabling conditions applicable to the ERDF, ESF+ and the Cohesion Fund[47] must also apply here.

The RRF practices that were designed to deal with the post-COVID-19 hurdle contain important elements that can help shape investment and the development of sustainable strategies while emphasising environmentally friendly activities:

- 37 per cent of the overall budget earmarked for green transition;
- the application of the 'do no significant harm' principle.

The planning and development of Ukraine's reconstruction should take a bottom-up, long-term strategic approach, rather than relying on top-down decision-making. Civil society organisations and socioeconomic actors should have a profound role across a range of different stages of the process (programming, implementation, monitoring and evaluation), in line with the European Code of Conduct on Partnership (N 240/2014).

If the partnership principle, climate targets and enabling conditions are followed properly, investment projects will better address regional needs, barriers to spending and future challenges, such as the climate crisis. Public participation also helps prevent fraud and the misuse of money.

[47] Thematic enabling conditions applicable to ERDF, ESF+ and the Cohesion Fund – Article 15(1), European Parliament and Council of the European Union, Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021.