



# ICLG

The International Comparative Legal Guide to:

## Oil & Gas Regulation 2016

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A practical cross-border insight into oil and gas regulation work

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**Group Publisher**

Richard Firth

**Published by**

Global Legal Group Ltd.  
59 Tanner Street  
London SE1 3PL, UK  
Tel: +44 20 7367 0720  
Fax: +44 20 7407 5255  
Email: info@glgroup.co.uk  
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# Ukraine

Vitaliy Radchenko



CMS Cameron McKenna

Inna Antipova



## 1 Overview of Natural Gas Sector

**1.1 A brief outline of your jurisdiction's natural gas sector, including a general description of: natural gas reserves; natural gas production including the extent to which production is associated or non-associated natural gas; import and export of natural gas, including liquefied natural gas (LNG) liquefaction and export facilities, and/or receiving and re-gasification facilities ("LNG facilities"); natural gas pipeline transportation and distribution/transmission network; natural gas storage; and commodity sales and trading.**

Ukraine's proven natural gas reserves are estimated at 900 billion cubic metres ("bcm") (0.5 per cent of the world's proven reserves). They are mainly concentrated in three regions: the Carpathians (Western Ukraine); Dnipro-Donetsk (Eastern Ukraine); and offshore Ukraine (in the Black and Azov Seas). The Dnipro-Donetsk basin is currently the most productive region, accounting for 90 per cent of domestic hydrocarbons production (8,482 bcm of the estimated recoverable resources).

Ukrainian unconventional gas opportunities have now attracted significant interest from the world's major oil and gas companies – in 2012 Eni (Italy) purchased 50.01 per cent of Westgasinvest (which holds subsoil rights to nine shale gas licence areas in the Lviv Basin of Ukraine). In 2012, the Ukrainian Government also held two tenders for production-sharing agreements ("PSAs") relating to shale and tight gas opportunities in the Oleska (awarded to Chevron) and Yuzivska (awarded to Shell) areas.

Offshore Ukraine is not well explored. Nevertheless, until recently offshore areas were considered to be attractive for foreign investors. Certain offshore blocks were awarded to foreign investors: in 2012 an ExxonMobil-led consortium won a tender to operate in a deepwater offshore area (Skifska); Vanco and the Government of Ukraine came to an amicable settlement with respect to the development of another offshore area (Prykerchenska); and in 2013 Ukraine also signed a PSA with a consortium of investors – Italian group Eni and Electricite de France.

However, due to the political crisis, the annexation of Crimea by the Russian Federation and hostilities in the Donetsk and Luhansk regions of Ukraine, all of the abovementioned PSA projects were put on hold in 2014.

Producing 20.17 bcm of natural gas per year, Ukraine usually manages to cover about 48 per cent of domestic natural gas consumption (2014). However, in light of the conflict with Russian

"Gazprom" in 2014, which resulted in the suspension of imports of Gazprom's gas to Ukraine, the current policy of the State for the gas sector is oriented at reducing consumption of gas by all types of consumers, replacing natural gas with other types of energy sources, as well as diversifying gas supplies to the greatest extent allowed by Ukraine's interconnectors with Europe. In 2014, 85 per cent of domestic production is undertaken by the State-owned oil and gas monopoly Naftogaz and its subsidiaries. The rest is produced by private producers and through farm-in agreements with State-owned companies.

Despite the outlined conflict with Gazprom, Ukraine still remains one of the main transit routes of Russian gas to European countries. There are three main pipeline corridors: the Braterstvo Pipeline (Urengoy-Pomari-Uzhgorod); the Progress Pipeline (Yamburg – western border of Ukraine); and the Soyuz Pipeline (Orenburg – western border of Ukraine).

The natural gas transmission system of Ukraine consists of 38,550 km of pipelines, including 22,160 km of main (high pressure) pipelines with a capacity of 288 bcm per year at the point of entry and 179 bcm per year at the exit point. The majority of the natural gas transmission infrastructure in Ukraine is State-owned and operated by Naftogaz's subsidiary Ukrtransgaz.

Ukraine has 13 gas storage facilities with an aggregate capacity of 34 bcm. As one other gas storage facility is located in the Crimea, currently Ukraine does not have access to it.

Ukraine has no LNG terminals at present. Construction of the first LNG terminal – in the Odessa region – is the Government's priority, and the officials on repeated occasions claimed that the negotiations with foreign investors are ongoing. However, the actual implementation of this project is not visible.

## 1.2 To what extent are your jurisdiction's energy requirements met using natural gas (including LNG)?

Natural gas and coal are the main components of Ukraine's primary energy supply. The share of coal in the country's energy balance in 2013 (official data for 2014 is not yet available) amounted to 36 per cent. The natural gas accounted for 34 per cent of total energy consumption. This makes the Ukrainian economy one of the world's most energy-intensive economies. According to the statistical data of 2013 other sources include: nuclear (uranium) (19 per cent); oil and petroleum products (9 per cent); and hydro and renewables (2 per cent).

Currently Ukraine neither imports nor produces LNG, but the Ukrainian population primarily consumes LPG produced in Ukraine

### 1.3 To what extent are your jurisdiction's natural gas requirements met through domestic natural gas production?

Ukraine's domestic production covers up to 48 per cent (20.17 bcm in 2014) of its total natural gas consumption, which amounted to 42.5 bcm in 2014. The rest is satisfied from natural gas imported by Naftogaz (19.5 bcm in 2014).

In 2014, Ukraine managed to reduce the volumes of gas imported from Russia (only 14.5 bcm in comparison to 25.8 in 2013) by increasing the share of European gas (5 bcm in comparison to 2.1 bcm in 2013) imported from EU (through the territories of Poland, Slovak Republic and Hungary).

In 2015, Naftogaz imports the European gas mostly from the Slovak Republic, but also erratically from Poland and Hungary.

### 1.4 To what extent is your jurisdiction's natural gas production exported (pipeline or LNG)?

In 2014 and 2015, Ukraine did not export any natural gas. It is unlikely that Ukraine will be exporting gas in 2016 due to its scarcity even for internal consumption.

## 2 Overview of Oil Sector

### 2.1 Please provide a brief outline of your jurisdiction's oil sector.

Ukraine has 395 million tonnes of proven oil reserves and 850 million tonnes of potentially recoverable reserves. Most of these are located in the Dnipro-Donetsk basin. The six largest fields together provide about one-fifth of Ukraine's oil production.

Undiscovered oil resources are estimated at 2.3 billion barrels, with 1.3 billion barrels of oil and 927 million barrels of gas condensate. Over 86 per cent of those potential reserves are located in the Dnipro-Donetsk basin.

Ukraine's oil transportation system consists of the Druzhba main pipelines in the west and Trans-Dnipro main pipelines in the east. The Druzhba corridor is one of two main export routes for Russian oil to Central European refineries. It has a maximum capacity of 1.2 million b/d. The Trans-Dnipro corridor transports oil from Russia to the Lisichansk, Kremenchug, Kherson and Odessa oil refineries in the south and east of Ukraine. The system has a total length of 2,400 kilometres and a capacity of 2.1 million b/d.

### 2.2 To what extent are your jurisdiction's energy requirements met using oil?

According to the statistical data of 2013, oil and petroleum products meet 8.5 per cent of Ukraine's energy mix, making it the fourth largest resource after coal, natural gas, and uranium.

### 2.3 To what extent are your jurisdiction's oil requirements met through domestic oil production?

Ukraine is an importer of oil (0.25 million tonnes of oil imported in 2014). The main source of crude imports is Russia and Kazakhstan (URALS).

Oil production in Ukraine amounted to 2.7 million tonnes in 2014. The majority of oil production is carried out by Naftogaz's

subsidiaries (2.4 million tonnes). The volume of production is lowering each year (in 2014 the oil production decreased by 8 per cent) due to depletion of the mature explored oil reserves and stagnation of the sector.

### 2.4 To what extent is your jurisdiction's oil production exported?

In recent years, none of Ukraine's oil production has been exported, owing to changes in the licensing regime and the introduction of export quotas. However, in 2014, the "zero" export quota for oil was cancelled and in 2014-2015 Ukrainian oil has been exported to Lithuania and Moldova.

## 3 Development of Oil and Natural Gas

### 3.1 Outline broadly the legal/statutory and organisational framework for the exploration and production ("development") of oil and natural gas reserves including: principal legislation; in whom the State's mineral rights to oil and natural gas are vested; Government authority or authorities responsible for the regulation of oil and natural gas development; and current major initiatives or policies of the Government (if any) in relation to oil and natural gas development.

The development of natural gas and oil reserves is governed by a number of industry-focused legal acts, namely:

- the Subsoil Code of Ukraine (the "**Subsoil Code**"), No. 132/94-BP of 27 July 1994;
- the Law of Ukraine "On Oil and Gas", No. 2665-III of 12 July 2001 (the "**Oil and Gas Law**"); and
- the Law of Ukraine "On Product Sharing Agreements", No. 1039-XIV of 14 September 1999 (the "**PSA Law**").

Article 13 of Ukraine's constitution provides that the Ukrainian nation is the sole owner of the land, subsoil, air, water and other natural resources located within the territory of Ukraine, including its continental shelf and in its exclusive maritime zone. The underlying principle of Ukraine's oil and gas legislation is that, although the Ukrainian nation must remain the owner of the subsoil, it can grant rights to use the subsoil and, once a mineral extracted by a subsoil user reaches the surface, ownership can pass to the subsoil user.

The main State authorities involved in the development of natural gas are:

- the Verkhovna Rada or Parliament – which passes primary legislation;
- the Cabinet of Ministers of Ukraine ("**CMU**") – which passes secondary legislation implementing the primary legislation;
- the Ministry of Energy and Coal Industry – which is responsible for allowing the production stage to commence; and
- the State Service for Geology and Subsoil of Ukraine – which issues special permits (licences) to subsoil users (see the following section).

Current major initiatives of the Government are as follows:

- reform (liberalisation) of the gas market based on Ukraine's commitments to the Energy Community. The Law of Ukraine "On the Natural Gas Market" No. 329-VIII (the "**Gas Market Law**") was adopted by the Parliament on 9 April 2015. In line with the mentioned Law a new gas market model (as compliant with the 3<sup>rd</sup> Energy Package) was implemented in Ukraine starting from 1 October 2015,

providing for the unbundling of system operators, free market prices, introduction of the concept of public service obligations and adequate roles of the State authorities;

- diversification of the energy supply (by promoting Ukrainian gas production, substituting Russian gas with the one imported from Europe, use of alternative energy sources); and
- cooperation with the International Monetary Fund (IMF has pledged USD 17.5 billion to support Ukraine's economy, but in turn demanded tough reforms. In particular: review of the country's fiscal policies; increase of the gas prices for households up to the market level to eliminate cross subsidies, etc.).

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### 3.2 How are the State's mineral rights to develop oil and natural gas reserves transferred to investors or companies ("participants") (e.g. licence, concession, service contract, contractual rights under Production Sharing Agreement?) and what is the legal status of those rights or interests under domestic law?

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Any investor (whether foreign or Ukrainian) wishing to conduct exploration and/or production activities in a particular area requires a licence (called a "special permit") in order to begin work. These are issued by the State Geology Service of Ukraine. The special permit can be obtained under one of two different regimes for subsoil use in Ukraine: (1) licensing; and (2) production-sharing.

#### The licensing regime

Under the licensing regime, the special permits are usually purchased by the investor at an auction held by CMU. The following are notable exceptions to the need for an auction:

- where an investor already holds a special permit allowing exploration in a particular area, and, having fulfilled its obligations under this permit, wishes to proceed to development of the area; and
- if the holder of a special permit relating to a particular area wishes to conduct exploration in an adjoining area, the area to which the special permit relates can be extended by up to 50 per cent.

#### The PSA regime

Under the PSA regime, the special permit is awarded to an investor as a result of it entering into an agreement with the Ukrainian State, acting through CMU, to share any hydrocarbons extracted by the investor in a particular area. As a rule, PSAs are executed with the winner of a competitive tender, to the investor offering the most attractive terms of cooperation with the State. There is also an option for the subsoil users working under the licensing regime to switch to the PSA without any tender procedures.

The PSA regime is generally more attractive to foreign investors, as an investor under a PSA enjoys significant benefits, including tax privileges, a "stability" clause protecting it from adverse changes in legislation, and help from the State in obtaining the necessary permits and authorisations (including the special permit for the relevant subsoil area) to perform the PSA.

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### 3.3 If different authorisations are issued in respect of different stages of development (e.g., exploration appraisal or production arrangements), please specify those authorisations and briefly summarise the most important (standard) terms (such as term/duration, scope of rights, expenditure obligations).

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As a rule, a special permit (see question 3.2) is obtained for each stage of development; however, combined permits also exist in Ukraine. The term of a special permit depends on the operations it covers, as indicated below:

- (a) geological survey, including pilot commercial development of fields: up to five years for onshore operations and 10 years for offshore operations;
- (b) production (extraction) of mineral resources: up to 20 years for onshore operations; and 30 years for offshore operations; and
- (c) a combined permit for both of the above stages: up to 20 years for onshore operations; and 30 years for offshore operations.

The lifetime of a special permit associated with a PSA may be up to 50 years (which is also the maximum term of a PSA without extensions).

Each special permit is supplemented by a "licensing agreement" between the subsoil user and the Ukrainian State. This licensing agreement establishes the basic rights and obligations of the special permit holder, including the minimum investment obligations, the timeframes and goals of the work programme, and environmental protection requirements.

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### 3.4 To what extent, if any, does the State have an ownership interest, or seek to participate, in the development of oil and natural gas reserves (whether as a matter of law or policy)?

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The position of the State differs according to the regime under which development takes place.

#### The licensing regime

As a matter of policy from year to year, substantial numbers of special permits are usually awarded to State oil and gas companies on a preferential basis. There is no requirement for the State to hold an interest in a special permit awarded to a private company.

#### The PSA regime

Under the PSA Law, the State receives a share of production under a PSA. The PSA Law states that the investor's share cannot be over 70 per cent at the cost-recovery stage. At the profit-production stage, the practice in previous PSA tenders shows that the State's share is likely to be at least 15 per cent (for unconventional gas projects) and 20 per cent (for oil and gas production).

Examples of PSA tenders held in 2012 demonstrate that the State may also require that the investor develop an area jointly with a State-owned company. This company is likely to be entitled to 50 per cent of the investor's share in profit production. This structure applied in the PSAs relating to the Oleska and Yuzivska areas, where foreign investors had to work with joint ventures established between the State-owned Nadra of Ukraine (90 per cent) and a privately owned entity – SPK-Geoservice LLC (10 per cent).

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### 3.5 How does the State derive value from oil and natural gas development (e.g. royalty, share of production, taxes)?

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Under the **licensing regime** the State derives value through taxation. The principal mechanisms for taxing oil and gas development are as follows:

- (a) **Corporate Profit Tax (CPT) at 18 per cent.**
- (b) **Rental Fee**, which is paid according to the volume and type of hydrocarbons produced and their effective or estimated price. A different rate of taxation applies in respect of oil, condensate or natural gas, the depth at which hydrocarbons are extracted and the area in which the deposits are located.

Oil and condensate:

- 45 per cent – for oil extracted from deposits at a depth of up to 5 km; and

- 21 per cent – for oil and condensates extracted from deposits at a depth of more than 5 km.

Natural gas sold not for households:

- 55 per cent – for gas extracted from deposits at a depth of up to 5 km;
- 28 per cent – for gas extracted from deposits at a depth of more than 5 km; and
- 11 per cent – for offshore gas extraction.

The tax base for calculation is (i) for natural gas – the maximum level of the price for natural gas sold to industrial consumers, the level of which is to be set by the Regulator (rather than the average customs value of imported natural gas, as it was before), and (ii) for oil – the URALS oil price.

(c) **Value-Added Tax (VAT) at the general 20 per cent rate** (0 per cent is levied on export of goods and in some other cases).

In addition, the payroll (social) withholding with a rate of between 36.76 per cent and 49.7 per cent is withheld by the subsoil users from the employees' salaries. The exact rate depends on the degree of risk attributed to a company's activity (67 classes of risk).

#### The PSA regime

The above taxes (CPT, rental fee, VAT), as well as payroll withholding and excise tax (levied on import of excisable goods) also apply to the production-sharing regime. However, the investor enjoys the following taxation privileges for the duration of the PSA:

- in certain cases VAT is levied at a zero rate, as for instance during import or export of equipment needed to carry out operations under the PSA;
- profits received under the PSA are exempt from the profit repatriation tax; and
- accrual of any other taxes and mandatory payments is substituted by the State's share of profit production.

Previously the investors used to enjoy lower rates of subsoil use charge (2 per cent of the URALS price and 1.25 per cent of the average customs value of gas). However these preferential rates were abolished as of August 2014.

### 3.6 Are there any restrictions on the export of production?

Please refer to questions 4.1 and 5.1.

### 3.7 Are there any currency exchange restrictions, or restrictions on the transfer of funds derived from production out of the jurisdiction?

Ukraine has relatively strict foreign currency restrictions currently in place. The transfer of foreign currency outside of Ukraine is subject to an individual licence issued by the National Bank of Ukraine, unless the particular transfer is expressly exempt from the licensing requirements (e.g. payments for imported goods or services, payments of interest and principal on foreign currency loans from non-residents, etc.).

Due to the current strict currency outflow restrictions, it is currently impossible to purchase and transfer foreign currency under the following transactions:

- repatriation of funds received by foreign investors as a result of sale of the securities issued by Ukrainian entities (with an exception for debt securities sold on the Ukrainian stock exchanges);
- repatriation of funds received by foreign investors as a result of: (a) sale of corporate rights in Ukrainian entities (other than shares); (b) reduction of charter capital; or (c) exit of foreign investors from the companies;

- repatriation of dividends to be paid to foreign investors; and
- early repayment of cross-border loans (subject to certain exceptions) by residents.

Foreign currency payments by non-residents to Ukrainian entities from abroad are generally allowed, subject to requirement for the mandatory conversion of 75 per cent of foreign currency proceeds from abroad received by legal entities, representative offices and entrepreneurs.

Under Ukrainian law, cross-border loan agreements must be registered with the NBU and compliant with the maximum interest rate limitations established by NBU.

If a payment for services to a non-resident is over EUR 50,000 or its equivalent in UAH, this payment must be approved by the State agency Derzhzovnishinform before the funds can be transferred abroad. The agency verifies whether the amount to be paid is in line with market prices. Ukrainian law provides for a long list of exceptions. For example, no price valuation statement will be required when a payment is made for financial, travel, communication, freight, and forwarding services supplied from abroad, provided that Ukrainian entities have respective licences to carry out relevant business activities.

A further connected restriction of relevance to a foreign investor requires goods and services exported out of Ukraine to be paid for by the receiving foreign entity within 90 days of the date of export. An investor wishing to export oil and gas production would have to ensure payment by its foreign partner within the 90-day period, or face heavy financial penalties.

The investors under the PSA regime, however, are exempted from a number of the above-mentioned restrictions (including the "90-day rule" – the requirement to obtain the individual NBU licence for performance of foreign currency operations, the requirement to limit the interest rate on foreign loans, etc.).

### 3.8 What restrictions (if any) apply to the transfer or disposal of oil and natural gas development rights or interests?

#### The licensing regime

Article 14 of the Oil and Gas Law prohibits the holder of a special permit from any assignment or transfer of the subsoil use rights, as well as contributing them in kind either in the capital of subsidiary companies or the joint activity. Notwithstanding that, the special permit holders are entitled to transfer special permits (as a result of introducing amendments thereto) to a new legal entity (i.e., subsidiary company, joint venture, etc.) provided that the share of the "original" permit holder in a new entity exceeds 50 per cent at the time of such transfer and the equipment, property and other assets needed to continue operations under the special permit were successfully transferred to the new entity.

#### The PSA regime

The PSA Law allows an investor to assign its rights and obligations, subject to the State's consent. In case of a conversion of special permit to the PSA, the special permit holder may apply for the conversion jointly with other co-investors, having no rights in such special permit.

### 3.9 Are participants obliged to provide any security or guarantees in relation to oil and natural gas development?

#### The licensing regime

Special permit holders are not required to provide any bank or parent-company guarantees to the State authorities.

**The PSA regime**

A guarantee of some sort may be required of participants in a PSA tender. Ukrainian law does not provide for a set of standard terms for such guarantees.

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**3.10 Can rights to develop oil and natural gas reserves granted to a participant be pledged for security, or booked for accounting purposes under domestic law?**


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**The licensing regime**

The Oil and Gas Law does not yet allow special permit rights to be pledged or booked for accounting purposes. At the same time, the pledge of minerals (including those which are to be produced by the subsoil user in the future) is not prohibited.

**The PSA regime**

The PSA Law does not make provision for rights under a PSA to be pledged or booked. Theoretically, it could be done with consent from the State.

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**3.11 In addition to those rights/authorisations required to explore for and produce oil and natural gas, what other principal Government authorisations are required to develop oil and natural gas reserves (e.g. environmental, occupational health and safety) and from whom are these authorisations to be obtained?**


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**PSA and licensing regime**

Under both regimes, the following key authorisations must be obtained (amongst others):

- Land acquisition – documents evidencing land use rights, obtained from local authorities.
- Construction works – (i) documents setting out the city-planning requirements to be reflected in the project design, issued by local city-planning and architectural bodies; (ii) approval of the construction project design by local authorities; and (iii) a permit allowing construction and a declaration that the works have been completed, issued by the State Architectural and Construction Inspectorate.
- Regulatory – (i) a special permit obtained from the State Geological Service; (ii) a permit to carry out hazardous works and/or operate hazardous equipment, issued by the State Service for Mining Supervision and Industrial Safety; (iii) a single permit for waste management activities (only if the subsoil user generates waste above the established threshold); (iv) an air pollution permit; (v) a special water use permit (to use water reservoirs or dispose water); (vi) an environmental impact assessment approved by the local representative bodies of the Ministry of Environment and Natural Resources and the State Sanitary-Epidemiological Service; and (vii) a mining allotment when operations reach the production stage issued by the State Service for Mining Supervision and Industrial Safety.

In April 2014 the Law of Ukraine on Reduction of the Number of Permitting Documents came into force. This law abolished 113 permits, consents and authorisations. This measure is to facilitate doing business and to eliminate fraudulent and corrupt practices in conducting activities that require permit (licensing) documents. For example: under the mentioned Law, if a State authority fails to issue a permit within the established deadline, then such permit is deemed to have been issued.

**The PSA regime**

Under the PSA regime, investors enjoy certain privileges. It is much easier to obtain documents permitting the use of land as the land is

allocated to the investor together with the subsoil block. The State also ensures the issue of the necessary authorisations relating to mining and construction.

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**3.12 Is there any legislation or framework relating to the abandonment or decommissioning of physical structures used in oil and natural gas development? If so, what are the principal features/requirements of the legislation?**


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Ukrainian legislation with regard to abandonment and decommissioning is pretty scarce. According to the Subsoil Code and Oil and Gas Law, abandonment and decommissioning are carried out under the control, and upon the consent, of the Committee for Industrial Safety and local authorities. The subsoil user must ensure that no damage is done to people, property and the environment.

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**3.13 Is there any legislation or framework relating to gas storage? If so, what are the principal features/requirements of the legislation?**


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In Ukraine, gas storage facilities (“GSF”) are owned by the State. They are operated by Naftogaz’s subsidiary Ukrtransgaz, which holds the necessary licence, issued by the National Commission on State Regulation of the Energy Sector and Municipal Services (the “Regulator”). Ukrtransgaz is also a holder of the special permit for construction and operation of GSF (for a period of 50 years), issued by the State Geological Service. However, the situation is expected to change soon. As of 14 August 2014, the Parliament of Ukraine has allowed transfers of the State-owned GSF assets to a commercial entity(-ies) for lease on a paid basis by offering European and American investors up to a 49 per cent share in the company.

In line with the Gas Market Law the GSF Operator may not be involved in natural gas production or supply. It should be legally and functionally independent from other types of activities not related to natural gas transportation and storage. Access to GSFs must be granted either on a regulated basis (tariffs to be established by the Regulator) or on the contractual basis (free market prices) in a manner provided by the Gas Storage Facilities Code (i.e. “GSF Code”, a document developed by the GSF Operator and adopted by the Regulator). The GSF Operator must always ensure that each player in the gas market has equal access to the GSF and that gas storage rules provided by the GSF Code are followed.

The gas storage agreement entered between the GSF and the customer must be based on the standard storage agreement developed and approved by the Regulator.

Currently, the gas storage tariffs (as established by the Regulator) stand at UAH 46.2 (USD 2.1) per month per 1,000 cm<sup>3</sup> for storage services and UAH 32.9 (USD 1.5) per 1,000 cm<sup>3</sup> for pumping gas in or out.

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## 4 Import / Export of Natural Gas (including LNG)

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**4.1 Outline any regulatory requirements, or specific terms, limitations or rules applying in respect of cross-border sales or deliveries of natural gas (including LNG).**


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**Export**

Since 2006, the export of natural gas has been subject to mandatory licensing. The licences are issued by the Ministry of Economy of

Ukraine, subject to including the relevant volumes in the annual Prognostic Balance of the Natural Gas Input and Output (which is subject to CMU approval). Export volumes remain insignificant: during recent years, the export of natural gas from Ukraine has not exceeded 90 million cm<sup>3</sup> (exported by Naftogaz to Poland). Naftogaz does not always agree with export requests of private companies and can intentionally obstruct the inclusion of such gas volumes in the draft balance. Therefore, in most cases, the quota for exporting natural gas of Ukrainian origin is either equal to zero or only takes into account the needs of Naftogaz.

Gas produced in the context of a PSA is not subject to export restrictions.

### Import

Since October 2012, any company in Ukraine may import natural gas for further supply to consumers. As a matter of practice, only major market players or smaller companies with a strong lobby could import natural gas in 2013. According to the Ukrainian mass media in 2014, only Naftogaz imported the Russian and European gas to Ukraine.

## 5 Import / Export of Oil

### 5.1 Outline any regulatory requirements, or specific terms, limitations or rules applying in respect of cross-border sales or deliveries of oil and oil products.

#### Export

Similarly to natural gas, the export of oil used to be subject to a licensing and quota regime, with a quota of zero in 2012 and 2013. However, in 2014, oil was removed from the List of Goods Subject to Export Quotas. In 2014-2015, oil has been exported to Lithuania and Moldova.

The export of oil products is not subject to licensing in Ukraine. However, due to the suspension of operations by the biggest exporters and the low level of the national production (only 2.6 million tonnes of oil were processed in 2014, which is 24.5 per cent less in comparison to 2013 data), the export volumes in 2014 were next to nothing.

#### Import

The import of oil and oil products is not subject to licensing. Import operations must comply with the decree of the Ministry of Finance "On Customs Formalities at Pipelines and Power Lines", which sets out in detail the customs clearance procedure, timeframes and a list of the relevant customs points. Due to shut down of the biggest oil refineries, only 305,200 tonnes (-54.7 per cent in comparison to 2013) of oil were imported to Ukraine in 2014, mostly from Belarus.

In 2014, Ukraine imported 6.8 million tonnes of light petroleum products, including 2 million tonnes of gasoline (which is 21.2 per cent less in comparison to the relevant data in 2013) and 4.7 million tonnes of diesel fuel (5.3 per cent less) mostly from: (i) Belarus; (ii) Lithuania; and (iii) Russia.

## 6 Transportation

### 6.1 Outline broadly the ownership, organisational and regulatory framework in relation to transportation pipelines and associated infrastructure (such as natural gas processing and storage facilities).

The principal legislation applicable to natural gas transportation is the Law of Ukraine "On Pipeline Transport" No. 192/96-BP, dated 15 May 1996 (the "Pipelines Law"). Currently, only one State-

owned company – Ukrtransgaz – holds a licence for transportation of natural gas through the main pipelines, and functions as the Operator of the Ukrainian Gas Transportation System (including transit pipelines and storage facilities).

However, in 2014 the Parliament of Ukraine decided to change the ownership structure of the GTS by offering foreign investors up to a 49 per cent share in the company. The potential investor(s) must comply with the following requirements: (i) be owned and controlled by residents of the EU, the US or members of the Energy Community; (ii) be an operator of a gas transportation system or a member of GTE (Gas Transmission Europe); (iii) be certified in accordance with Article 10 of the EU Directive No. 2009/73/EC concerning common rules for the internal market in natural gas and Article 3 of the Regulation (EC) No. 715/2009 on conditions for access to the natural gas transmission networks; and (iv) have at least five years' experience in the management of a gas transportation system in the European or American market. The joint control over GTS should make possible Ukraine's old plans on its modernisation and make other gas transportation projects bypassing Ukraine less attractive for European investors. As of September 2015, CMU did not commence implementation of this ambitious project.

Currently, Naftogaz is the sole owner of Ukrtransgaz. The Gas Market Law provides that unbundling of Naftogaz (in compliance with the requirements of the 3<sup>rd</sup> Energy Package) is to be performed in 2016. CMU has to make a choice between two different models (Ownership Unbundling (OU) and Independent System Operator (ISO)):

**OU model:** The Law provides that this option becomes applicable in Ukraine by default. As a result of its implementation, the production of gas will be effectively separated from gas transmission business. Supply and production companies are not allowed to hold a majority stake in a transmission system operator (TSO), exercise voting rights or appoint its board members.

**ISO model:** Under this option, the transmission pipelines may remain under the ownership of a vertically integrated undertaking; however, operation and control of the day-to-day business must be transferred to an independent system operator.

One of the regulatory novelties introduced by the Gas Market Law is that the Ukrainian GTS will be functioning on the basis of the entry-exit model, meaning that the customers intending to transport natural gas through the system shall not only pay for the transportation services, but would also have to book the capacity with the GTS Operator at the entry/exit points.

A subsidiary of Naftogaz, Ukrtransnafta, is responsible for the transportation of oil through the main oil pipelines.

The company PrykarpatZakhidTrans is responsible for the transportation of oil products. It is a subsidiary of the Southern-Western Open JSC for the Transportation of Oil Products through Pipelines (reportedly owned by Russia). In March 2015 the Ukrainian Supreme Commercial Court recognised Ukraine's ownership of sections of the Samara-Western Direction and Grozny-Armavir-Trudova oil product pipelines located in the Ukrainian territory (1,433 km); however, as of October 2015 PrykarpatZakhidTrans has still not transferred the pipelines to the State Property Fund of Ukraine.

### 6.2 What governmental authorisations (including any applicable environmental authorisations) are required to construct and operate oil and natural gas transportation pipelines and associated infrastructure?

Under article 13 of the Pipeline Law, the design, construction, operation and maintenance of pipelines can only be undertaken by licensed entities. The relevant licences are currently held only by Ukrtransgaz. There are currently no private pipelines operators.

The current state of things might change in the future. Under the PSA Law the PSA investors are now entitled to construct and also operate pipelines in Ukraine. The PSA Law does not establish any specific requirements and/or authorisations needed therefor.

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**6.3 In general, how does an entity obtain the necessary land (or other) rights to construct oil and natural gas transportation pipelines or associated infrastructure? Do Government authorities have any powers of compulsory acquisition to facilitate land access?**

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If the site of a planned pipeline or related infrastructure is on State-owned or municipal land, then the Land Code of Ukraine authorises the State body or local authority that owns the land to lease it for this purpose without the need for a land auction.

In the case of privately owned land, the Land Code allows the owners or users of this land to create easements over it for the purpose of constructing and operating a pipeline. These easements can be created either by contract, by operation of law, or by a court decision.

Governmental authorities cannot expropriate land from landowners. However, the Government and local authorities may purchase land for the purpose of constructing and operating transport networks (including pipelines), subject to the owner's consent, and on the basis of public need. They must contact the owner of the land at least one year before the land is purchased.

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**6.4 How is access to oil and natural gas transportation pipelines and associated infrastructure organised?**

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**Gas**

Under the Gas Market Law, the right of access is granted to all customers subject to compliance with the established requirements. The GTS Operator shall publish access tariffs set by the regulator, available capacity, list of entry/exit points, etc.

The connection procedure is provided by the Gas Transmission System Code (the "GTS Code", which is a document developed by Ukrtransgaz and approved by the Regulator). In general, the customers are allowed to connect to the main gas transportation networks only in the particular instances (for example, if the customer is a gas producing company). No model agreement for access to the transportation networks is provided and the parties are free to determine terms and conditions (subject to compliance with the mandatory requirements established by the GTS Code).

A party wishing to connect to the main gas pipelines must submit an application to the Operator. The latter is obliged to grant access on a non-discriminatory basis and can deny access only in certain circumstances (please refer to question 6.6 below). In response to an application, the operator provides the customer with the technical specifications for interconnection.

**Oil**

As for access to pipelines for oil and oil products, the procedures are set out in technical regulations which are not publicly available.

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**6.5 To what degree are oil and natural gas transportation pipelines integrated or interconnected, and how is co-operation between different transportation systems established and regulated?**

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**Gas**

Currently the Ukrainian gas pipelines are components of the Ukrainian Gas Transportation System ("UGTS"). The day-to-day management of gas flow and pipeline maintenance is undertaken by

Ukrtransgaz, which also co-ordinates the co-operation between the different parts of the system.

**Oil and oil products**

The Ukrainian oil transportation pipelines connect Ukrainian oil refineries and ensure the export of Russian crude oil to the EU. The system is operated by Ukrtransnafta.

Oil products are transported by PrykarpatZakhidTrans via two main corridors (from Ukraine to Hungary and the Slovak Republic), which are parts of the international system for transportation of oil products (connecting Russia, Belarus and Ukraine with the EU).

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**6.6 Outline any third-party access regime/rights in respect of oil and natural gas transportation and associated infrastructure. For example, can the regulator or a new customer wishing to transport oil or natural gas compel or require the operator/owner of an oil or natural gas transportation pipeline or associated infrastructure to grant capacity or expand its facilities in order to accommodate the new customer? If so, how are the costs (including costs of interconnection, capacity reservation or facility expansions) allocated?**

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**Gas**

The Gas Market Law provides for non-discriminatory access to the gas transportation infrastructure. Ukrtransgaz is obliged to grant capacity and to expand the gas transportation system to accommodate demand. If it does not do so, it could be forced to do so at the request of the Regulator or by a court decision.

Access may be denied only if: (1) there is no free transportation capacity; (2) granting an access may hinder the operator from performance of its special obligations on protection of the public interests; and (3) the operator's refusal is substantiated by the Regulator's decision in terms of the 'take-or-pay' obligations (i.e. the Gas Market Law provides that in the event of severe economic and financial difficulties due to non-fulfilment of the 'take-or-pay' obligations, the Regulator may allow the relevant market player not to comply with the rules on equal access to the gas transportation infrastructure).

Ukrtransgaz levies a fee for connection to gas pipelines (in line with the methodology approved by the Regulator). The fee covers connection costs and contributes to the cost of new infrastructure.

**Oil**

As noted in question 6.4, regulations governing access to oil pipelines are not publicly available.

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**6.7 Are parties free to agree the terms upon which oil or natural gas is to be transported or are the terms (including costs/tariffs which may be charged) regulated?**

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**Gas**

The parties must agree the terms for gas transportation using a model gas transportation agreement approved by the Regulator. The tariffs for gas transportation are established by the Regulator and are non-negotiable (currently the average tariff for transportation of natural gas by main pipelines for Ukrtransgaz amounts to UAH 236.70 (USD 10.8) per 1,000 cm<sup>3</sup>). The new (entry-exit) tariffs are expected to become applicable in the new "gas season" (starting from April 2015).

**Oil and oil products**

There is no standard oil (or oil products) transportation agreement publicly available. The prices for transportation services are established by the Regulator and are non-negotiable. The prices vary

according to region and transportation route. For oil transportation, they do not exceed UAH 182 (USD 8.3) per tonne; for oil products, UAH 88 (USD 4) per tonne.

## 7 Gas Transmission / Distribution

### 7.1 Outline broadly the ownership, organisational and regulatory framework in relation to the natural gas transmission/distribution network.

There are two major sectors of gas consumers in Ukraine: 1) residential customers, heat generation plants and organisations funded by State or municipalities; and 2) industrial and commercial customers.

Prior to 1 October 2015 there were two major categories of gas suppliers:

- (a) regulated tariff suppliers; and
- (b) non-regulated tariff suppliers.

Regulated tariff suppliers known as “Oblgazes” were regional gas distribution companies which supplied gas at the regulated tariff mostly to households, State-financed institutions, heat generating companies and also to industrial consumers. They usually conducted their business activity in specific regions of Ukraine, where they also operated the gas distribution networks. In 2015, “Oblgazes” were unbundled into distribution and supply entities, which, however, did not result in total independence in terms of decision-making and corporate control.

The ownership structure of the Oblgazes is ambiguous due to the chaotic history of their privatisation. Currently, the State, as represented by Naftogaz, holds blocking and controlling stakes in a number of them, however Naftogaz mostly fails to exercise operational control, leaving this to private businessmen. As a result, CMU took the decision to sell its stakes and, according to the recent CMU Resolution, Naftogaz intends to transfer the blocking stakes in 36 Oblgazes and controlling stakes in Kyrovogradgaz and Cherkasygas to the State Property Fund for further privatisation in the nearest future.

According to the recent CMU Resolution, until 1 April 2017, the gas suppliers which have executed gas supply contracts with households (i.e. currently, supply entities of Oblgazes) shall be required to perform so-called “public service obligations” (PSOs). PSOs are imposed solely for the purpose of interruptible gas supply to households. In turn, NJSC “Naftogaz of Ukraine” and its affiliate State gas producers will ensure that natural gas of Ukrainian origin is supplied to such gas suppliers at the tariffs established by CMU.

### 7.2 What governmental authorisations (including any applicable environmental authorisations) are required to operate a distribution network?

Historically, private gas traders have not operated gas distribution networks, nor have they supplied gas to households or government-funded organisations in Ukraine. As discussed above, the restructuring of the Oblgazes in 2015 resulted in establishment of separate distribution and supply entities. The companies operating distribution networks must hold licences issued by the Regulator and comply with numerous licensing requirements and safety regulations.

### 7.3 How is access to the natural gas distribution network organised?

The procedure is somewhat similar to the one described in questions 6.4 and 6.6 above, with a due account of the following differences:

- a customer wishing to obtain access to the distribution network and connection services must enter into a contract with the local DSO (i.e. Oblgaz);
- the connection procedure is provided by the Gas Distribution System Code (the “GDS Code”, which is a document developed and approved by the Regulator);
- access is granted by the local DSO on the basis of the relevant agreement as prepared in line with the model agreement for access to the distribution network; and
- the agreement on provision of the gas distribution services is executed directly between the local DSO (Oblgaz) and the consumer (thus, a gas supplier is not obliged by law to ensure that the supplied gas is duly distributed to its consumers).

### 7.4 Can the regulator require a distributor to grant capacity or expand its system in order to accommodate new customers?

The position with respect to requiring the Oblgazes to grant capacity is similar to that as described with respect to Ukrtransgaz in question 6.6.

### 7.5 What fees are charged for accessing the distribution network, and are these fees regulated?

The fees for connection to the gas distribution networks are established by DSOs in compliance with the relevant methodology, approved by the Regulator.

### 7.6 Are there any restrictions or limitations in relation to acquiring an interest in a gas utility, or the transfer of assets forming part of the distribution network (whether directly or indirectly)?

There are no restrictions on the acquisition of shares in a gas utility, save for those relating to competition law matters (please see section 11 on this point). According to CMU Resolution No. 667-p dated 17 July 2014, the privatisation of 38 Ukrainian Oblgazes is to happen in the near future.

Please note that, according to the Gas Market Law, DSOs may not be involved in activities related to natural gas production or supply and should be legally and functionally independent from other types of activities which are not related to natural gas distribution. The Law provides that only small gas distribution companies (i.e. companies with less than 100,000 customers) can be exempt from this requirement, subject to the Regulator’s approval. These independence requirements become applicable starting from 1 January 2016.

## 8 Natural Gas Trading

### 8.1 Outline broadly the ownership, organisational and regulatory framework in relation to natural gas trading. Please include details of current major initiatives or policies of the Government or regulator (if any) relating to natural gas trading.

Prior to 1 October 2015, Ukrainian law provided that the supply of natural gas to end consumers may be carried out in Ukraine either on the regulated tariff or on the non-regulated tariff. In January 2015 there were:

- (i) about 300 companies licensed to supply gas **at the non-regulated tariff** (they are either large industrial companies purchasing gas for their own needs or traders supplying gas to the industrial sector); and

- (ii) 49 companies licensed to supply gas **at the regulated tariff** in Ukraine (i.e. Oblgazes).

Starting from 1 October 2015, both State and private entities (including Oblgazes) are required to obtain the gas supply licence from the Regulator and they have three months (following adoption of the new licensing conditions for gas supply) to do so. In addition, prior to 1 January 2016 Oblgazes shall be required to ensure compliance with the established independence requirements mentioned in question 7.6 above.

## 8.2 What range of natural gas commodities can be traded? For example, can only “bundled” products (i.e., the natural gas commodity and the distribution thereof) be traded?

The range of natural gas commodities that may be traded in Ukraine include natural gas (including coal bed methane and types of unconventional gas) and compressed natural gas. The volume of natural gas is traded by the gas supplier (and the supplier is usually obliged to ensure gas transportation to the point of destination). However, it is the consumer who is responsible for execution of the relevant gas distribution agreement with the local DSO.

## 9 Liquefied Natural Gas

### 9.1 Outline broadly the ownership, organisational and regulatory framework in relation to LNG facilities.

Ukraine has no LNG terminals at present. However, the Government claimed on repeated occasions that construction of the first LNG terminal – in the Odessa region, near the port of Yuzhnyi – is the Government’s priority. In July 2015, Naftogaz reported that a memorandum on the construction of an LNG terminal was signed with Frontera Resources (USA). The American company will work on the possibility of bringing LNG to Ukraine from its ongoing gas exploration projects in Georgia.

### 9.2 What governmental authorisations are required to construct and operate LNG facilities?

Ukrainian law does not specifically provide for the construction and operation of LNG facilities. The authorisations generally required for construction projects will apply here.

### 9.3 Is there any regulation of the price or terms of service in the LNG sector?

The Gas Market Law provides that the tariffs for services of the LNG facilities shall be transparent, non-discriminatory and based on economically justified and transparent costs of the relevant operators. The methodology for calculation of the applicable tariffs shall be developed and approved by the Regulator.

### 9.4 Outline any third-party access regime/rights in respect of LNG facilities.

Access to LNG facilities shall be granted by the LNG Operator. The LNG Operator shall be an entity licensed for operation of the LNG facilities. The Operator may not be involved in natural

gas production or supply; it should be legally and functionally independent from other types of activities, and not related to natural gas transportation and storage. The detailed procedures shall be provided by the LNG Code, as developed by the Operator and approved by the Regulator.

## 10 Downstream Oil

### 10.1 Outline broadly the regulatory framework in relation to the downstream oil sector.

There are six oil refineries in Ukraine:

- Odessa Refinery (owned by VETEK and allegedly transferred to VTB bank);
- Lisichansk Refinery (Rosneft);
- Kherson Refinery (Kontynium);
- Kremenchug Refinery (Ukratnafta and Privat Group);
- Drogobych Refinery (Privat Group); and
- Nadvirna Refinery (Privat Group).

Of these, Lisichansk and Kremenchug are the largest. The refineries’ total primary processing capacity is 51.1 million tonnes of oil per year.

The refining of crude oil and sale of oil products is not subject to licensing in Ukraine. Many of the downstream oil sector’s operations are governed by the regulations in the Instructions on Acceptance, Transportation, Storage, Sale and Accounting of Oil and Oil Products, dated 20 May 2008. Retail sales of oil products by fuel filling stations must comply with the Rules for Retail Sales of Oil Products, dated 20 December 1997, which regulate how filling stations are operated and receive, store and sell oil products.

### 10.2 Outline broadly the ownership, organisation and regulatory framework in relation to oil trading.

Oil traders fall into two categories: State-owned; and privately owned traders. State-owned companies are licensed and can only sell the oil they produce at auctions. A new auction procedure was adopted by CMU in October 2014.

In contrast, private oil producers may sell crude oil directly to oil refineries. They are not required to follow the auction procedure, nor even hold a licence. Each oil producer determines the price of its crude oil independently. Even though private traders are not obliged to hold auctions, some still prefer to do so.

## 11 Competition

### 11.1 Which governmental authority or authorities are responsible for the regulation of competition aspects, or anti-competitive practices, in the oil and natural gas sector?

The Antimonopoly Committee of Ukraine (“AMC”) is responsible for enforcing competition law in Ukraine.

In Ukraine, natural gas transportation, distribution and storage are considered to be natural monopolies. As such, the Regulator is responsible for regulating them. The Regulator’s functions include approving and setting tariffs, establishing the licensing requirements for activities in this sector, and monitoring and controlling them.

### 11.2 To what criteria does the regulator have regard in determining whether conduct is anti-competitive?

Ukrainian law prohibits the abuse of market dominance and anti-competitive concerted practices.

Although holding a dominant position is not, of itself, prohibited in Ukraine, companies having a 35 per cent or greater market share usually fall under the scrutiny of the Ukrainian competition authorities. Abuse of a dominant position is treated as one of the hard-core violations of competition law, triggering significant financial penalties on infringers. Abusive behaviour would include: (i) setting high prices that would be unsustainable in a competitive market; (ii) limiting the supplies of goods on the market when there are no alternative sources of supply; and (iii) excluding competitors from the market.

### 11.3 What power or authority does the regulator have to preclude or take action in relation to anti-competitive practices?

The AMC has a wide range of functions and powers, in particular:

- to monitor and control companies' compliance with competition law;
- to review applications and to investigate suspected infringements;
- to decide whether or not the actions of an entity violate competition law;
- to apply to the competent authorities to withdraw the licences of companies that have violated competition law; and
- to impose fines of up to 10 per cent of revenue.

For its part, the Regulator is authorised:

- to issue instructions and to impose binding resolutions on entities in the natural gas sector; and
- to impose financial penalties and apply sanctions on entities that have violated competition law (e.g., by withdrawing their licence).

### 11.4 Does the regulator (or any other Government authority) have the power to approve/disapprove mergers or other changes in control over businesses in the oil and natural gas sector, or proposed acquisitions of development assets, transportation or associated infrastructure or distribution assets? If so, what criteria and procedures are applied? How long does it typically take to obtain a decision approving or disapproving the transaction?

AMC clearance is required for a transaction if it would result in the market share of the parties (including their affiliates) exceeding 35 per cent.

AMC clearance is also required for the acquisition of 100 per cent of the shares in a company, if the parties to the transaction meet all of the following financial thresholds:

- the worldwide assets or sales of all of the parties to the transaction (including their group entities) exceed EUR 12 million in the financial year preceding the transaction;
- the worldwide assets or sales of at least two parties to the transaction (including their group entities) exceed EUR 1 million each in the financial year preceding the transaction; and
- the Ukrainian assets or sales of at least one party to the transaction (including its group entities) exceed EUR 1 million in the financial year preceding the transaction.

Clearance can be obtained in an average of 45 days (for simple cases) to 4.5 months (for complex cases).

## 12 Foreign Investment and International Obligations

### 12.1 Are there any special requirements or limitations on acquisitions of interests in the natural gas sector (whether development, transportation or associated infrastructure, distribution or other) by foreign companies?

There are, in general, no specific requirements or limitations with respect to foreign companies acquiring interests in Ukrainian oil and gas companies. Foreign companies may also participate in the tenders that are part of the ongoing privatisation process in this sector, unless they fall into one of the following categories:

- legal entities registered in offshore zones and countries black-listed as non-cooperative in the global fight against money laundering and terrorist financing; and
- companies or joint ventures in which either the Ukrainian State or a foreign State have an interest greater than 25 per cent (including via State-owned enterprises).

According to the recent Law on Reforming the System of Management of the Unified Gas Transportation System, foreign investors may own up to 49 per cent shares in the company operating the GTS and/or GSF. The relevant requirements are listed in question 6.1 above.

In June 2015 the Law of Ukraine "On Licensing of Types of Economic Activity" entered into effect. The Law provides for grounds for cancellation of licences (including the licences issued by the Regulator) held by entities under the control of persons from countries undertaking armed aggression against Ukraine and/or creating conditions for armed conflict or use of military force against Ukraine. Although the mentioned Law does not provide for any procedures for background investigation or provision of documentary evidence of such control, the Ukrainian State authorities have already adopted a few decisions against companies with the Russian capital on cancellation of the relevant licences.

### 12.2 To what extent is regulatory policy in respect of the oil and natural gas sector influenced or affected by international treaties or other multinational arrangements?

The regulatory policy in this sector is influenced by relations with the EU and the IMF.

#### EU

Policy is affected by Ukraine's obligations under agreements with the EU, in particular the Energy Charter Treaty, the Protocol on Accession of Ukraine to the Energy Community and the Association Agreement between the EU and Ukraine (as ratified in September 2014).

In September 2014 the Ukrainian Parliament ratified the Association agreement with the EU, which provides for mutual access to commodity markets. This is the first step towards Ukraine's membership to the EU. The ratification is supposed to stimulate implementation of the relevant EU *acquis communautaire*, in particular the Second and Third Energy Packages.

On 9<sup>th</sup> April 2015, the Ukrainian parliament passed the Gas Market Law, which is one of the most significant reforms adopted by the Government so far. The main purpose of the law is to implement legal acts in Ukrainian legislation which regulate the EU gas sector (including the Third Energy Package). This, in turn, is intended to create a competitive gas market in Ukraine in all segments of the

market. The law sets legal and organisational rules for how the gas market should function, provides for gas market de-monopolisation, offers consumer protection and enables consumers to freely choose their gas supplier.

The Gas Market Law spurred a reorganisation of Naftogaz to break up its monopoly over the gas market. The unbundling requirements have been transposed by the Gas Market Law, allowing a choice between ownership unbundling and independent system operator. Certification has to be done by the Government by 1<sup>st</sup> June 2016.

#### IMF

In 2015 the IMF Executive Board approved a four-year extended arrangement under the Extended Fund Facility for Ukraine. The arrangement amounts to USD 17.5 billion and was approved under the Fund's exceptional access policy. The economic programme supported by the Facility will build on and deepen reforms launched under the previous IMF programmes and arrangements. The new economic programme supported by the Fund aims to secure external and financial stability through advancing structural reforms. This includes deregulation and tax administration reforms, and reforms of State-owned enterprises to improve corporate governance and reduce fiscal risks. Broader energy sector reforms, including Naftogaz's restructuring, would increase energy efficiency and foster energy independence.

## 13 Dispute Resolution

**13.1 Provide a brief overview of compulsory dispute resolution procedures (statutory or otherwise) applying to the oil and natural gas sector (if any), including procedures applying in the context of disputes between the applicable Government authority/regulator and: participants in relation to oil and natural gas development; transportation pipeline and associated infrastructure owners or users in relation to the transportation, processing or storage of natural gas; downstream oil infrastructure owners or users; and distribution network owners or users in relation to the distribution/transmission of natural gas.**

Disputes in the oil and gas sector mostly fall within the jurisdiction of the administrative and commercial courts. Disputes with the State authorities and regulators are considered by local administrative courts. Commercial disputes between private companies or between private companies and utilities are considered by the commercial courts.

The PSA Law provides that disputes under a PSA should be considered by the Ukrainian courts unless the parties agree otherwise in the PSA. The parties are therefore free to decide that disputes should be resolved by foreign courts or by international arbitration.

**13.2 Is your jurisdiction a signatory to, and has it duly ratified into domestic legislation: the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards; and/or the Convention on the Settlement of Investment Disputes between States and Nationals of Other States ("ICSID")?**

Yes. The New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards was ratified by the Soviet Union in 1960, and by Ukraine in 1961. Ukraine ratified the ICSID in 2000.

**13.3 Is there any special difficulty (whether as a matter of law or practice) in litigating, or seeking to enforce judgments or awards, against Government authorities or State organs (including any immunity)?**

The Code of Civil Procedure of Ukraine allows enforcement of foreign judgments based on the reciprocity principle. Reciprocal enforcement is now presumed to exist, unless otherwise proved by the respondent.

Ukraine also has a long history of enforcing court decisions made in countries that are signatories to the Minsk Convention on Civil, Family and Criminal Law Issues, Legal Assistance and Legal Relationships (signed in 1993 between CIS countries). Moreover, Ukraine has a number of bilateral legal assistance treaties that provide for the enforcement of foreign judgments, predominantly with formerly socialist countries.

Despite Ukraine's accession to the New York Convention, national courts are still relatively inexperienced in enforcing arbitral awards. As a result there are occasions when judges may be considered to exercise too liberally their discretion to refuse to enforce an award on grounds of public policy. Nevertheless, the overall rate of successful enforcement of foreign judgments and arbitral awards is over 90 per cent.

**13.4 Have there been instances in the oil and natural gas sector when foreign corporations have successfully obtained judgments or awards against Government authorities or State organs pursuant to litigation before domestic courts?**

Yes, there are a number of such instances. The most recent example relates to the arbitration proceedings commenced by JKC Oil & Gas plc and its wholly owned Ukrainian and Dutch subsidiaries ("JKX") against Ukraine. In particular, JKC is seeking repayment of more than USD 180 million in rental fees that its Ukrainian subsidiary has paid on production of oil and gas in Ukraine since 2011.

In June 2015, Pecherskyi District Court of Kyiv upheld an application lodged by JKC to enforce an emergency arbitrator award rendered under the Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce against Ukraine. Apart from being the first enforcement of an award issued by an emergency arbitrator against a State in investment treaty arbitration, the Pecherskyi Court decision also marks the first ever attempt to enforce an emergency arbitrator award in Ukraine. JKC had commenced arbitration proceedings against Ukraine under the Energy Charter Treaty and the Ukraine's bilateral investment treaties with the Netherlands and the United Kingdom. The emergency arbitrator issued a decision ordering Ukraine to refrain from imposing royalties on Poltava Petroleum Company in excess of the rate of 28 per cent (as the Tax Code of Ukraine provided for until 31<sup>st</sup> July, 2014), as opposed to the currently applicable rate of 55 per cent.

## 14 Updates

**14.1 Please provide, in no more than 300 words, a summary of any new cases, trends and developments in Oil and Gas Regulation Law in your jurisdiction.**

2015 appears to be the year of radical reforms in the natural gas market of Ukraine. Ukraine made significant progress in the implementation of the Third Energy Package by adopting the Gas Market Law. Secondary legislation relating to the Gas Market

Law has also come into effect, including: the Gas Transmission System Code; the Gas Distribution System Code; the Gas Code; and the Rules of Supply. The new legislation brings transparency of interactions between gas market actors and simplifies market access.

There have been no significant M&A deals in the oil and gas market in 2015. The recession in the M&A market is explained by two major factors: the significant increase of tax royalties, which has forced producers to put their new exploration programmes on hold; and anticipation of the new legislative and regulatory framework in the gas market sector.



#### Vitaliy Radchenko

CMS Cameron McKenna  
6th floor, 38 Volodymyrska Street  
Kyiv 01030  
Ukraine

Tel: +380 44 391 33 77  
Fax: +380 44 391 33 88  
Email: [vitaliy.radchenko@cms-cmck.com](mailto:vitaliy.radchenko@cms-cmck.com)  
URL: [www.cms-cmck.com](http://www.cms-cmck.com)

Vitaliy is a partner of the Energy and Projects practice at the Kyiv office of CMS Cameron McKenna. His specialties are: Oil and Gas; Mineral Resources; Conventional & Renewable Power Generation; and Energy Commodities Finance & Trading.

Vitaliy was ranked by Chambers Europe 2012-2015 as a Band 1 lawyer in Energy and Natural Resources for Ukraine with commentators identifying him as "a standout figure for energy law in Ukraine" and "a superb lawyer, instrumental to the practice".

Vitaliy is the Co-Chairman of the Fuel and Energy Committee of the American Chamber of Commerce, an active participant of the European Business Association in Ukraine, and is also the first Ukrainian member of Association of International Petroleum Negotiations (AIPN).



#### Inna Antipova

CMS Cameron McKenna  
6th floor, 38 Volodymyrska Street  
Kyiv 01030  
Ukraine

Tel: +380 44 391 33 77  
Fax: +380 44 391 33 88  
Email: [inna.antipova@cms-cmck.com](mailto:inna.antipova@cms-cmck.com)  
URL: [www.cms-cmck.com](http://www.cms-cmck.com)

Inna is a lawyer in the Kyiv office of CMS Cameron McKenna. Since 2008, Inna has been one of the core members of the Energy practice group, working mainly on oil & gas and electricity projects. She has advised major international clients and leading players in the national energy sector with respect to export/import of gas to/from Ukraine, obtaining permits and licences for gas exploration, production, storage and supply, compliance with the national regulations, relationships with the State and third parties. Inna's recent experience includes advising on the concept of reform of the State monopoly "Naftogaz of Ukraine" and development of the secondary legislation to enable the new Gas Market Law. Inna also worked as a secondee for the Kyiv office of an international oil and gas company. She has a deep understanding of the energy sector and combines the very best of in-house and external experience and practices.



CMS Cameron McKenna in Kyiv provides access to more than 25 domestic and internationally qualified lawyers, who combine their understanding of the Ukrainian market with the requirements and expectations of global organisations and investors. Our energy, corporate M&A, banking, dispute resolution, competition and property lawyers specialise in key sectors of the Ukrainian economy, including Energy, Agribusiness, and Technology. With the expertise and experience to deal with transactions and matters of all sizes, CMS handles local, national and multi-jurisdictional projects. Our energy practice group in Kyiv is the leader in the Ukrainian energy sector and the team has been ranked as the Top energy practice in the country (Chambers Europe 2012-2015, the Legal 500, 2015 and Ukrainian Law Firms 2009-2015). Also, according to Chambers Europe 2012-2015, the leading international directory in Europe, CMS Cameron McKenna has been recognised for its excellence in the Energy and Natural Resources sector in Ukraine and has become the Band 1 law firm in this practice area. Vitaliy Radchenko, partner, is recognised by the same directory as a Band 1 lawyer in Energy and Natural Resources for Ukraine with commentators identifying him as "a standout figure for energy law in Ukraine".

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59 Tanner Street, London SE1 3PL, United Kingdom  
Tel: +44 20 7367 0720 / Fax: +44 20 7407 5255  
Email: [sales@glgroup.co.uk](mailto:sales@glgroup.co.uk)

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