

An Abstract on Road Reform in Ukraine



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Development of road infrastructure is vital in promoting economic growth of the countries. Progressive policy regime and legal framework regulating road sector can go a long way in bringing various competitive advantages to the country and greater efficacy for society in general. Managing and conserving the roads is one of the main tasks many states currently need to face, while some of them need to consider it as an urgent priority.

In Ukraine, the condition of an extensive road network leaves a great deal to be desired. As the situation has reached crisis levels, in the past few years, Ukrainian Government has put greater focus on the road infrastructure, introducing various reforms aimed at rescuing the road sector. Numerous alarming issues with regard to provision of an adequate financial support, attraction of investments and implementation of the quality control systems on the roads have been put forward as the main targets to be achieved in the near future.

In 2018 the Ukrainian road industry will get state-guaranteed financing. Starting from 1 January an updated version of the Road Fund was launched, designated to pay for construction and maintenance of the road network. Aimed at increasing the funding of the road sector, the Fund is supposed to be filled with excise duties and taxes on petroleum products, fuel and cars, and, possibly, with fines for the overloaded trucks and speeding violations. Yet, revenues will flow in gradually: in 2018 the Fund will receive only a half of the specified excises and fees; in 2019 it will get 75%; and only in 2020 the Fund will be filled by 100%.

This year, UAH 50 billion are expected to be spent on repairing 4,000 kilometers

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of roads of local and state importance in Ukraine, part of which (UAH 32 billion) is supposed to be taken from the Road Fund. The remaining portion of funds will derive from additional budgetary programs and customs experiments. The Road Fund's money will be used to maintain roads of state importance (60%) and local roads (35%), while the remaining 5% will be directed at implementation of various safety measures on the roads. Referring in particular to the latter point, the Cabinet of Ministers has recently presented the Safe Roads programme, on whose implementation the Government is planning to spend UAH 2.6 billion in 2018.

The responsible organ for the roads of state importance with a total length of 50,000 kilometers will remain the specialized State Automobile Agency of Ukraine (Ukravtodor), which has previously been responsible for the nation's entire road network. The agency, however, had previously failed to prove its capacity to effectively manage, monitor and maintain

the entire road assets of Ukraine, and so decentralization measures have been taken to establish a more suitable system of road management. Accordingly, the local level roads extending on 120,000 kilometers have recently come under the supervision and control of regional state administrations. Although this may be an ambitious step, the transition did not proceed without certain impediment. For example, some administrations have still not yet assigned internal departments or structures responsible for procuring works on the roads and monitoring their implementation. As a result, currently the use of the Road Fund's money at local level is complicated by organizational issues, which need to be addressed and resolved in the shortest term possible.

Besides, the money for construction and maintenance of the roads is expected to come not only from internal revenues and external loans, but also from investors who are willing to buy road management contracts on the concession terms.

In the past couple of years, the Ukrainian Government has been seeking ways to establish and implement a road concession system in order to maintain state's road network within the constraints posed by limited financial resources. In March 2018 the President of Ukraine signed the law, which amended several legislative acts in the field of construction and operation of roads with the aim of attracting investments on concession terms. Despite the risks associated with concession of public roads, this legislative reform has seemed to be a moderate solution taking into account the current condition of Ukrainian road network, as well as other problems facing the sector. The delegation of road administration to private investors will allow the

Government to shift some risks to the private parties while retaining a measure of control over the roads. Besides, it must be admitted that in certain cases, transferring a concession to the private party is the only viable way to construct and maintain a road in the shortest term possible.

According to the law, only roads of state importance can be transferred for construction and operation under concession terms. The Cabinet of Ministers of Ukraine (CMU) adopts a decision on holding a concession tender when the project has showed feasibility to turn to a concession. The CMU also determines the term of concession, compensation mechanism, an alternative road not exceeding double length of the toll road and, finally, the maximum amount of one-way payment for using concessional roads. It is expected that the first concession projects in Ukraine will be the 84-kilometer long Lviv-Krakovets-Korchova road, which should become a modern highway connecting Ukrainian city of Lviv to the European Union's border. At the same time, the market remembers well that talks on construction of this particular road on concession terms began many years ago. The recent reforms and the announcements by the Government provide for further hope that we would finally have the first toll road in Ukraine.

Leaving financial issues aside, another acute problem is proper functioning of the public procurement system in the road industry, as 4,000 kilometers of roads of local and state importance in Ukraine are expected to be repaired in 2018.

It is important to realize that such large volumes of work are complicated by a shortage of companies, which are capable of repairing thousands of kilometers. Hence, the same companies with the necessary equipment and capacity to complete such kinds of projects win the majority of large-scale tenders. This state of affairs does not encourage new enterprises to enter the competition and submit their bids. A small number of contractors taking part in the procurement process stifles competition on the road market and does not benefit greater efficiency and better utilization of taxpayers' money. Nonetheless, the ability to undertake and manage large road construction and reconstruction projects is not the only deterrent factor that produces a monopoly in the industry.

By the same token, the lowest price criteria used in the majority of the tenders to determine the winner, forces the leading contractors, including international con-

struction companies that provide higher quality works using new technologies, materials and equipment, to refrain from presenting their tender proposals. Lower price tags for works on the roads can indeed be regarded a short-term financial saving for the budget, but such economy can result in significant quality and safety losses, which will double the costs imposed on society in the future.

The solution to the monopoly problem in the road sector can lie in motivating small and medium-size road construction companies, as well as foreign contractors, to participate in the tender by *inter alia* break up large tenders into smaller ones, eliminating discriminatory requirements for participation in the tender (e.g. having

relevant experience in particular regions), reassessing tender evaluation criteria, etc. Ultimately, the road sector's monopoly does not benefit the quality of the performed works and hampers development of the Ukrainian road infrastructure in general.

There is no doubt, however, that a commitment to quality will be the key ingredient of any work carried out on state roads. Most roads are worn out and do not meet modern technical requirements. This issue is attempted to be addressed in Ukraine through introduction of various quality assurance systems on the roads. Among such systems currently at play in Ukraine is a quality control and technical audit performed by an independent consulting engineer who is a key figure of the FIDIC's conditions of contracts.

FIDIC stands for the International Federation of Consulting Engineers. FIDIC is an international organization publishing international standard forms of contracts for works and other services related to construction. As indicated previously, FIDIC contracts involve an independent consulting engineer who provides an expert consulting support and supervision during the period of implementation of a construction project. One of the most apparent advantages of the FIDIC forms is their global use for implementation of various construction projects worldwide, which makes it easier for parties from different countries and jurisdictions to have a certain degree of legal certainty as to their rights, obligations and

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liabilities under the contract regulating a specific project.

A few years ago, Ukraine embarked on using FIDIC standard forms in international procurement of construction projects financed by multilateral financial institutions like the EBRD, World Bank and EIB. In 2016, the Cabinet of Ministers of Ukraine adopted a resolution providing for an obligation of an agency that procures the roads construction, reconstruction and repair works to involve an independent consulting engineer to exercise a permanent technical supervision of the project. These measures have started to bear fruit, as to date, several road projects funded by international financial institutions have already been implemented under FIDIC terms, including the repair of H-01 Kyiv-Znamenska and reconstruction of the M-03 Kharkiv-Dolzhenskoye highways.

A point to consider is that despite global usage of FIDIC contracts, they have not yet been officially translated into the Ukrainian language. Besides, case law on the FIDIC form of contract in Ukraine is

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still sparse. This may cause differences with regard to interpretation and enforcement of contracts, leading to the emergence of claims and disputes between parties to a project. In many respects, however, we consider that adapting FIDIC contracts to Ukrainian law is a smart step, which will

lead to expansion of the pool of interested contractors in upcoming large-scale road projects in Ukraine.

While providing important social and economic opportunities, roads present many problems that need to be addressed in due time. However, better late than never. It is only recently that Ukraine has started to take confident steps towards maintaining national roads and for now it is hard to assess the long-term impact of the reforms being introduced. Besides, big challenges await the Ukrainian road sector with regard to maintaining the balance between economic interests and environmental sustainability, as well as finding ways to mitigate the negative impact of roads on ecological conditions. Yet, first things first. Currently, the main tasks of the Ukrainian Government and society in general is to rehabilitate road network from the adverse effects of awful management of roads in recent decades and to prevent neglect in the future.

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