

**Ukraine District Heating
Energy Efficiency Project**

Statement of Sources and
Uses of Funds
for the period from
21 November 2014 till
31 December 2015

This Statement of Sources and Uses of Funds contains 10 pages

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Independent Auditors' Report

To the Ministry of Regional Development, Construction, Housing and Communal Services of Ukraine

We have audited the accompanying Statement of Sources and Uses of Funds of the Ukraine District Heating Energy Efficiency Project (the "Project") for the period from 21 November 2014 till 31 December 2015, and notes, comprising a summary of significant accounting policies and other explanatory information (together "the Statement of Sources and Uses of Funds"). The Statement of Sources and Uses of Funds has been prepared by management using the cash receipts and disbursements basis of accounting described in Note 3 to the Statement of Sources and Uses of Funds.

Management's Responsibility for the Statement of Sources and Uses of Funds

Management is responsible for the preparation of this Statement of Sources and Uses of Funds in accordance with the cash receipts and disbursements basis of accounting described in Note 3 to the Statement of Sources and Uses of Funds, for determining the acceptability of this basis of accounting, and for such internal control as management determines is necessary to enable the preparation of the Statement of Sources and Uses of Funds that is free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on this Statement of Sources and Uses of Funds based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the Statement of Sources and Uses of Funds is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Statement of Sources and Uses of Funds. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the Statement of Sources and Uses of Funds, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the Statement of Sources and Uses of Funds in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, if any, made by management, as well as evaluating the overall presentation of the Statement of Sources and Uses of Funds.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the Statement of Sources and Uses of Funds of the Project for the period from 21 November 2014 till 31 December 2015 is prepared, in all material respects, in accordance with the cash receipts and disbursements basis of accounting described in Note 3.

Emphasis of Matter

We draw attention to Note 2 to the Statement of Sources and Uses of Funds, which describes the political and social unrest and regional tensions in Ukraine that started in November 2013 and escalated in 2014 and afterwards. The events referred to in Note 2 could adversely affect the Project's activities in a manner not currently determinable. Our opinion is not qualified in respect of this matter.

Basis of Accounting and Restriction on Use

Without modifying our opinion, we draw attention to Note 3 to the Statement of Sources and Uses of Funds, which describes the basis of accounting. This Statement of Sources and Uses of Funds is prepared to provide information on cash receipts and disbursements of the Project to the current lenders of the Project. As a result, the Statement of Sources and Uses of Funds may not be suitable for another purpose.

JSC KPMG Audit

JSC KPMG Audit

28 October 2016

Ukraine District Heating Energy Efficiency Project
Statement of Sources and Uses of Funds for the period from 21 November 2014 till 31 December 2015

<i>(in US dollars)</i>	<i>Note</i>	Period from 21 November 2014 till 31 December 2015
Opening balance of cash and cash equivalents		-
Financing received		
<i>IBRD Loan:</i>		
Direct payments from loan account	7	830,000
Transfers from loan account to special account	8	1,651,800
<i>CTF Loan:</i>		
Direct payments from loan account	7	225,000
Transfers from loan account to special account	8	186,600
Total financing		2,893,400
Cash disbursements		
Special purpose programs		-
Front-end fees		1,055,000
Administrative expenses	9	354,160
Total cash disbursements		1,409,160
Closing balance of cash and cash equivalents		1,484,240

The Statement of Sources and Uses of Funds is to be read in conjunction with the notes set out on pages 6 to 10.

1 Background

On 26 May 2014, the International Bank for Reconstruction and Development (the "IBRD"), the Clean Technology Fund (the "CTF") and the Government of Ukraine (the "Borrower") signed loan agreements No.8387-UA and No. TF016327 to finance the Ukraine District Heating Energy Efficiency Project (the "Project"). The objectives of the Project are to improve the energy efficiency and quality of service of the selected Ukrainian district heating companies, improve their financial viability and decrease their carbon dioxide emissions.

The initial cost of the Project was estimated at USD 382,000,000. Sources of financing are the IBRD loan of USD 332,000,000 and the CTF loan of USD 50,000,000.

The Project is scheduled for final completion by the end of the year 2020. Disbursement per loan agreement can be made up to 30 October 2020. The maturity date of the loans from IBRD and CTF is 15 December 2031 and 15 December 2033, respectively.

Ministry of Regional Development, Construction, Housing and Communal Services (the "Ministry") was appointed by the Borrower as the Executor of the Project. The Project is managed by the Central Project Management Unit (CPMU) established within the Ministry.

The Statement of Sources and Uses of Funds is prepared for the reporting period from 21 November 2014 till 31 December 2015.

2 Ukrainian political and economic environment

Ukraine's political and economic situation has deteriorated significantly since 2014. Following political and social unrest, which started in November 2013, in March 2014 various events in Crimea led to the accession of the Republic of Crimea to the Russian Federation, which was not recognised by Ukraine and many other countries. This event resulted in a significant deterioration of the relationship between Ukraine and the Russian Federation. Following the instability in Crimea, regional tensions have spread to the Eastern regions of Ukraine, primarily Donetsk and Lugansk regions. In May 2014, protests in those regions escalated into military clashes and armed conflict between supporters of the self-declared republics of the Donetsk and Lugansk regions and the Ukrainian forces, which continued throughout the date of this Statement of Sources and Uses of Funds. As a result of this conflict, part of the Donetsk and Lugansk regions remains under control of the self-proclaimed republics, and Ukrainian authorities are not currently able to fully enforce Ukrainian laws on this territory.

Political and social unrest combined with the military conflict in the Donetsk and Lugansk regions has deepened the ongoing economic crisis, caused a fall in the country's gross domestic product and foreign trade, deterioration in state finances, depletion of the National Bank of Ukraine's foreign currency reserves, significant devaluation of the national currency and a further downgrading of the Ukrainian sovereign debt credit ratings. Following the devaluation of the national currency, the National Bank of Ukraine introduced certain administrative restrictions on currency conversion transactions, which among others included restrictions on purchases of foreign currency by individuals and companies, the requirement to convert 75% of foreign currency proceeds to local currency, a ban on payment of dividends abroad, a ban on early repayment of foreign loans and restrictions on cash withdrawals from banks. As at the date of this Statement of Sources and Uses of Funds, mentioned administrative restrictions, however, are gradually relaxed by the National Bank of Ukraine as a response to the improving economic conditions.

The above events had a negative effect on Ukrainian companies and banks, significantly limiting their ability to obtain financing on domestic and international markets. The final resolution and the effects of the political and economic crisis are difficult to predict but may have further severe effects on the Ukrainian economy.

Whilst management believes it is taking appropriate measures to ensure continuity of the Project in the current circumstances, a continuation of the current unstable business environment could impair lenders' confidence in liquidity of the Project and negatively affect the availability of funds for future disbursements. This Statement of Sources and Uses of Funds reflects management current assessment of the impact of the Ukrainian business environment on the continuity of the Project. The future business environment may differ from management's assessment.

3 Basis of preparation

This Statement of Sources and Uses of Funds is prepared on the accounting basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than accounting principles generally accepted in Ukraine. On this basis, revenue is recognised when received rather than when earned, and expenditures are recognised when paid rather than when incurred.

4 Foreign currency translation

This Statement of Sources and Uses of Funds is presented in US dollars. Transactions in other currencies are converted to US dollars at the National Bank of Ukraine (NBU) exchange rate effective at the date of the transaction. Cash balances in other currencies are converted to US dollars at the period end NBU exchange rate.

5 Funds withdrawal procedures

IBRD and CTF loans

Funds from the IBRD and CTF loan account are distributed through the special account and as direct payments to suppliers' and contractors' accounts. The special account is a current account with a state owned bank, which was opened and controlled by the Ministry of Finance of Ukraine. All payments to suppliers and contractors from the special account must be approved by the IBRD as eligible expenditures.

In accordance with the application for withdrawal sent to the IBRD by the CPMU, the IBRD may also process direct payments to suppliers' and contractors' accounts in accordance with the provisions of contracts for goods and services as approved by the IBRD.

6 Funds repayment procedure

IBRD loan

Upon signing of the loan agreement No. 8387-UA the Ministry paid a one-off lump-sum commission to the IBRD amounting to USD 830,000 (front-end fee).

The interest is paid on a semi-annual basis charged on the outstanding loan principal. The interest rate is variable based on LIBOR 6m plus variable spread. During the reporting period the average annual interest rate for the loan was 0.68% plus a margin of 1.00% payable by the district heating companies to the Ministry of Finance of Ukraine.

Interest on the IBRD loan is payable twice a year on 15 June and 15 December. The loan principal is repayable in installments twice a year on 15 June and 15 December starting from 15 June 2019.

As at 31 December 2015, the disbursed outstanding balance of loan principal due to the IBRD is USD 2,481,800.

CTF loan

Upon signing of the loan agreement No. TF016327 the Ministry paid a one-off lump-sum commission to the CTF amounting to USD 225,000 (front-end fee).

The interest is paid on a semi-annual basis charged on the outstanding loan principal. The interest rate is 0.75% plus a margin of 1.00% payable by the district heating companies to the Ministry of Finance of Ukraine.

Interest on the CTF loan is payable twice a year on 15 June and 15 December. The loan principal is repayable in installments twice a year on 15 June and 15 December starting from 15 June 2024.

As at 31 December 2015, the disbursed outstanding balance of loan principal due to the CTF is USD 411,600.

7 Direct payments from loan account

Direct payments from loan account for the reporting period are represented by one-off lump-sum commission to the IBRD and the CTF amounting to USD 830,000 and USD 225,000 (front-end fee), respectively.

8 Special account statement

A special account was opened by the Ministry of Finance of Ukraine in state-owned bank PJSC “The State Export-Import Bank of Ukraine”.

Movements on the special account for the period from 21 November 2014 till 31 December 2015 are as follows:

(in US dollars)

Opening balance as at 21 November 2014	-
Movements on special account during the period:	
Transfer from a loan account to special account	1,838,400
Expenditures paid	(354,160)
Closing balance as at 31 December 2015	1,484,240

9 Administrative expenses

Administrative expenses for the reporting period are presented as follows:

(in US dollars)

	Period from 21 November 2014 till 31 December 2015
Consulting services	179,340
Salaries	152,933
Purchase of equipment	21,555
Other	332
Total	354,160

10 Reconciliation of the budgeted financing with the amount of financing used

Reconciliation of the budgeted financing under loans No 8387-UA and No TF016327 with the amount of financing used is as follows:

(in US dollars)

	Budgeted financing	Actual financing used	Available
Goods, works, non-consulting services, consultants' services, and EEI Implementation Cost for special purpose programs:			
Public Power-generating Utility Enterprise "Chernihivska Teploelektrocentral" of LLC "TehNova"	34,905,000	-	34,905,000
Public Utility Enterprise "Dniproteploenerho" of Dnipro Oblast' Council	22,165,000	-	22,165,000
Public Commercial Utility Enterprise "Donetskmiskteplomerezha"	16,755,000	-	16,755,000
Public Utility Enterprise "Kharkivski Teplove Merezhi"	107,300,000	-	107,300,000
Municipal Public Utility Enterprise "Khersonteploenerho"	21,595,000	-	21,595,000
Subsidiary Enterprise "Kirovohradteplo" of Limited Liability Company "Center of Scientific and Technical Innovations of Ukrainian Oil and Gas Academy":	29,615,000	-	29,615,000
Public Utility Enterprise "Miskteplovodenerhia" of Kamianets-Podilskyi City Council	15,320,000	-	15,320,000
Regional Public Utility Enterprise "Mykholaivoblteploenerho"	21,710,000	-	21,710,000
Public Utility Enterprise of Vinnytsia City Council "Vinnytsiamiskteploenerho"	43,320,000	-	43,320,000
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Goods, non-consulting services, consultants' services, training, audit and other operating costs for administration of the Project	5,500,000	354,160	5,145,840
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Front-end Fees	1,055,000	1,055,000	-
	<hr/>	<hr/>	<hr/>
Unallocated	62,760,000	-	62,760,000
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Total	382,000,000	1,409,160	380,590,840
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Eduard Borysovykh Krugliak

28 October 2016

*Deputy Minister of Regional
Development, Construction, Housing
and Communal Services of Ukraine*