The Pragma Corporation

Access to Credit Initiative

Sixth Quarterly Report

For the Period

January 1, 2006 – March 31, 2006

For the

U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT

GENERAL INFORMATION

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KYIV, UKRAINE

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A. PROJECT OVERVIEW

I. PROJECT DESCRIPTION

ATCI is tasked with developing the primary and secondary mortgage market with its associated infrastructure; increased capacity for the leasing industry including the development of certified leasing professionals; the ability for municipalities and utilities to use debt instruments to modernize vital infrastructure, and a credit bureau to facilitate the growth of credit for mortgages- and other retail lending. While the credit bureau/credit rating component is subordinated to the mortgage component, it is being treated as a stand alone for purposes of implementation. The preliminary work plan was presented and accepted by USAID in November 2004.

In response to changing requirements for technical assistance, and a changing political landscape, the work plan is being reviewed quarterly for necessary adjustments. The CTO and COP are working closely to coordinate all technical assistance including defining expected outcomes for each planned activity and the results thereof.

ATCI is cooperating with numerous counterparts and expects to sign a series of formal protocols in addition to those already signed. These Protocols are expected to govern mutual activity as well as manage expectations during the course of the project.

The priorities of the Project for this period are noted by component in the boxes below.

The project update for this quarterly report will correspond to the activities set forth in the action plan described below and reported by component.

II. SIGNIFICANT EVENTS AND ACHIEVEMENTS

- CML COURSE II IS COMPLETED
- PRESIDENT YUSHCHENKO SIGNS MORTGAGE BOND LAW
- THIRD MORTGAGE TRAINING SEMINAR FOR SSMSC IS DELIVERED
- ASSESSMENT OF REAL ESTATE SALES PRACTIONERS AND APPRAISERS BY IRPF IS COMPLETED AND DELIVERED
- FIRST MUNICIPAL PILOT BOND IS ISSUED & PLACED
- INTERNATIONAL WORKSHOP ON CREATING A MUNICIPAL FINANCE FACILITY IS CONDUCTED
- MINISTER OF CONSTRUCTION PAVLO KACHUR FORMALLY REQUESTS USAID'S TECHNICAL ASSISTANCE TO CREATE A BOND BANK.

- FIRST DEPUTY MINISTER OF THE ECONOMY ANATOLY MAKSIUTA COMMITS SUPPORT FOR ESTABLISHING BOND BANK.
- FACILITATED ENTRANCE OF MAJOR EUROPEAN LEASING COMPANIES, *SG EQUIPMENT FINANCE* AND *BANK AUSTRIA~ CREDITANSTALDT LEASING,* INTO THE UKRAININ MARKET;
- CO-ORGANIZED A CONFERENCE ON "THE ROLE OF BANKS IN UKRAINE'S LEASING INDUSTRY,"
- DEVELOPED AND DELIVERED TRAINING & CONSULTING SERVICES TO LESSORS ON '*SALES AND RISK ASSESMENT FOR LEASING TO AGRICULTURAL ENTERPRISES"*
- MINISTRY OF JUSTICE (MOJ) REQUESTS LEGAL ASSISTANCE IN DRAFTING VARIOUS CB REGULATIONS
- ATCI DRAFTS AND SUBMITS LICENCING REGULATIONS TO MOJ
- MOJ REQUESTS ATCI TO DRAFT REGULATIONS GOVERING THE UNIFIED REGISTRY.
- UKRAINIAN PARLIAMENT ADOPTS PERSONAL DATA PROTECTION LAW ON MARCH 16, 2006

III. PROJECT EXECUTIVE SUMMARY

This Report provides details on the events and activities summarized below, as well as other events and activities regarding the USAID Access to Credit Initiative, as implemented by consultants for The Pragma Corporation (the Project), for the period from January, 2006 through March 31, 2006. The report is comprised of four components: Mortgage, Municipal Finance, Leasing and Credit Bureau/Credit Rating. Each component section of the report will have a summary with specific activity tasks identified and the status of each task with appropriate commentary, relevant attachments, and reference to administrative issues, if any.

Mortgage

Development of the primary market continued with the certification of sixteen new CML who successfully completed all three modules of CML Course II. ATCI also continued cooperation with the Ukrainian National Mortgage Association by seconding an analyst to its staff.

Development of the secondary market gathered impetus with passage of the Covered Bond Law. With the formal signing of the coved bond law by President Yushchenko, Ukraine began the year with a legal framework. ATCI met several times with four banks it has signed protocols for issuance of pilot mortgage bonds to discuss how various aspects of the law will be implemented: for example - how to define the appropriate level of bond coverage. Shortly afterward, ATCI took the initiative to contact the SSMSC and offer its assistance to manage the process of drafting the implementing regulations.

Meanwhile, the State Mortgage Institution continued developing its operational procedures in anticipation of a one billion UAH state guarantee. During the quarter, it conducted a tender for placement of corporate securities secured by the government guarantee. The Ministry of Finance and The World Bank (at the request of the Ministry of Finance) prepared for a separate diligence visit to determine SMI's fitness to handle the guarantee. ATCI contributed to the discussion by preparing several discrete memos that detailed ATCI outlook for SMI's being able to credit against mortgages or buy them in response to queries from The World Bank as well as to keep USAID informed of developments. The SMI is preparing for the visit in early April.

ATCI's third direction of activity in mortgage is development of associated market infrastructure. During the quarter, ATCI in cooperation with the International Real Property Foundation, conducted an assessment of real estate sales practices and the state of real estate appraisal in Ukraine. IRPF submitted its report which will be followed by a suggested solution package and accompanying budget. Additionally, ATCI conducted a survey of the insurance industry and determined that many different term life insurance products were available but not widely used in mortgage transactions due to the additional cost that premiums added to already expensive mortgages. ATCI plans to follow – up with a seminar that addresses the role of insurance in mortgages – personal and as well as the role of PMI to make mortgages more affordable.

Lastly, as part of ATCI's continuing cooperation with the SSMSC that impacts the registration of any future securities issuance, ATCI agreed to deliver three seminars on the fundamentals of mortgage lending in three locations throughout Ukraine determined by the SSMSC. The third of these was delivered for twenty-four SSMSC members attending from ten regions.

Municipal Finance

During the quarter Ivano-Frankivsk placed its first bond, which was ATCI's first pilot bond. Ten banks competed to buy the bonds, resulting in favorable terms: 5 years, no put option, 12 percent interest, no fees paid by the city. The winning bidder was Kreschatik Bank. Bonds were listed for trading on the PFTS exchange. ATCI continues its work on the project's second pilot issue with the city of Berdanysk.

The workshop on creating a municipal finance facility featured nine experts from Russia, Sweden, Finland, South Africa, Canada and the US. The workshop attracted top-level government interest, resulting in formation of a task force including senior officials of three ministries (First Deputy Minister Maksiuta, Ministry of the Economy; and Deputy Minister Lisovenko, Ministry of Finance). ATCI delivered a rapid analysis of ownership options for the new facility, and added our recommendations for immediate and medium-term action steps to create the bank. ATCI began acting as secretariat for the working group.

ATCI continued its active involvement in the long-running development of Ukraine's legal framework for local borrowing, as expressed in the Ministry of Finance's draft Law on Local

Borrowing and Guarantees noting for the Ministry of Finance obstacles or contradictions in the draft legislation that impeded efficient borrowing by cities.

Leasing

In this quarter, ATCI focused on building capacity of market participants through delivering advisory services and training, attracting investors and new lessors to Ukraine's leasing market, developing the Certified Leasing Professional (CLP) Program, and improving the legal and tax environment for the development of Ukraine's leasing industry.

Plans to enter Ukraine's leasing market were announced by Bank Austria Creditanstaldt (Unicredit) and SG Equipment Finance (Societe Générale). ATCI assisted both companies in their due diligence process by providing market data, legal and tax analyses, and introducing them to potential partners. Both companies will begin operations in the second half of 2006. ATCI will continue to support both organizations by providing analyses, market information, and contacts. ATCI will continue to pursue foreign lessors, investors, and equipment suppliers in order to attract them to Ukraine and assist them with entering the market.

In its efforts to demonstrate to equipment distributors the efficacy of leasing, ATCI identified two distributors that could function as market leaders. ATCI prepared the first draft of the business plan for Amaco Finance in accordance with the consulting service engagement concluded last quarter with Amako Ukraine Ltd., a US-owned distributor of agricultural machinery in Ukraine. The business plan is vital for Amako Finance to secure adequate funding to meet the Ukraine's significant market demand for medium-term financing of agricultural equipment. In the next two quarters, ATCI will support Amaco Finance to secure funding and build operations. Amaco plans to establish operations in October 2006 in order to begin offering financing by January 1, 2007. The business plan projects approximately $25 million in equipment financing by Amako Finance to Ukrainian agricultural enterprises in the first year.

In its work in training and professional development, ATCI developed the first draft of five of thirteen training modules for the CLP Program along with the Body of Knowledge (a guide to the content included in the program). In the next quarter, ATCI will finish the remaining training modules and focus on building training capacity for the CLP Program.

In other training related activities, ATCI partnered with USAID's Farmer-to-Farmer (FtF) Program, administered by the Citizens Network for Foreign Affairs (CNFA), to deliver training and consulting services to Ukrainian lessors on, *"Sales and Risk Assessment for Leasing to Agricultural Enterprises."* ATCI specialists, together with the FtF expert delivered a two-day training and on-site consulting for three Ukrainian lessors to assist them in developing and implementing an agricultural leasing program based on international standards of best practice. The next of three assignments will be conducted in July, 2006 on *"Marketing and Product Development for Leasing to the Agricultural Industry."*

Credit Bureau/Credit Rating

ATCI's area of focus remained in two basic areas: a) overall coordination of the market given the likelihood of data fragmentation and b) drafting regulations.

Regarding the selection of an international operator, respondents to FNBCH's tender document included Creditinfo, D&B, SCHUFA/KKB and Transunion/CRIF. In March, two companies made the short list: D&B and Transunion/CRIF. Each provided a compelling business proposal on information system delivery, specifications and servicing. Pricing Information with respect to the business proposal included the respondent's best estimate of costs and expenses and fees required of the FNBCB.

The short listed companies specified separate business models for the proposed credit bureau structure that would deal with information on natural persons and legal entities as well as the minimum required functionality and extension options. It is most probable that FNBCH has not yet selected a winner because of an inability to agree on pricing and share ownership. There should be no questions in connection with technical capabilities.

In the previous quarter, the Cabinet of Ministers of Ukraine issued a Resolution in which it assigned the Ministry of Justice of Ukraine to serve as the authorized body responsible for licensing and regulation of credit bureau operations. Pursuant to the Ukrainian Credit Bureau Law, and the authorized body was mandated to draft the regulations governing licensing requirements and other rules for credit bureau operations in Ukraine. The purpose of the regulations is in the first instance to ensure that private information is safeguarded and that bank secrecy laws are not violated.

During the period, the Ministry of Justice requested ATCI to draft at least 3 sets of regulations and to carry out at the MOJ a series of workshops and training for its employees. Personnel at the MOJ (including key specialists involved in the development of regulations) in fact have a very poor idea of what credit bureaus are and how to supervise them. It is for these reasons that the MOJ, at the Deputy Ministerial level, asked us to carry out educational workshops.

ATCI finalized regulations governing licensing requirements. ATCI, FNBCH, Creditinfo, and MOJ agreed on draft licensing regulation. The regulations need to be agreed with the State Committee for Entrepreneurship and Regulatory Issues.

Separately, the Ministry of Justice requested ATCI to prepare materials for and advise the Ministry of Justice ('MOJ') regarding two specific sets of regulations: a) Regulation governing the Unified Registry, and b) Inspection of Credit Bureaus. These regulations will be drafted and negotiated (redrafted) over the course of the next several months. More detailed work with respect to these regulations is expected to commence in the 2nd quarter of 2006. Considering the complex nature of this task, its successful fulfillment will significantly depend on the degree of cooperation and input from all interested parties.

Regardless of which credit bureaus eventually operate in Ukraine's market, the regulation s that ATCI is drafting will apply to any and all.

The situation with regard to further development of the credit rating market (in terms of both operations and legislative regulation) is unclear.

It is quite probable that other rating agencies will fail to meet the SSMSC requirements and "Credit-Rating" will remain the only Ukrainian authorized rating agency (Credit-Rating does not meet the charter capital requirement only). However, with international rating agencies operating in the domestic market Credit-Rating is most likely to lose some of the biggest clients.

In February 2006, the Ministry of Justice drafted the resolution that cancels mandatory ratings for municipalities. Under this resolution municipalities will not have to submit a report on the assignment of credit rating to receive permission for a bond issue. However, progress with this resolution is unclear.

Gender

During the quarter, ATCI conducted activities in three of its four major components while striving for gender balance.

ATCI conducted mortgage training for twenty-four members of the SSMSC staff, eighteen of whom were women. In CML training, three women and thirteen men were certified. In a seminar ATCI conducted on developing municipal finance liquidity facilities, eight-three participants (twenty-five women) learned how bond banks function around the world. One hundred sixty persons (fifty women) participated in the two leasing activities conducted by ATCI on risk management; leasing and banking.

Other

NONE

IV. PROJECT STAFFING

The following personnel were engaged in project activities this quarter:

- David Lucterhand, Chief of Party
- Richard Genz, Senior Advisor, Municipal
- Richard Caproni, Senior Advisor, Leasing
- Javier Piedra, Senior Advisor, Credit Bureau
- Bob Homans, Senior Advisor, Leasing
- Jim Butler, Senior Advisor, Mortgage
- Olexander Kopeikin, Advisor, Mortgage
- Natalia Rogozhina, Advisor, Mortgage
- Steve Moody, Senior Advisor, Mortgage
- Dr. Wayne Thirsk, Senior Advisor, Municipal
- Francis J. Conway, Advisor, Municipal
- Johan Kruger, Advisor, Municipal
- Michael Curley, Advisor, Municipal

- Michael DeAngelis, Advisor, Municipal
- Sergey Sivayev, Advisor, Municipal
- Nicholas Anderson, Advisor, Municipal
- Lars Andersson, Advisor, Municipal
- Dr. John E. Petersen, Advisor, Municipal
- Norman Flynn, Advisor, Mortgage

V. ADMINISTRATIVE ISSUES

NONE

B. MORTGAGE

I. COMPONENT DESCRIPTION

This Report provides details on the events and activities relating to the Mortgage Component of the USAID Access to Credit Initiative, as implemented by The Pragma Corporation, during the period from January 1, 2006 through March 31, 2006.

The primary purpose of the ATCI is to develop the primary and secondary mortgage market with its associated infrastructure. Primary market development involves legal review and addressing legislative deficiencies, the use of standardized documentation for underwriting and loan servicing, certification of personnel for mortgage lenders that results in a CML designation; technical assistance to financial institutions engaged in mortgage lending, and assessment of titling and all related processes. Development of the secondary market involves assistance to the newly formed state Mortgage Institution to become operational, development of national mortgage insurance as well as private, term life, and the structuring of mortgage-backed bonds with the appropriate legal environment for issuance. Associated market infrastructure involves appraisers, registration centers, real estate sales practitioners, and appropriate regulation.

While the credit bureau component is subordinated to the mortgage component, it is being treated as a stand alone for purposes of implementation.

II. SIGNIFICANT EVENTS

- PRESIDENT YUSHCHENKO SIGNS MORTGAGE BOND LAW
- CML COURSE II IS COMPLETED
- THIRD MORTGAGE TRAINING SEMINAR FOR SSMSC IS DELIVERED
- ASSESSMENT OF REAL ESTATE SALES PRACTIONERS AND APPRAISERS BY IRPF IS COMPLETED AND DELIVERED

III. EXECUTIVE SUMMARY

2006 began with President Yushchenko signing the covered bond bill into law in early January - setting the stage for development of Ukraine’s secondary mortgage market.

ATCI continued its development of the primary mortgage in league with SMI and UNIA completing the third CML module of Course II. The CML candidates receiving the training are from local financial institutions and the SMI. Sixteen received certification. *(See attached photos)*

Development of the secondary market gathered impetus with passage of the Covered Bond Law. With the formal signing of the coved bond law by President Yushchenko, Ukraine began the year with a legal framework. ATCI met several times with four banks it has signed protocols for issuance of pilot mortgage bonds to discuss how various aspects of the law will be implemented: for example - how to define the appropriate level of bond coverage. Shortly afterward, ATCI took the initiative to contact the SSMSC and offer its assistance to manage the process of drafting the implementing regulations. The SSMSC asked that ATCI spearhead this effort in association with UNIA. ATCI retained a specialist who had helped to draft the covered bond law to coordinate ATCI activity with mortgage legal specialist Jim Butler. Several meetings took place with the SSMSC. The SSMSC tasked ATCI with drafting regulations dealing with coverage ratio and functions of the bond manager while coordinating other working groups to meet Commission deadlines. This work will continue through the seventh quarter.

While the most significant event in terms of developing the secondary market was passage of the Mortgage Bond law, ATCI has been providing support to the SMI in its development as a liquidity facility, and cooperating with three financial institutions UkrSibbank, Ukrsotsbank, and UkrGasBank to develop pilot mortgage bonds. Letters of confidentiality have been signed with each bank. Discussion with each have involved diagnostics regarding the complexion of their portfolios. In anticipation of the passage of the law "On Mortgage Bonds," ATCI senior advisors began developing mortgage portfolio reporting procedures and interviewing three potential bank/issuers. Accurate and timely mortgage pool reporting is the mainstay of "covered bonds" and, given that mortgage pools can contain thousands of individual mortgages, the reporting process must both very simple and highly automated. Now that passage has occurred, discussion has moved from the theoretical to the practical.

In fact, the first criterion for qualifying a potential issuer is the degree of automation of its loan portfolio. The initial discussions with UkrSibbank, Ukrsotsbank and UkrGazBank revolved about the ability of the banks' software to extract specific information from loan ledgers and, subsequently, to generate specific reports on the condition of the mortgage pools. The "Report on the Condition of Mortgage Coverage" summarizes the key attributes of the mortgage pool: number of mortgages in the pool, current outstanding balance (value) of the pool, weighted average interest rate, weighted average term, and the percentage of residential (as opposed to commercial) mortgages. The issuer will make this report quarterly to the Trustee will in turn instruct the issue's auditor to verify or refute the issuer's claims.

Of course, for mortgage pools with thousands of mortgages (Ukrsotsbank's dollar-denominated mortgage pool contains more than five thousand mortgages), the auditor cannot examine every mortgage. Instead, the auditor randomly samples the pool; the size of the random sample is determined using specific statistical techniques involving two delimiters—precision intervals and confidence intervals. Using 95% confidence intervals (two standard deviations), it is possible to reduce the representative sample size to fewer than two hundred mortgages.

However, the auditor does not actually "audit" or "review" the representative sample; the auditor performs an "agreed-upon procedure," specifically designed to determine if the sample (and therefore the entire mortgage pool) conforms with the requirement in the law. For example, the procedure will check that all loans in the sample are standard (i.e., performing) assets, that the Loan to Value Ratio (LTV) does not exceed 75% and that commercial mortgages do not represent more than 15% of total mortgages. Such an agreed-upon procedure is considerably less time-consuming and expensive than an audit or a review. *(See attachment 1)* From initial discussions, it appears that software at both Ukrsibbank and Ukrsotsbank will be able to sort the loan portfolios by required fields and generate the required reports. Ukrgazbank will have to conduct a test of its software.

Meanwhile, the State Mortgage Institution continued developing its operational procedures in anticipation of a one billion UAH state guarantee. During the quarter, it conducted a tender for placement of corporate securities secured by the government guarantee. The Ministry of Finance and The World Bank (at the request of the Ministry of Finance) prepared for a separate diligence visit to determine SMI's fitness to handle the guarantee. ATCI contributed to the discussion by preparing several discrete memos that detailed ATCI outlook for SMI's being able to credit against mortgages or buy them in response to queries from The World Bank as well as to keep USAID informed of developments. The SMI is preparing for the visit in early April.

ATCI's third direction of activity in mortgage is development of associated market infrastructure. During the quarter, ATCI in cooperation with the International Real Property Foundation, conducted an assessment of real estate sales practices and the state of real estate appraisal in Ukraine. IRPF submitted its report along with a suggested solution package. *(See attachments 2 & 3)*

As part of ATCI's continuing cooperation with the SSMSC that impacts the registration of any future securities issuance, ATCI agreed to deliver three seminars on the fundamentals of mortgage lending in three locations throughout Ukraine determined by the SSMSC. The third of these was delivered Kiev *(see attached photos).* Twenty-four SSMSC staff members attended from ten regions. ATCI has received a request by the SSMSC for further training in mortgage covered bonds.

IV. ADMINISTRATIVE ISSUES

Determining what level of LOE will be optimal to both structuring the pilot issue while setting the legal standard for all subsequent covered bond issues.

V. DESCRIPTION AND STATUS OF TASKS

Task 1. Mortgage - Certified Mortgage Lender Program

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **IUE review of training materials for applicability to Ukraine**	• WORK COMMENCED IN COOPERATION WITH THE UNIA AND SMI TO REVISE CML COURSEWORK FOR DELIVERY IN UKRAINE.
• **Selection of candidates for CML training**	• IN COOPERATION WITH UNIA AND SMI, ATCI SELECTS THE BANKS AND OTHER INSTITUTIONS FOR STAFF TRAINING.
• **Develop and administer CML training**	• COURSE MODIFICATION FOR DELIVERY IN UKRAINE IS COMPLETED AND READY FOR DELIVERY
• **Deliver two complete CML courses**	• DURING THE QUARTER, CML MODULE 3 (FINAL) FOR COURSE II WAS DELIVERED. SIXTEEN PERSONS RECEIVED CERTIFICATIONS
• **Assess rural lending, titling registration, appraisal of profitable agricultural production units**	• THIS ACTIVITY IS EXPECTED TO BEGIN AFTER THE LAND LAW IS PASSED

Task 2. Mortgage - Assistance to Banks

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Standardize rules and procedures for retail mortgage lending**	• ATCI, EBED, UNIA, AND SMI HAVE ALL AGREED TO SET ONE STANDARD FOR MBS ISSUANCE. SOME BANKS ARE CHAFING AT USING THEM FOR COMPETITIVE REASONS. NONETHELESS, MORTGAGE BONDS WILL REQUIRE UNIFORM STANDARDS FOR ISSUANCE. WITH PORTFOLIO ANALYSIS UNDERWAY, ATCI WILL SOON BE ABLE TO DETERMINE THE EXTENT TO WHICH COMMON STANDARDS ARE BEING USED THROUGHOUT THE INDUSTRY.
• **Select candidate banks for receipt of on –site technical assistance**	• THE SAME BANKS THAT HAVE STAFF PARTICIPATE IN CML TRAINING WILL BE THE SAME WHO RECEIVE ON SITE TECHNICAL ASSISTANCE
• **Provide on – site technical assistance**	• THIS IS NOW UNDERWAY AT SEVERAL BANKS WHOSE STAFF HAVE ACHIEVED CML DESIGNATION

Task 3. Mortgage - Home Loan Guarantee

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• Analyze market for existing mortgage insurance practices	• THIS ASSESSMENT WAS COMPLETED DURING THE FOURTH QUARTER.
• Assess legal and regulatory framework	• ASSESSMENT IS CONTINGENT ON ATCI IDENTIFYING A CHAMPION .FOR THE GUARANTEE FUND INSIDE THE GOU.
• Complete Feasibility Study	• THIS WILL COMMENCE AFTER COMPLETION OF THE ASSESSSMENT AND THE CHAMPION AGREES TO PROCEED
• Complete Business Plan	• THIS WILL FOLLOW THE FEASIBILITY STUDY
• Assist in operational set-up of guarantee facility	• NOTHING DONE THIS QUARTER
• Provide on-site technical assistance to facility	• NOTHING DONE THIS QUARTER
• Promote the use of mortgage insurance	• ATCI IS LOOKING FOR A SPONSOR TO DISCUSS THE ROLE OF A STATE MORTGAGE GUARANTEE FUND. DISCUSSIONS REGARDING THE USE OF PRIVATE MI WITH BANKS, UNMA AND THE NMB OCCUR WHEN POSSIBLE. ATCI CONTINUES TO PROMOTE THE IDEA WITH THE SMI.AND EXPECTS TO HOST A CONFERENCE DURING THE EIGTH QUARTER THAT WILL MARRY MORTGAGE BOND ISUANCE TO INCREASED AFFORDABILITY AND INCREASED SECURITY FOR INVESTORS

Task 4. Mortgage - Life Insurance Products

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• Analyze insurance and mortgage markets for existing products	• ATCI COMPLETED AN ANALYSIS OF RELATED MORTGAGE INSURANCE PRODUCTS AS WELL AS THE INSTITUTIONS OFFERING THEM. SEVERAL COMPANIES ARE OFFERING MORTGAGE TERM-LIFE INSURANCE PRODUCTS. HOWEVER, THE ASSESSMENT DETERMINED THAT BANKS ARE NOT REQUIRING THESE POLICIES BECAUSE THEY ADD TO THE COST OF THE MORTGAGE. FURTHER DISCUSSION IS ANTICIPATED WHEN ATCI HOLDS A ROUNDTABLE REGARDING COVERED BONDS AND THE ROLE OF PMI DURING THE EIGHTH QUARTER.
• Assess legal and regulatory framework	• NO ACTION TAKEN THIS QUARTER
• Assess existing actuarial data	• NO ACTION TAKEN THIS QUARTER
• Select candidate insurers	• ASSESSMENT PHASE IS UNDERWAY
• Develop term sheet and rate structure	• NO ACTION TAKEN THIS QUARTER
• Draft Product policy	• NO ACTION TAKEN THIS QUARTER
• Conduct Road Show with mortgage lending banks and financial institutions	• NO ACTION TAKEN THIS QUARTER

Task 5. Mortgage - Appraisers/Brokers Associations

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Assessment of UTO and other organizations**	• ASSESSMENT COMPLETED BY IRPF AND SOLUTION PACKAGE OFFERED.
• **Facilitate development and use of unified methodology**	• NO ACTION TAKEN THIS QUARTER
• **Work with UAREP**	• NO ACTION TAKEN THIS QUARTER
• **Study tours to U.S.**	• NO ACTION TAKEN THIS QUARTER
• **Design, establish and sustain the transaction and price database**	• NO ACTION TAKEN THIS QUARTER

Task 6. Mortgage - Mortgage Backed Securities

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Establish Legal Working Group to assess legal and regulatory basis**	• ATCI PARTICIPATED IN WORKING GROUPS WITH UNIA AND CLC.TO AFFECT PASSAGE OF THE MORTGAGE BOND LAW. ATCI IS PARTICIPATING WITH UNIA AND THE SSMSC IN DRAFTING THE IMPLEMENTING RULES AND REGULATIONS.
• **Select Candidate Issuer**	• ATCI IS WORKING WITH UKRAGASBANK, UKRASOTSBANK, AND UKRASIBBANK. .MOST PORTFOLIOS ARE DOLLAR DENOMINATED. MORTGAGES DENOMINATED IN LOCAL CURENCY ARE IMPORTANT TO MITIGATE CURRENCY RISK IN DOMESTIC ISSUANCE. THIS IS NOT THE CASE FOR INTERNATIONAL ISSUANCE. LETTERS OF CONFIDIENTIALITY HAVE BEEN SIGNED BY EACH BANK. CURRENT ACTIVITY INVOLVES PORTFOLIO ANALYSIS TO DETERIMINE THE QUALITY OF MORTGAGE COLLATERAL, DENOMINATION OF THE MORTGAGES SELECTED FOR INCLUSION IN THE POOL AND SUITABILITY FOR ISSUANCE; AND DEVELOPMENT OF STANDARDIZED MECHANISMS FOR AUDITING THE COVERAGE OF THE MORTGAGE POOL.
• **Draft investment memorandum**	• DRAFTING IS EXPECTED TO BEGIN DURING THE SEVENTH QUARTER AND IS PREDICATED ON COMPLETION OF IMPLEMENTING RULES AND REGULATIONS.
• **Identify potential investors**	• THE COP AND ADVISORS HAVE MET WITH POTENTIAL INSTITUTIONAL INVESTORS TO DESCRIBE COVERED BONDS AND TO GAGE INVESTMENT INTEREST. LIFE INSURANCE COMPANIES AND ASSET MANAGERS OF PRIVATE PENSION FUNDS APPEAR TO BE LIKELY INVESTORS BUT PFTS IS THE LIKELY MECHANISM FOR DISTRIBUTION. • SMI HAS INVESTED AS PILOTS IN SOME WHOLE MORTGAGES PRECEDENT TO ANY SECURITIZED ISSUE. SMI NEEDS MORE CAPITAL FOR INVESTMENT AND SYSTEMS TESTING. A STATE GUARENTEE REPRESENTS ONE SOURCE; ANOTHER IS AN INCREASE IN STATUTORY CAPITAL.
• **Price and Place Issue**	• NO ACTION TAKEN THIS QUARTER

LIST OF ATTACHMENTS

C. MUNICIPAL FINANCE

I. COMPONENT DESCRIPTION

The municipal finance program of the Access to Credit Initiative helps cities and communal service enterprises issue long-term bonds for essential infrastructure. The program is also promoting the development of a municipal finance facility in Ukraine.

Technical assistance from the program's team of Ukrainian and international experts in finance, accounting, and law will enable at least three municipalities or communal enterprises to issue bonds. The pilot bonds will demonstrate practices that creditworthy issuers employ to win investor confidence, such as transparent accounts, full disclosure, and financing capital projects that "pay for themselves" with cost savings.

Pilot bonds will disclose legal and regulatory obstacles to bond issuance. The bond program will develop solutions and advocate for their enactment. Legal goals include promotion of stable, predictable central government transfers to municipalities, greater fiscal autonomy for cities, and full-cost recovery tariffs for utility companies.

Key counterpart organizations supporting the bond program are the Association of Ukrainian Cities and the Ministry of Construction, Architecture and Housing and Communal Economy.

II. SIGNIFICANT EVENTS AND ACHIEVEMENTS

- CITY OF IVANO-FRANKIVSK PLACED ITS FIRST BOND ISSUE OF UAH 5.5 MILLION.
- CONSULTANT FRANCIS CONWAY PREPARED RECOMMENDATIONS FOR REVISIONS TO ATCI'S SPREADSHEET MODEL FOR EVALUATING CREDITWORTHINESS.
- CONDUCTED INTERNATIONAL WORKSHOP ON CREATING A MUNICIPAL FINANCE FACILITY.
- MINISTER OF CONSTRUCTION PAVLO KACHUR FORMALLY REQUESTED USAID'S TECHNICAL ASSISTANCE TO CREATE A BOND BANK.
- MET WITH FIRST DEPUTY MINISTER OF THE ECONOMY ANATOLY MAKSIUTA AND RECEIVED A COMMITMENT OF SUPPORT FOR ESTABLISHING BOND BANK.
- ATCI CONSULTANT JOHN PETERSEN ANALYZED STRENGTHS, WEAKNESSES, OPPORTUNITIES AND THREATS (SWOT) OF POSSIBLE OWNERSHIP STRUCTURES FOR A BOND BANK.

- COMPLETED BOND CAPACITY ASSESSMENT OF THE CITY OF BERDYANSK.

- PREPARED COMMENTS ON THE MINISTRY OF FINANCE'S LATEST DRAFT LAW ON LOCAL BORROWINGS AND LOCAL GUARANTEES.

- BRIEFED GARY LINDEN OF USAID ON THE IMPACT OF RECENT CHANGES IN UKRAINIAN BUDGET LEGISLATION ON MUNICIPAL CREDITWORTHINESS.

- RE-VISITED THE CITY OF CHERKASY TO DISCUSS BOND ISSUANCE BY ITS WATER AND HEAT UTILITIES.

III. EXECUTIVE SUMMARY

During the quarter Ivano-Frankivsk placed its first bond, which was ATCI's first pilot bond. Ten banks competed to buy the bonds, resulting in favorable terms: 5 years, no put option, 12 percent interest, no fees paid by the city. The winning bidder was Kreschatik Bank. Bonds were listed for trading on the PFTS exchange.

The workshop on creating a municipal finance facility featured nine experts from Russia, Sweden, Finland, South Africa, Canada and the US. *(See attached photos)* The workshop attracted top-level government interest, resulting in formation of a task force including senior officials of three ministries (First Deputy Minister Maksiuta, Ministry of the Economy; and Deputy Minister Lisovenko, Ministry of Finance). ATCI delivered a rapid analysis of ownership options for the new facility, and added our recommendations for immediate and medium-term action steps to create the bank. ATCI began acting as secretariat for the working group. *(See attachment 4)*

ATCI is in the planning stage to develop an options paper for bond bank with support from international finance, bond banking, and legal experts *(See attachment 5).* Additionally, the ATCI is providing technical support to the bond bank task force and is taking steps to institutionalize the task force, in view of the coming change in the government following March elections.

ATCI continued its active involvement in the long-running development of Ukraine's legal framework for local borrowing, as expressed in the Ministry of Finance's draft Law on Local Borrowing and Guarantees.

The Municipal advisory team refined its understanding of the credit risks of municipal borrowing with expert help from consultants Wayne Thirsk and Francis Conway *(See attachment 6).* ATCI consultant Wayne Thirsk and Richard Genz briefed Gary Linden of USAID on the impact of recent changes in Ukrainian budget legislation on municipal creditworthiness. Credit assessment will be a core activity of any future bond bank.

The municipal advisory group also sought out new clients for pilot bond issuance, which has included a visit to Berdyansk - planned to be our next bond client, and Cherkasy. At the invitation of local Rada deputy and director of European Integration Pavlo Karas, we re-visited the city of Cherkasy to discuss bond issuance by its water and heat utilities. The water company is thought to be profitable, but despite numerous attempts we have not been able to get financial data. Unfortunately neither enterprise chose to send a representative to the meeting and as of the end of the quarter, nothing had resulted from the effort. Other potential cities for pilot issuance the municipal advisory group is looking at include the City of Lugansk, the City of Yalta, Rivne Oblast Vodakanal, and Lugansk Oblast Vodakanal.

IV. ADMINISTRATIVE ISSUES

NONE

V. DESCRIPTION AND STATUS OF TASKS

Task 1. Municipal Finance – Constraints to Bond issuance

Defined Activity	PROGRESS MADE DURING QUARTER/PROPOSED FUTURE ACTIONS
• **Monitor GOU intergov't finance practices for credit risks**	• PRESENTED SUMMARY FINDINGS TO GARY LINDEN, DIRECTOR, OEG, USAID/KYIV
• **Participate in Drafting on Law on Local Borrowing**	• CONSULTANTS MICHAEL DEANGELIS AND A. J. HEATH DELIVERED POLICY AND TECHNICAL COMMENTS ON THE DRAFT LAW TO THE MINISTRY OF FINANCE.

Task 2. Municipal Finance – Prepare for a Pilot Issue

Defined Activity	PROGRESS MADE DURING QUARTER/PROPOSED FUTURE ACTIONS
• **Initiation of pilot**	• DELIVERED FINAL BOND CAPACITY ASSESSMENT FOR BERDYANSK. • FRANCIS CONWAY DELIVERED RECOMMENDATIONS FOR CREDIT EVALUATION METHODOLOGY.

Task 3. Municipal Finance – Issuance

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Implementation**	• IVANO-FRANKIVSK ISSUED ITS FIRST BOND, UAH 5.5 MILLION.

Task 4. Municipal Issuance – Legislation and Dissemination

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Workshops and public education**	• FOR CO-SPONSORS THE MINISTRY OF FINANCE, MINISTRY OF CONSTRUCTION, AND USAID, ATCI PRESENTED A WORKSHOP ON ESTABLISHING A MUNICIPAL BOND BANK, INCLUDING NINE INTERNATIONAL EXPERTS.

LIST OF ATTACHMENTS

ATTACHMENT 4 Agenda for Workshop on Creating a Municipal Finance Facility for Ukraine.

ATTACHMENT 5 *Municipal Finance Facility Ownership Structures: A SWOT Analysis* by John Petersen.

ATTACHMENT 6 *Key Financial Risk Factors for Ukraine's Cities* by Francis Conway.

D. LEASING

I. COMPONENT DESCRIPTION

This report details events and activities relating to the Leasing Component of the USAID Access to Credit Initiative, implemented by the Pragma Corporation, during the period from January 1 through March 31, 2006.

The primary purpose of the Leasing Component is not only to create a supportive environment for modern financial leasing but to provide specific technical, advisory, and training assistance in order to increase access to credit throughout Ukraine. Leasing is an efficient alternative to bank financing.

ATCI will aim to strengthen existing leasing companies. Capacity building will consist of training and consulting for lessors, lessees, farmers, regulators, and other interested parties, such as vendors and banks. In addition, ATCI will seek potential foreign and local investors as well as conduct public awareness efforts.

Moreover, the Leasing Component will develop the cadre of leasing professionals by introducing the Certified Leasing Professional Program (CLPP), a designation for market participants so that they may attain world standards of practice.

ATCI will continue to support and/or develop the proper legislative and regulatory framework to support the leasing industry and facilitate the entry of foreign capital into the leasing sector.

II. SIGNIFICANT EVENTS

- FACILITATED ENTRANCE OF MAJOR EUROPEAN LEASING COMPANIES, *SG EQUIPMENT FINANCE* AND *BANK AUSTRIA~ CREDITANSTALDT LEASING,* INTO THE UKRAININ MARKET;

- IMPLEMENTED IMPROVEMENTS TO THE BUSINESS AND OPERATIONAL STRATEGY OF LEASEIT, UKRAINE'S FIRST SMALL-TICKET LESSOR

- DEVELOPED FIRST DRAFT OF BUSINESS PLAN FOR AMACO FINANCE, THE FIRST CAPTIVE LESSOR OF AGRICULTURAL MACHINERY TO ENTER THE UKRAINIAN MARKET

- CO-ORGANIZED A CONFERENCE ON "THE ROLE OF BANKS IN UKRAINE'S LEASING INDUSTRY,"

- DEVELOPED AND DELIVERED TRAINING & CONSULTING SERVICES TO LESSORS ON '*SALES AND RISK ASSESMENT FOR LEASING TO AGRICULTURAL ENTERPRISES'*

- DEVELOPED THE FIRST FIVE OF THIRTEEN TRAINING MODULES FOR THE CERTIFIED LEASE PROFESSIONAL (CLP) PROGRAM

III. EXECUTIVE SUMMARY

In this quarter, ATCI focused on building capacity of market participants through delivering advisory services and training, attracting investors and new lessors to Ukraine's leasing market, developing the Certified Leasing Professional (CLP) Program, and improving the legal and tax environment for the development of Ukraine's leasing industry.

Plans to enter Ukraine's leasing market were announced by Bank Austria Creditanstaldt (Unicredit) and SG Equipment Finance (Societe Générale). ATCI assisted both companies in their due diligence process by providing market data, legal and tax analyses, and introducing them to potential partners. Both companies will begin operations in the second half of 2006. ATCI will continue to support both organizations by providing valuable analyses, market information, and contacts. ATCI will continue to pursue foreign lessors, investors, and equipment suppliers in order to attract them to Ukraine and assist them with entering the market.

In its efforts to demonstrate to equipment distributors the efficacy of leasing, ATCI identified two distributors that could function as market leaders. ATCI prepared the first draft of the business plan for Amaco Finance in accordance with the consulting service engagement concluded last quarter with Amako Ukraine Ltd., a US-owned distributor of agricultural machinery in Ukraine. The business plan is vital for Amako Finance to secure adequate funding to meet the Ukraine's significant market demand for medium-term financing of agricultural equipment. In the next two quarters, ATCI will support Amaco Finance to secure funding and build operations. Amaco plans to establish operations in October 2006 in order to begin offering financing by January 1, 2007. The business plan projects approximately $25 million in equipment financing by Amako Finance to Ukrainian agricultural enterprises in the first year. (The executive summary for the business plan is found in *(See attachment 7)*

ATCI assisted LeaseIT, Ukraine's first small-ticket (average transaction of 3,000 USD) lessor, to implement improvements to their operational and business strategy that the project recommended in the previous quarter. These improvements, along with financial models and investment proposals that ATCI developed, will help LeaseIT to secure sources of equity and debt financing. In this quarter, ATCI introduced LeaseIT's management to various funding sources with whom the company has begun negotiations. The project will continue to assist LeaseIT to secure debt financing in the next quarter. It is planned that LeaseIT will be able to secure venture capital funding in the second half of 2006 in order to significantly expand its business and provide financing of IT equipment to thousands of Ukrainian SMEs. Since ATCI began its work with Lease IT, they have provided over $430,000 in leases spanning more than 100 leases to Ukrainian SMEs. (The investment proposal developed by ATCI for LeaseIT is included as *(See attachment 8)*

ATCI leasing advisors provided assistance to existing local leasing companies to help them improve the attractiveness of financing options they offer to their clients. These advisory services focused on the following activity: a) help leasing companies to establish relationships with equipment vendors and develop financial products tailored to the needs of those vendors' customers; b) provide advisory services on tax, legal, operational and credit issues, mainly on a transactional basis; and c) assist leasing companies to access financing sources including equity financing, credit lines, and post-import financing from agencies such as US ExIm Bank;

In its work in training and professional development, ATCI developed the first draft of five of thirteen training modules for the CLP Program along with the Body of Knowledge (a guide to the content included in the program). In the next quarter, ATCI will finish the remaining training modules and focus on building training capacity for the CLP Program.

In other training related activities, ATCI partnered with USAID's Farmer-to-Farmer (FtF) Program, administered by the Citizens Network for Foreign Affairs (CNFA), to deliver training and consulting services to Ukrainian lessors on, *"Sales and Risk Assessment for Leasing to Agricultural Enterprises."* ATCI specialists, together with the FtF expert delivered a two-day training and on-site consulting for three Ukrainian lessors to assist them in developing and implementing an agricultural leasing program based on international standards of best practice. The next of three assignments will be conducted in July, 2006 on *"Marketing and Product Development for Leasing to the Agricultural Industry."* (List of training participants and training materials, as well as the consultant's report are attached *(See attachments 9 and 10 respectively).*

ATCI continued to provide technical assistance to the new leasing association, the Ukrainian Union of Lessors (UUL), in establishing its development strategy, increasing its membership and in joining Leaseurope. Leaseurope's current members consist of 27 leasing associations in and around Europe, and it is widely considered the main voice for the leasing industry throughout Europe. It is expected that UUL's membership in Leaseurope will be approved next quarter.

ATCI co-organized a conference for over 130 senior mangers of banks and leasing companies on, *"The Role of Banks in Ukraine's Leasing Industry,"* with the National Bank of Ukraine, Ukrainian Association of Banks, and International Finance Corporation (IFC). The goal of the conference to increase the interest of local banks in working with leasing companies and improve the terms on which banks provide financing to leasing companies. The list of participants and conference program are attached. *(See attachment 11)*

ATCI participated in an internet press conference with UUL, government officials and IFC on, "Leasing 2006: Main Challenges." The conference received television coverage and was cited in economic print media and websites.

ATCI actively participated in numerous meetings of a Ukraine Cabinet of Ministers working group led by the Commission on Regulation of Financial Service Markets to develop a, "Government Program for the Development of the Leasing Industry for 2006-2010." ATCI prepared comments and recommendations to the Program itself as well as to draft laws developed as part of the Program.

ATCI also analyzed two additional draft laws that were registered in Parliament and provided recommendations to industry stakeholders, particularly UUL which encouraged the introduction of the laws in order to improve the legal and tax framework for development of Ukraine's leasing industry. Due to Parliamentary elections, none of these initiatives were presented in a

Parliamentary session and therefore new initiatives are expected after the new Parliament convenes in May 2006. ATCI will continue to advise relevant government officials and industry stakeholders in their efforts to get these reforms implemented.

IV. ADMINISTRATIVE ISSUES

Yuri Sosyorko, the President of Ukrleasing Association, the project's main partner for the CLP Program, returned in mid-January from a long illness. Mr. Sosyorko returned gradually and the Association's activities are almost back to full capacity. As a result, some progress has been made in defining roles and responsibilities for developing and subsequently administering the CLP Program and industry members have finally become more active in the program's development.

V. DESCRIPTION AND STATUS OF TASKS

Task 1. Financial Leasing – Building Participant Capacity

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Development of CLP Program for Ukraine**	▪ DEVELOPED THE FIRST 5 OF 13 TRAINING MODULES THAT COMPRISE THE CLP PROGRAM CIRRICULUM. ▪ THE NEXT QUARTER WILL FOCUS ON BUILDING TRAINING CAPACITY, DEVELOPING THE REMAINDER OF THE TRAINING MODULES, AND ESTABLISHING POLICIES AND PROCEDURES FOR DEVELOPING, ADMINISTERING, SCORING AND GRADING THE CERTIFICATION EXAM.
• **Develop and deliver training seminars for industry participants**	▪ DEVELOPED AND DELIVERED TRAINING AND PROVIDED ON-SITE CONSULTING SERVICES TO UKRAINIAN LESSORS ON, “SALES AND RISK ASSESSMENT FOR LEASING TO AGRICULTURAL ENTERPRISES,” IN COOPERATION WITH US FARMER-TO-FARMER PROJECT. ▪ THE SECOND OF THREE ASSIGNMENTS WITH FTF ON PROVIDING TRAINING AND CONSULTING SERVICES FOR LESSORS TO THE AG INDUSTRY WILL BE IN JULY 2006 AND FOCUS ON “MARKETING AND PRODUCT DEVELOPMENT FOR LEASING TO AGRICULTURAL ENTERPRISES.”.

Task 2. Financial Leasing – Information Network

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Work with key industry stakeholders to agree upon necessary reforms to create a favorable legal, tax and regulatory environment for leasing in Ukraine**	▪ ATCI ACTIVELY PARTICIPATED IN SEVERAL MEETINGS OF A WORKING GROUP FORMED UNDER THE UKRAINE CABINET OF MINISTERS AND LED BY THE STATE COMMISSION FOR REGULATION OF FINANCIAL SERVICE MARKETS TO DEVELOP THE ‘GOVERNMENT PROGRAM TO DEVELOP UKRAINE'S LEASING INDUSTRY FOR 2006-2010.” THIS ACTIVITY INCLUDED ANALYZING AND DRAFTING RECOMMENDATIONS TO DRAFT LEGISLATION ADDRESSING THE TAX, LEGAL AND REGULATORY ENVIRONMENT FOR LEASING. ▪ ATCI PROVIDED ANLAYSES AND RECOMMEDNATIONS TO THE UKRAINIAN UNION OF LESSORS WHO WORKED AGRESSIVELY WITH PARLIAMENT MEMBERS TO REGISTER A BILL IN PARLIAMENT TO IMPROVE TAXATION FOR LEASING. ▪ ATCI WILL CONTINUE TO WORK DIRECTLY WITH VARIOUS INDUSTRY STAKEHOLDERS TO RAISE THE PROFILE OF LEASING AMONG RELEVANT GOVERNMENT OFFICIALS AND IMPLEMENT REFORMS TO IMPROVE THE LEGAL AND TAX ENVIRONMENT FOR LEASING IN UKRAINE.

• **Conduct nation-wide informational and educational campaign on international best practice in leasing**	▪ ATCI CO-ORGANIZED A CONFERENCE ON "THE ROLE OF BANKS IN UKRAINE'S LEASING INDUSTRY," FOR OVER 130 SENIOR MANAGERS FROM UKRAINE'S LEASING AND BANKING INDUSTRY WITH THE NATIONAL BANK OF UKRAINE, UKRAINIAN ASSOCIATION OF BANKS, AND INTERNATIONAL FINANCE CORPORATION (IFC). ▪ ATCI PARTICIPATED IN AN 'INTERNET PRESS CONFERENCE' ALONG WITH GOVERNMENT OFFICIALS, THE UKRAINIAN UNION OF LESSORS AND IFC CALLED, "LEASING 2006: MAIN CHALLENGES." ▪ ATCI WILL CONTINUE TO WORK WITH INDUSTRY ASSOCIATIONS AND OTHER RELEVANT PARTIES TO ORGANIZE EVENTS AND DISTRIBUTE INFORMATION THAT RAISES THE PROFILE AND INCREASE UNDERSTANDING OF LEASING AND ITS BENEFITS WITHIN UKRAINE'S GOVERNMENT AND BUSINESS COMMUNITIES..

Task 3. Financial Leasing - Consulting Services

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Provide advisory services to market participants**	▪ FACILITATED ENTRANCE OF MAJOR EUROPEAN LEASING COMPANIES, SG EQUIPMENT FINANCE AND BANK AUSTRIA~ CREDITANSTALDT LEASING INTO THE UKRAININ MARKET; ▪ IMPLEMENTED IMPROVEMENTS TO THE BUSINESS AND OPERATIONAL STRATEGY OF LEASEIT, UKRAINE'S FIRST SMALL-TICKET LESSOR, AND INTRODUCED THE COMPANY TO POTENTIAL DEBT AND EQUITY FUNDING SOURCES. ▪ DEVELOPED FIRST DRAFT OF BUSINESS PLAN FOR AMACO FINANCE, THE FIRST CAPTIVE LESSOR OF AGRICULTURAL MACHINERY TO ENTER THE UKRAINIAN MARKET ▪ PROVIDED ADVISORY SERVICES AND FACILITATED RELATIONSHIP BUILDING BETWEEN VARIOUS LESSORS, BANKS, EQUITY INVESTORS, AND VENDORS TO ENABLE INCREASED LEASING ACTIVITY BASED ON INTERNATIONAL BEST PRACTICE. ▪ IN THE NEXT QUARTER, WILL CONTINUE PROVIDING CONSULTING SERVICES TO LEASEIT AND AMAKO. ▪ ATCI WILL CONTINUE TO FACILITATE RELATIONSHIPS BETWEEN LESSORS, BANKS, EQUITY INVESTORS, AND VENDORS TO FACILITATE INCREASED LEASING ACTIVITY BASED ON INTERNATIONAL BEST PRACTICE.

LIST OF ATTACHMENTS

ATTACHMENT 7 Executive Summary of Amaco Finance business plan

ATTACHMENT 8 Investment proposal developed for Lease-IT

ATTACHMENT 9 Program, presentation and list of participants for two-day training seminar delivered for leasing company managers on, *Sales and Risk Assessment for Leasing to Agricultural Enterprises*

ATTACHMENT 10 Trip report from Tom Meade, FtF Volunteer and e-spotlight article

ATTACHMENT 11 Agenda and List of Participants for the conference, *The Role of Banks in Ukraine's Leasing Industry*

E. CREDIT BUREAU/CREDIT RATING AGENCY

I. COMPONENT DESCRIPTION

Credit Bureau

This report provides details on events and activities relating to the Credit Bureau component of the USAID Access to Credit Initiative, as implemented by the Pragma Corporation, during the period from January 1, 2005 through March 31, 2005.

The objective of this activity is to establish and develop a Credit Bureau in Ukraine, which is a key piece of financial infrastructure. A Credit Bureau serves as a financial intermediary between the lender and the borrower in order to stimulate, in the first instance, the SME and retail markets within a free market competitive economic system.

The practical definition of a Credit Bureau, for design and implementation purposes in Ukraine, is one of an impartial entity that will store all past and present credit transactions entered into by a particular legal or physical person, and one that will indicate the manner in which the subject of the credit profile repaid the obligation to the respective creditors. The Credit Bureau would contain gender-neutral demographic information on a consumer to ensure proper identification, information that is pertinent to their creditworthiness, and an indication of the overall risk relating to an applicant. The Credit Bureau will provide an avenue for the verification or validation of any information that may be questioned or disputed by the subject of the credit profile. A Credit Bureau serves both parties in a credit transaction and is an excellent tool to reduce risk and facilitate and accelerate the approval process.

II. SIGNIFICANT EVENTS

- MINISTRY OF JUSTICE (MOJ) REQUESTS LEGAL ASSISTANCE IN DRAFTING VARIOUS CB REGULATIONS
- ATCI DRAFTS AND SUBMITS LICENCING REGULATIONS TO MOJ
- MOJ REQUESTS ATCI TO DRAFT REGULATIONS GOVERING THE UNIFIED REGISTRY.
- UKRAINIAN PARLIAMENT ADOPTS PERSONAL DATA PROTECTION LAW ON MARCH 16, 2006
- FNBCH DELAYS SELECTION OF INTERNATIONAL CREDIT BUREAU OPERATOR TO NEXT QUARTER

III. EXECUTIVE SUMMARY

ATCI continued to provide on-going consultancy to ensure compliance with international standards of best practice during the development phase of a credit reporting system, and to provide advice to the overall market with respect to data sharing and the reduction of data fragmentation.

ATCI's area of focus remained in two basic areas: a) overall coordination of the market given the likelihood of data fragmentation and b) drafting regulations.

Moreover, ATCI further helped to consolidate the interests of commercial banks to fund a private credit bureau, and to deepen the market's awareness of a credit bureau's role in risk and portfolio management. ATCI, based on experience in other markets and interviews in country, understands the educational challenges in communicating to all stakeholders the importance of data sharing.

ATCI continues to interface on a regular basis with FNBCH and other interested parties, including foreign credit bureau operators. Major highlights and accomplishments over the past quarter follow:

1. Cooperation with FNBCH and Creditinfo

In 1st quarter 2006, both FNBCH and Creditinfo continued to request assistance from ATCI, particularly in connection with a) educating market participants, and b) providing support to the credit bureau regulatory authorities with respect to draft regulations, the meaning of data exchange and the need to find a balance between privacy and data flows. ATCI supported our counterpart in the following areas:

- Work at the legal and regulatory levels
- Work with banks and other financial institutions.
- Work with non-financial institutions to secure their participation in data sharing.
- No work was carried out in the regions.

FNBCH remains ATCI's primary counterpart. Activities with Creditinfo and other potential market players are first discussed with FNBCH prior to taking any action. .

2. Legal/Regulatory and Ministry of Justice

In the previous quarter, the Cabinet of Ministers of Ukraine issued a Resolution in which it assigned the Ministry of Justice of Ukraine to serve as the authorized body responsible for licensing and regulation of credit bureau operations. Pursuant to the Ukrainian Credit Bureau Law, and the authorized body was mandated to draft the regulations governing licensing requirements and other rules for credit bureau operations in Ukraine. The purpose of the regulations is in the first instance to ensure that private information is safeguarded and that bank secrecy laws are not violated.

During the period, the Ministry of Justice requested ATCI to draft at least 3 sets of regulations and to carry out at the MOJ a series of workshops and training for its employees. Personnel at the MOJ (including key specialists involved in the development of regulations) in fact have a very poor idea of what credit bureaus are and how to supervise them. It is for these reasons that the MOJ, at the Deputy Ministerial level, asked us to carry out educational workshops.

ATCI finalized regulations governing licensing requirements. ATCI, FNBCH, Creditinfo, and MOJ agreed on draft licensing regulation. The regulations need to be agreed with the State Committee for Entrepreneurship and Regulatory Issues.

Separately, the Ministry of Justice requested ATCI to prepare materials for and advise the Ministry of Justice ('MOJ') regarding two specific sets of regulations: a) Regulation governing the Unified Registry, and b) Inspection of Credit Bureaus. These regulations will be drafted and negotiated (redrafted) over the course of the next several months. More detailed work with respect to these regulations is expected to commence in the 2nd quarter of 2006. Considering the complex nature of this task, its successful fulfillment will significantly depend on the degree of cooperation and input from all interested parties.

3. International Credit Bureau Operators still not selected by FNBCH

Respondents to the tender document included Creditinfo, D&B, SCHUFA/KKB and Transunion/CRIF. In March, two companies made the short list: D&B and Transunion/CRIF. Each provided a compelling business proposal on information system delivery, specifications and servicing. Pricing Information with respect to the business proposal included the respondent's best estimate of costs and expenses and fees required of the FNBCB.

The short listed companies specified separate business models for the proposed credit bureau structure that would deal with information on natural persons and legal entities as well as the minimum required functionality and extension options. It is most probable that FNBCH has not yet selected a winner because of an inability to agree on pricing and share ownership. There should be no questions in connection with technical capabilities.

4. Law on Personal Data vs. Credit Bureau Law:

Ukraine’s 2005 credit bureau law cleared the way for the establishment of a system of credit bureaus, and served as a benchmark for data processing. This law provided solid protections for consumers. On March 16th, Ukraine’s Parliament passed the Law on Personal Data, which is designed to protect the privacy of individuals. If signed by the President of Ukraine, the law will come into force on Jan. 1, 2007. This law appears to contain language that may conflict with the Credit Bureau Law in some areas, thus making data processing less inefficient and more costly. This law needs to be closely reviewed and, as of the end of March, it had not been signed by the President.

5. Conferences

ATCI, together with IFC and Visa International, began discussions regarding a Ukrainian Credit Bureau conference for late June 2006. Because of time constraints, the conference will most likely be postponed until the fall of 2006. Conference participates will include all the major banks, other financial institutions in Ukraine as well international operators. The conference will be specific and geared towards to needs of the market place. In addition, given ATCI's position as credit bureau leader/broker in Ukraine, i.e., ATCI is not perceived as having a business interest in Ukraine. In this context, VISA International requested ATCI to speak at the international Payment Card – 2006 conference which will be held in Kiev (June 7-9, 2006). Part of the conference will be dedicated to credit bureau issues – particularly those issues connected with the processing of personal data and credit cards.

II. Credit Rating Industry

1. Historic Note

The mandatory rating concept in Ukraine was introduced in 2004[1] by the Resolution of the Cabinet of Ministers #208 "On the System of Rating Assessment", Regulation of the Securities and Stock Market State Commission (SSMSC) # 236 "On Terms of Tender/Competition for Selecting Authorized Rating Agencies", and Resolution of the SSMSC # 542 dated Dec. 8, 2004 "On Introducing the System of Mandatory Rating for Stock Market Participants and Instruments". As a result, international rating agencies found themselves outside the Ukrainian legal framework and could not assign mandatory ratings. Mandatory ratings were only assigned under the national scale and "Credit-Rating" was the only Ukrainian rating agency that met the requirements to assign mandatory ratings.

2. Situation at the end of March, 2006

Adoption of the Law of Ukraine # 3201 dated Dec. 15, 2005 expands and legislates mandatory ratings. This Law specifies the issuers and types of securities[2] subject to mandatory rating. In addition, under the above Law, insurance companies and pension funds are mandated to keep their reserves only in banks that have been assigned a rating.

Pursuant to the Law # 3201 mandatory ratings can be assigned by:

- Authorized Ukrainian rating agencies certified by the SSMSC;
- International rating agencies recognized by the SSMSC; and

The national scale must be used only by authorized Ukrainian rating agencies;

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[1] Rating for municipalities was introduced in 2003. Pursuant to the Resolution of the Cabinet of Ministers of Ukraine # 207 dated Feb. 24, 2003, municipalities had to submit a report on the assignment of credit rating to receive permission for bond issue.

[2] All types of issues/equity securities are subject to mandatory rating, except the following types of securities: *government securities, shares, securities of non-diversified joint investment institutions, securities issued by State Mortgage Institution*

- International rating agencies can use their own scales.

In accord with Law #3201, the SSMSC developed a draft resolution that allows Ukrainian companies to use Fitch, Moody`s and Standard & Poor`s ratings in the domestic market. In other words, these three international rating agencies will be able to assign mandatory ratings to Ukrainian issuers and their securities and will be allowed to use their own scales. Consequently, Ukrainian companies, banks and municipalities will be able to use international ratings without going through the procedure of getting mandatory ratings from Ukrainian authorized agencies.

However, (due to the entry of international rating agencies to the domestic market) the SSMSC tightened the requirements for Ukrainian rating agencies willing to obtain the status of authorized rating agency. Pursuant to draft amendments to SSMSC Regulation #236 "On Terms of Tender/Competition for Selecting Authorized Rating Agencies", the applying company must meet the following requirements:

- Charter capital – no less than UAH 3 mln;
- No less than 2 year experience of relevant operation on the market;
- Company track record – no less than 35 ratings assigned to Ukrainian business entities;
- A financial institution or a person associated with a financial institution may not be among the founders of an agency applying for the status of authorized agency.

SSMSC postponed the tender for selecting authorized agencies till the end of April. Currently none of Ukrainian rating agencies, including "Credit-Rating", fully meets the above mentioned requirements. Among all potential candidates, only "Credit-Rating" meets the 2 year requirement.

3. Further Market Development Options

The situation with regard to further development of the market (in terms of both operations and legislative regulation) is unclear.

Operations

It is quite probable that other rating agencies will fail to meet the SSMSC requirements and "Credit-Rating" will remain the only Ukrainian authorized rating agency (Credit-Rating does not meet the charter capital requirement only). However, with international rating agencies operating in the domestic market Credit-Rating is most likely to lose some of the biggest clients.

Prospective legislation

- In February 2006, the Ministry of Justice drafted the resolution that cancels mandatory ratings for municipalities. Under this resolution municipalities will not have to submit a report on the assignment of credit rating to receive permission for a bond issue. **Progress with this resolution is unclear.**

- By May 15, 2006, SSMSC is supposed to submit to the Cabinet of Ministers a Draft Law "On Rating System in Ukraine". This law might introduce some new requirements and provisions. **Drafting of this law has yet to start.**.

IV. ADMINISTRATIVE MATTERS

THE FBNCH HAS YET TO SELECT AN INTERNATIONAL OPERATOR.

V. DESCRIPTION AND STATUS OF TASKS

Defined Activity	PROGRESS MADE DURING QUARTER/PROPOSED FUTURE ACTIONS
• **Develop and establish linkages with primary international credit bureau operators**	• CREDITFO MOVES BEYOND ESTABLISHING COMPANY AND BEGINS TO MARKET ITS STRENGTHS TO BANKING SECTOR. OTHER INTERNATIONAL CREDIT BUREAU OPERATORS RECONFIRM INTEREST IN UKRAINE. DISCUSSIONS CONTINUE WITH EXPERIAN (UK), CRIF (ITALY/CZECH REPUBLIC) AND D&B (SIGNAPORE).
• **Secure buy-in of local data providers and users**	• MARKET REMAINS SPLIT – DATA FRAGMENTATION BECOMING A REALITY AS IT APPEARS THAT AT LEAST 4 CREDIT BUREAUS WILL BE ESTABLISHED. • ARTICLE PUBLISHED ON THE IMPACT OF AN EFFECTIVE CREDIT REPORTING SYSTEM IN DEVELOPING CREDIT MARKETS. • ATCI PRESENTS AT BANKING CONFERENCE (ATTENDED BY THE LEADING UKRAINIAN BANKS)
• **Sponsor visits to potential foreign CB partners**	• FNBCH INDEPENDENTLY VISITED CERTAIN POTENTIAL PARTNERS (TRANSUNION/CRIF, D&B). FINANCIAL ASSISTANCE WAS NOT REQUESTED.
• **Determine and review CIC development strategy with government and counterparts**	• FNBCH REQUESTS FURTHER ATCI ASSISTANCE • CONTINUED TO DISCUSS WITH AUB AND OTHER REPRESENTATIVES OF THE CIC (OR FCB) DEVELOP IMPLEMENTATION STRATEGY FOR THE DEVELOPMENT OF CB.
• **Market best approach for structuring, establishing and operating CIC**	• PUBLIC RELATIONS STRATEGY CONTINUED, AND INCLUDED VISITS TO INDIVIDUAL MARKET PARTICIPANTS. • WILL BE HARD SELL TO GET TELECOMMUNICATIONS SECTOR TO WORK WITH BANKS – WORK CONTINUES TO CONVINCE THEM.
• **Analyse and Coordinate passage of law**	• IN JULY 2005, THE PRESIDENT OF UKRAINE, FOLLOWING PASSAGE BY PARLIAMENT IN JUNE, SIGNED THE UKRAINE'S CREDIT BUREAU LAW: "*ON ORGANIZATION, FORMATION AND CIRCULATION OF CREDIT HISTORIES*". • CABINET OF MINISTERS AUTHORIZES MINISTRY OF JUSTICE AS REGULATORY BODY TO LICENSE AND REGULATE CREDIT BUREAUS • ATCI BEGINS ANALYZING OPTIMAL APPROACH TO DRAFT REGULATIONS GOVERNING CREDIT BUREAU OPERATIONS IN UKRAINE.
• **Define Business and Operations Plan**	• BUSINESS PLAN FINALIZED AND DELIVERED TO THE AUB IN BOTH RUSSIAN AND ENGLISH. DISTRIBUTED TO MAJOR CREDIT BUREAU OPERATORS • BUSINESS PLAN IN PROCESS OF IMPLEMENTATION AFTER FORMAL PRESENTATION TO BANKING SECTOR
• **Outline Package of Technical Requirements**	• ATCI DRAFTS RFP FOR FIRST NATIONAL BUREAU OF CREDIT HISTORIES (FNBCH) • CREDITINFO, D&B, KKB, CHUFA, AND TRANSUNION/CRIF. RESPOND TO TENDER

	• AS OF THE END OF MARCH 2006, THE LIST OF POTENTIAL PARTNERS INCLUDES TRANSUNION/CRIF, D&B, AND CREDITINFO.
• **Discussions with Government Data Providers**	• IN PROGRESS ALBEIT VERY SLOW BECAUSE OF THE DIFFICULTY OF FINDING THE "PERSON" IN CHARGE
• **Secure Buy-in of Foreign Investors and Banks**	• INTERNATIONAL CREDIT BUREAU OPERATORS MOVE TO ESTABLISH OFFICES IN KIEV AND CONTINUE TO UNDERTAKE "DUE DILIGENCE" • CREDIT INFO FORMALLY REQUESTS FURTHER ATCI ASSISTANCE • EXPERIAN AGAIN DECLARES ITS WILLINGNESS TO INVEST IN UKRAINE
• **Develop and Deliver Package of Training Programs (banks, leasing, credit unions)**	• AUB REQUESTS ATCI TO CARRY OUT A SERIES OF PRESENTATIONS FOR REGIONAL BANKS. • THIS ACTIVITY WAS SUPPOSED TO HAVE BEEN ORGANIZED BY AUB AND UNDERTAKEN JOINTLY WITH AUB. ACTIVITY POSTPONED DUE TO THE DELAYS IN DETERMINING TENDER WINNER.
• **Assist the Ministry of Justice in drafting regulations governing CB operations**	• THE MINISTRY OF JUSTICE REQUESTS ATCI ASSISTANCE IN DRAFTING REGULATIONS GOVERNING CREDIT BUREAU OPERATIONS. • ATCI, CREDIDITINFO, AND FNBCH JOINTLY DRAFT AND SUBMIT TO THE MINISTRY OF JUSTICE THE REGULATION ON LICENSING REQUIREMENTS. • ATCI, CREDIITINFO, AND FNBCH AGREE TO JOINTLY DRAFT TWO MORE REGULATIONS: ON UNIFIED REGISTRY OF CREDIT BUREAUS, AND ON INSPECTION OF CREDIT BUREAUS.
• **Deliver educational workshops for the specialists of the Ministry of Justice**	• THE MINISTRY OF JUSTICE REQUESTS ATCI TO ORGANIZE EDUCATIONAL WORKSHOPS ON CREDIT BUREAU ISSUES FOR ITS SPECIALISTS. • DUE TO UNCERTAINTY WITH PERSONNEL ARRANGEMENTS AT THE MINISTRY OF JUSTICE EDUCATIONAL WORKSHOPS POSTPONED FOR THE NEXT QUARTER (EXPECTED TIME FOR HOLDING WORKSHOPS – MAY/JUNE 2006).
• **Discuss participation in international credit bureau conference to be held in Kyiv/Ukraine**	• ATCI, TOGETHER WITH IFC AND VISA INTERNATIONAL, BEGAN DISCUSSIONS REGARDING A UKRAINIAN CREDIT BUREAU CONFERENCE FOR LATE JUNE 2006. BECAUSE OF TIME CONSTRAINTS, THE CONFERENCE WILL MOST LIKELY BE POSTPONED UNTIL THE FALL OF 2006.
• **Discuss participation in international Conference "Payment Card – 2006"**	• ATCI WAS REQUESTED TO SPEAK AT THE INTERNATIONAL PAYMENT CARD – 2006 CONFERENCE, WHICH WILL BE HELD IN KIEV (JUNE 7-9, 2006). PART OF THE CONFERENCE WILL BE DEDICATED TO CREDIT BUREAU ISSUES – PARTICULARLY THOSE ISSUES CONNECTED WITH THE PROCESSING OF PERSONAL DATA AND CREDIT CARDS.

LIST OF ATTACHMENTS

NONE

E. GENDER

I. COMPONENT DESCRIPTION

Programs related to gender have political and cultural implications that should be considered in any approach. ATCI is seeking opportunities for increased income and empowerment for both women and men.

ATCI management recognizes the importance of carrying out gender sensitivity training for the staff in order to have a solid basis for the monitoring work.

With respect to monitoring participation in training programs and events by gender, the following activities will be undertaken to the extent feasible and possible:

- Examine the program to ascertain whether if there are any provisions that could differentially discourage persons of one sex or another from participating;
- Inquire about how program outreach is conducted to understand whether if these procedures may be differentially affecting participation by gender;
- Examine the actual patterns of participation by gender in selected programs, to the extent permitted by the data;
- Where differential participation by gender is identified, try to understand its causes and make appropriate changes.
- With respect to the representation of women in higher positions in government agencies, the ATCI will work to balance the composition by gender of groups being trained by the project.

Pragma continues to partner with local organizations managed by women or consisting mostly of women. Three good examples are the Association of Ukrainian Banks and the Commercial Law Center as well as the PFTS securities trading system

II. SIGNIFICANT EVENTS AND ACHIEVEMENTS

- SIXTEEN PARTICIPANTS (THREE WOMEN) BECOME CML CERTIFIED
- ATCI PROVIDES MORTGAGE TRAINING FOR THE SSMSC FOR TWENTY - FOUR PARTICIPANTS (EIGHTEEN WOMEN)
- ATCI CONDUCTS WORKSHOP ON THE ROLE OF BOND BANKS IN MUNICIPAL FINANCE FOR EIGHTY-THREE PARTICIPANTS (TWENTY-FIVE WOMEN)

III. EXECUTIVE SUMMARY

All ATCI tasks present opportunities to identify and address gender bias, and to actively promote gender equality in Ukraine's financial sector. For example, ATCI is working closely with the Association of Ukrainian Banks, the Commercial Law Center and other organizations which understand the importance of gender sensitivity with respect to product and services development. These issues have not only been discussed but plans are underway to draft material and articles which point out important opportunities in this area.

During the quarter, ATCI delivered seminars, workshops, and conferences involving three of its four components. In Mortgage, ATCI developed and delivered a three day training seminar on the fundamentals of the mortgage market for 24 regional employees (eighteen women) of the SSMSC. The training focused on credit analysis, underwriting practices and deal structuring practices for regulators to understand what mortgage securities are. In CML certification, three women received the designation. The Municipal component conducted a workshop on the role of bond banks play in assisting smaller municipalities to access the capital markets. Eighty – three participants (25 women) heard nine internationally recognized experts make presentations on international experience with bond banks.

All ATCI training and professional development strives for gender balance during the invitation process as well as in delivery of content. Post - event analysis to understand the reasons for underweighting when it occurs.

The Project staff of ATCI project includes 11 women out of 24 with professional and technical skills in finance and law.

IV. ADMINISTRATIVE ISSUES

NONE

III. DESCRIPTION AND STATUS OF TASKS

Defined Activity	Progress Made During Quarter/Proposed Future Actions
• **Partner with Woman – run organizations (CLC & UAB)**	• ATCI IS WORKING CLOSELY WITH THE ASSOCIATION OF UKRAINIAN BANKS, THE COMMERCIAL LAW CENTER AND OTHER ORGANIZATIONS WHICH UNDERSTAND THE IMPORTANCE OF GENDER SENSITIVITY RELATED TO PRODUCT AND THE DEVELOPMENT OF SERVICES.
• **Increasing the role of women in the financial sector through training and /or other initiatives**	• STAFF OF THE ATCI INCLUDES WOMEN WITH PROFESSIONAL AND TECHNICAL SKILLS IN FINANCE AND LAW. • ALL PROJECT TRAINING TRIES FOR AN EVEN BALANCE OF PARTICIPANTS
• **Gender and cultural sensitization training**	• UNDER DISCUSSION / GENDER SENSITIVITY IS PRACTICED DAILY BY ALL ATCI STAFF.

LIST OF ATTACHMENTS

NONE

ATTACHMENT 1

Procedure for Monitoring the Mortgage Pool

Frequency of audit procedure
With mortgage prepayment rates at relatively high levels in all banks, it is recommended that the audit procedure required by the law "On Mortgage Bonds" be performed at least once a quarter.

Audit procedure nomenclature
In order to avoid confusion with established types of audit procedures—to wit, "audit" and "review"—the procedure required by the law "On Mortgage Bonds" shall be called an "agreed-upon audit procedure" (in Russian, *"условная аудиторская процедура").*

Initiating the agreed-upon audit procedure
The agreed-upon audit procedure is initiated by the Issuer who, in accordance with law and the investment memorandum (prospectus), within five business days of the end of each quarter sends to the Manager a report entitled "Issuer's Report on the Condition of the Mortgage Coverage of Mortgage Bond No. (Registration Number)" (in Russian, *"Отчет эмитента о состоянии ипотечного покрытия ипотечной облигации No. (номер регистрации)." (See Attachment 1.)*

The Manager acknowledges receipt of said report in writing, requesting that the Issuer forward to the Auditor the Register of Mortgage Coverage (in Russian, *Реестр ипотечного покрытия) (See Attachment 2.)* for said issue.

Simultaneously, the Manager forwards to the Auditor the Report on the Condition of the Mortgage Coverage and instructs the Auditor verify the report by conducting the Agreed-upon Audit Procedure.

Upon receipt of the Register of Mortgage Coverage from the Issuer, the Auditor constructs a random sample of the mortgage pool, using specified sampling methodology based on Large Number Theory. *(See Attachment 3.)* The Auditor sends the Issuer the list of the loan numbers in the random sample and requests that the Issuers make those files available to the Auditor's personnel for the agreed-upon audit procedure. (It is customary for the auditor's personnel to perform the agreed-upon audit procedure on the issuer's premises.)

Details of the agreed-upon procedure
A. Validating the Register of Mortgage Coverage
The Auditor verifies that entries for the following components of every mortgage file in the sample comply exactly with entries for the same components as recorded the Register of Mortgage Coverage:

1. Payment Status (standard or non-performing)
2. Outstanding Balance
3. Loan-to-Value (of original loan amount)
4. Interest Rate
5. Residential or Commercial Loan

Failure of any entry of any component in the sample files to comport exactly with its counterpart entry in the Register of Mortgage Coverage invalidates both the Register and the Issuer's Report on the Condition of Mortgage Coverage.

The Auditor reports the failure to the Manager.

The Manager informs the Issuer of the failure and instructs him to recompile the Register of Mortgage Coverage and reissue the Issuer's Report on the Condition of Mortgage Coverage within five business days.

Exact compliance of all components in the sample files with their counterparts in the Register of Mortgage Coverage validates the Register.

B. Verifying the Issuer's Report on the Condition of Mortgage Coverage

The Auditor verifies the following calculated components of the Report on the Condition of Mortgage Coverage by either (1) recalculating the components or (2), if the Register has been transmitted in spreadsheet format, verifying the formulas used in the spreadsheet to calculate the various calculated components:

1. Outstanding Balance of all loans
2. Outstanding Balance of all loans and other assets in the pool
3. Weighted Average Term of loans and other assets
4. Weighted Average Interest Rate of loans and other assets
5. Weighted Average initial Loan-to-Value
6. Residential loans as a percent of mortgage coverage

Failure of any component calculated or verified by the Auditor to conform exactly to its counterpart in the Issuer's Report invalidates *only that calculated component*.

The Auditor reports the failure to the Manager.

The Manager informs the Issuer of the failure and request the Issuer recalculate the component within two business days.

Exact compliance of all components recalculated or verified by the Auditor with their counterparts in the Issuer's Report on the Condition of Mortgage Coverage constitutes successful conclusion of the Agreed-upon Audit Procedure for the date of record.

The Auditor sends the following to the Manager: "Having conducted the Agreed-upon Audit Procedure in compliance with the Management Agreement and Regulations X-XX of the Securities Commission, we herewith conclude that the Issuer's Report on the Condition of Mortgage Coverage of Mortgage Bond No. XXXXXXX, of [date of record] is correct as written."

ATTACHMENT 2

UKRAINE

CONDUCTING A REAL ESTATE PRIVATE PRACTICES
ASSESSMENT IN TRANSITIONAL MARKETS

FEBRUARY 11-21, 2006

Brokerage by: Norman D. Flynn, CRE, CRB, CIPS

Quantitative Analysis

1. Determine number of practitioners in the country.

The estimates as to the number of practitioners in the country are pretty consistently listed as 50,000. Some sources suggest that government statistics indicate that this is the number. Of these, there are a substantial number of practitioners that are marginal and illegal operators, either on their own or in small clusters of two or three people. These don't have offices, keep office hours, or pay taxes.

2. Assess the number of companies into which these practitioners are formed. Estimate the relative size of the companies.

Legitimate companies throughout the country are estimated to be about 2,000. Approximately 1,000 of those are in the capital city of Kiev. The other four major million population cities also have a larger number of companies and mortgage companies are willing to make loans in those markets. In Kiev, of the 1,000 companies, approximately 100 are substantial and more refined in their approach.

3. Estimate the "unprofessional" practitioners (i.e., those without phones, offices or any trapping of permanence. Often called "black brokers" or "muckluckers.")

It would appear that between 15,000 and 20,000 of the 50,000 practitioners would fall into this category.

4. Determine the fee or commission practice in the country. Who pays (buyer/seller)? How much? Co-brokerage?

The commission fee ranges between 1%-5% depending on the size of the property. Nearly all firms indicated that they strive to get 5%. Almost without exception, the buyer pays the commission. This is opposite from practice throughout the worlds where the seller (or both sides) pay the commission. Occasionally brokers are able to list the buyer exclusively, but by and large, they attempt to get them to cooperate with them simply by "trust." There is co-brokerage among "legitimate companies." That is nearly always 50%-50% with the exception of the very large companies that have additional overhead where they take 60%-70% and leave 30%-40% for the co-broke partner. They have reached a point in this market where sharing of commissions, and, in some instances property information, is becoming more of a way of life.

5. Estimate the volume of business the average company does in dollar terms.

This information was extremely difficult to obtain the Ukraine. In part, the large brokers simply refuse to answer the question, and in other instances, said "I hope you don't talk to the police." It was generally felt that because of the nature of the government's intrusion into people's personal lives that they had very little interest in sharing that information. However, extrapolating from those companies that did give me the data, it would appear that the top 100 companies are averaging gross incomes of $200,000 to $400,000 with net incomes in the $50,000 to $100,000 range. Associates are earning as low as $10,000 to $35,000 depending on the market and company.

6. What percent of the transactions are broker assisted?

That estimate is approximately 15%-18% are broker assisted. It appears to be higher in Kiev and the large cities than in the regions. In the primary market (defined as new construction) broker assistance is under 10%.

7. What is the incidence of home ownership by percent and by numerical count in the country?

The incidence of home ownership is estimated between 87%-94%. One expert suggested that the only non-privatized residential properties were those which were really hotels or where the resident did not have an heir. Far fewer of the commercial properties have been privatized and especially large and complex companies remain still to get to the private market.

The number of housing units in the country is approximately 20,000,000 (47,000,000 population divided by approximately 2.4 person's per unit).

8. Is there adequate legal/regulatory structure to allow the business to grow? Does a "secondary sale market" exist? If so, how large and active is it?

The legal and regulatory structure in Ukraine, while complex, sometimes contradictory and overlapping, does allow for transfer of property. There is also now an active secondary market in the Ukraine. The one substantial difficulty in operating within the market structure is the lack of information from the Bureau of Housing Inventory (BiH). They only will allow owners to access the information and not even lenders with a lien right on the property can examine title (even if they have the permission of the owner). Since there is little market transparency, there is substantial reputed corruption where owners will bribe the registrars to falsify information inside of the document.

9. How are the transactions completed?

! Contracts involved?
Yes, there are listing contracts for the properties. The transaction follows with a "deposit" contract often provided by the notaries which articulates the price and

the deposit to hold the property. If the seller refuses to sell, they are subject to a fine equal to the deposit plus a 100% penalty. If the buyer refuses to close, they give up the deposit. Some of the larger companies have a draft of an actual contract that then is validated by the notary public and is ready for transfer.

! Legal work?
Most small firms rely on the notary publics to provide the legal work options. They charge 1% plus additional fees for these efforts. Larger companies have their own legal department that prepares documents for their agents.

! Recordation systems in place?
Yes, and it is relatively inexpensive – 40 to 60 UAH (about $8 to $12) but once recorded, the information is no longer transparent or accessible except solely to the owner of the property.

! Actual closings and documentation?
Yes, generally by the notary public when the taxes are collected and paid. If there is a mortgage, the bank collects and pays these fees.

! Taxation policies
There are several layers of taxes at the point of closing. A 1% fee for the notary, a 1% contribution to the Pension Fund, a transfer fee recently limited to no-charge for the first 100 square meters and 1% for any square meters above that and a registration fee to the BTI of 40-60 UAH. There is no capital gains tax.

! Financing involved
There is financing available by some of the institutions only in the cities with populations of 1 million or more. There is limited financing in the rural arena which comprises a very small portion of it. Practitioners estimate that between 20%-30% of their current transactions now has a mortgage involved with them for new buyers. It remains that less than ½ of 1% of the properties in the Ukraine have a mortgage on it at this time.

10. Is there information sharing through multiple listing or other network sources?

There are some attempts at creating a Multiple Listing Service from the Kiev Real Estate Institute as well as a data sharing agreement in Odessa. These are encouraging signs that efforts are beginning to emerge in the marketplace to share information and data and bring greater transparency to the market. These need to be built upon to create a more transparent and efficient market.

11. Are there real estate associations that have evolved? How many practitioners belong? What is their dues structure?

There is one national association, the Ukrainian Realtors Association (URA). It has been in existence since 1994 and boasts a membership of 500. Reputedly, 90% are managers of larger companies in the Ukraine. They estimate the size of each of those companies to average approximately 30 with some very large and others in the 3-5 member category. That would suggest that there are approximately 15,000 agents in association-related companies which would comprise approximately 30% of the practitioners in the marketplace. These Associates are virtually uninvolved in Association activities.

There is a series of regional organizations in the major million plus cities. However, in Kharkiv, there are two associations that battle for supremacy, and Kiev, as well. Too often, the regional associations are in conflict with the national and therefore cloud legislative agendas especially on the certification issue.

12. Does any training exist in the companies or associations to enhance productivity?

Yes, the URA has a training program leading to certification that has been wholly inadequate. It has been in existence for five years and only 200 have qualified to be certified under this program. They assert that there are many more that have been trained but since they are not members of the Association, they cannot get the certification. They train in three locations, anywhere from 2 to 6 courses per year and average 25 per classroom. This means that 275 complete the certification courses each year which number is extraordinarily low.

The Kiev Real Estate Union also has a certification program and they assert that 20% of their members have completed it and have an objective in the next year and a half to have 80% through the course. There is not cost for that course whereas the URA's course costs $100 per person and lasts for 6 days.

Many of the larger firms have in-house trainers and coordinators. Nearly every company that I interviewed that had 40+ practitioners had in-house training. Some of the training is conducted by appraisers, notary publics, attorneys, or engineers.

13. Are there forms of real estate finance?

! Costs - terms of loans

There are mortgages available in the marketplace whose terms are 10 ½% -13% for residential properties, 12%-14% for commercial.

- ! Availability
  They will do 70-80% mortgages and amortize them at between 15-30 years.

- ! Usage by the buying public
  The current buying public is looking at between 20%-30% who use mortgages and, if secured, they will attempt to pay these off as soon as practicable, in many instances, 1-3 years.

14. Is there a "code of ethics" or standards that practitioners follow?

Yes, for those who are part of the Ukrainian Realtors Association. Their subset regional organizations also have codes of ethics including the unaffiliated Kiev Real Estate Union. People outside of these associations have no codes of ethics to subscribe to.

Qualitative Analysis

1. Do practitioners follow ethical practice standards? If a code of ethics exists, how well is it enforced?

There is a code of ethics but its enforcement is sporadic at best

2. What is the sophistication of the practice in the country?

- ! Amount and quality of computerization
  All of the major companies are networked and have substantial computerization. Each of those firms is internet connected and many have standardized their forms that are computerized. Of the many countries in the emerging market, it appears that the Ukrainians have embraced internet and computerization technology into

their practice resulting in a fair sophistication internally and nearly 100% internet connection of the URA members.

- Existing training and training capacity

  There is a weakness in the certification program in that it is not very wide, nor deep. There was an attempt five years ago to give status and credibility to the industry, but has fundamentally failed. The Kiev Real Estate Union is making a concerted effort to improve its certification program to try to get 80% of its members to reach this status.

  There are other training programs that are available at conferences and conventions, but they are limited and difficult for members to get to.

  The larger companies have in-house training, generally focusing on market understanding, psychology, and legal aspects of transactions.

- Quality of the offices

  I was very impressed with the bulk of the offices that I visited in Ukraine. This is true both in Kiev and Odessa. The quality of the locations and size of the offices are substantial and the furnishings, well-maintained and/or new.

- General deportment of the agents

  The agents and staff in the offices visited appeared to be very professional, generally well-dressed, and carried themselves in a business-like manner.

- Do they have effective company policies

  The larger companies do have company policies; those under the size of 20, do not.

- To what extent are contracts enforceable

  It appears that the brokerage community has some confidence that the deposit agreement and vital contracts drafted by the notary publics are enforceable. Several indicated that they had been to court over deposits that sellers refused to return and the courts had sided with the buyers in each instance. In addition, the hearings held on this can occur within 2-3 days, as opposed to the lengthy delays in most countries.

- Do they have appropriate compensation structures

  There is no consistent fee splitting structure in Ukraine. The fee splits are from 20% to 80%. Those companies that fall into the category of "body shops," that is to say large numbers of agents that work fundamentally out of their homes pay up to 80% of the commissions that come into the office to the agents. In the smaller, outlying, rural areas where commissions are approximately 60% of those in the major cities, the norm seems to be approximately 30% to the salesperson and

70% to the company. Since incomes in these smaller cities are much lower, it appears that the agents can survive on those kinds of compensation models.

3. How sophisticated is their computerization (MLS's) and networking opportunities?

The networking agreement in Odessa was quite sophisticated. Seventeen companies have come together and submit information on properties as well as pricing. It represents about 40% of the market which allows a substantial grasp on values by both property type and location. The MLS at the Kiev Real Estate Union has 700 properties on it and is not yet functioning properly. What is most important is the fact that they are attempting to put it together and now need to get it to work.

4. Leading Broker Analysis

! Do they determine market share?

Yes. The larger brokers are computing market share, one of the largest to suggest that he has 15% of the market. There are five companies in Kiev that are large and much more dominant.

! Are there broad advertising approaches?

Yes, the legitimate companies advertise in publications and many competitors analyze the depth and breadth of the competition by the number of ads that are run.

! Have they developed data bases?

There are some data bases that are available. Janus has 30,000 residential properties in its data base going back 15 years. Each individual larger company maintains its own data base and now the banks are utilizing their individual data bases for mortgages that they have let over the time period that they have been in that business. There is no national, unified data base, nor MLS program that has scope beyond a fairly limited range.

! Are there any evaluation methodologies?

Many companies have an appraisal division in their firm and sometimes even the smaller ones. This allows the appraisers to make a living if they cannot work at it full-time. In addition, brokers use their sense of the marketplace by taking comparative market analysis in the neighborhoods in which the properties exist. This is not unlike most of the rest of the region and Western countries.

! What is their organizational structure?

The larger companies in both Kiev and Odessa have organized themselves into departments and divisions not unlike their Western counterparts. There is *delineation between commercial brokers and residential brokers and many have appraisal departments, property management departments, a legal and accounting department, and a training department.*

! Do they do commercial brokerage as well as residential?
In the smaller companies, the practitioners do all forms of real estate. The larger companies have divided into commercial and residential brokerage, although most companies indicate the bulk of their income comes from residential transactions. There are some commercial companies that fundamentally are focusing on income properties, investment analysis, and commercial brokerage and property management, but even in these instances, there generally is a residential division in the company although, in some instances, quite small.

5. Association Development

! How sophisticated is the real estate association?
The URA is a relatively small association with limited staff capacity. They reside in two rooms in a prestigious business center in downtown Kiev. Vladislov Orlov, the Executive Director has been with the association for 10 years, and as such, is one of the senior association executives in the region. He has four additional staff members. The URA recently hosted the CEREAN Conference attended by 400 people in downtown Kiev that went off nearly without a hitch. That speaks very well for the ability of the staff to perform complex tasks that are out of the ordinary.

Also the recent acknowledgement of their lobbying capacity speaks to some degree of sophistication. There are those that are more cynical that indicate that too much credit may have been given to URA for the successful passage of the Transfer Tax Reduction.

Regional associations also have limited staff capacity with the exception of the Kiev Real Estate Union, the association of 42 larger companies in Kiev which is stronger.

The URA also publishes books and statistics on the real estate market in Ukraine that may be useful but the information is substantially dated. It also has a website which is updated nearly daily.

! What is the quality of their training program?
The certification program is the major educational effort by the URA. That is limited to 275 students in 11 offerings in 3 cities. The only additional training is programs at their conferences and conventions.

Additional capacity has got to be developed to grow the business in Ukraine.

Training programs in the regions are on a sporadic, quarterly basis and are limited to one to two days. They are not involved directly in delivering the certification program which may be a mistake.

! Are there clear job descriptions for lay leadership and paid staff?
Yes. The URA has developed job descriptions for all officers and the staff which has been passed by the Board of Directors.

! How effective are the leaders and staff members?
The President is thoughtful and dedicated, but seems to have lost sufficient support of the Board to allow for a competitive race for re-election.

Orlov has proven to be a steady and reliable EVP who uses his military and educational background to his advantage.

! Do they have effective communication mechanism for their membership?
The primary source of communication is the website which the officers encourage all to read daily. They readily admit that this doesn't happen often. URA attempts to get messages to the members through the media, also with mixed results.

A well-thought out communications plan needs to be implemented.

! Is there long-term viability and sustainability in the association?
The URA can and has sustained itself for 11 years with fairly limited membership of 500. A combination of that dues income plus income from their various conferences supplies them with sufficient income to continue into the future. Their office space is extremely small and on a shared basis with an insurance company. Therefore, their overhead costs are limited.

Vladislov Orlov has been with the Association for a substantial period of time and appears to know how to survive.

For the Association to truly have an impact on the country, it needs to grow itself to represent between 40%-50% of the legitimate practitioners in the country. This may require expanding its membership categories for more deeply involve the agents as well as the managers. While there is resistance from some managers to involve themselves in this activity, in the long-run, it will be to the advantage of the Association to do so.

! How well is the industry viewed by government officials and the society in general?

Most practitioners are still troubled by the negative activities of the "black brokers" and "mucklers" in the marketplace. However, there are a series of larger companies that have distinguished themselves as market leaders and do not feel that this is as substantial a problem as it had been 6-8 years ago.

They have not been able to get a real estate law passed, but, in fact, successfully worked on a transfer tax reduction and gained recognition in a business publication as one of the top lobbying forces in Ukraine. They assert that they have very good relations with the Ministries, the Members of the Parliament, and the Presidential area, after years of working in these environments. There are a number of former members that are now in the Rada that they rely on to help carry their mail.

Summary

Real estate practice in Ukraine is beginning to flourish. Since the abandonment of the "exchanges" seven of which controlled the marketplace prior to the year 2000, many companies have grown and expanded. At the top end of the market, there are some very sophisticated players that understand how to be profitable and how to represent clients openly and successfully.

Even at that, the percent of brokerage-assisted transaction is very low throughout the country at 15%. While some markets, the percentage may be higher, across the board, it is extremely low. This would indicate that there is a need for continued education and perhaps a certification program which would recognize those practitioners who are serious about the business and have contributed to their educational basis to improve their practice.

It also seems clear that there is a need for additional legislative redress on some provisions in the very complex, Ukrainian legal framework. Overlaps and contradictions should be removed and considerable thought should be given to the possibility of recognizing the realtors as a profession.

There is a decided lack of adequate data bases and information on the marketplace.

With members willing to co-broke on a fairly normal and regular basis and serious attempts being made to start MLS and data-sharing services, the environment seems ready to attempt to streamline the MLS systems and work towards more exclusive listings. Since sellers do not pay commissions, there seems little reason for them not to exclusively list and put the properties on an integrated system that would work broker-wide.

The Association's governance structure is as it was approximately six years ago. They could benefit from a structural audit and a strategic plan which might re-focus their energies, leads to *a broader and wider certification program, and expand their membership base. Personalities still play a substantial role in the association politics in Ukraine. That may be, in part, due to the relatively small size of the association given the number of members, geographic size, and population base. It also is probably a result of the fact that leadership does not turn over either at the national level or at the regional level on any regular basis. Some of the regional representatives have been there for 6-8 years. Some dynamic leadership training would be a useful addition to help adjudicate that problem.*

The market has been encouraging and prices have been increasing. In addition, for the first time in the last three or four years, mortgage capital is now becoming available. This is breathing new life into markets in the major cities and allowing properties for the first time to appreciate in value to a point where home ownership becomes more of an "investment" than simply a place to live. In looking at some specific properties, the new ones seem fairly equitably priced, but the secondary market still lags behind new construction. This is not uncommon in Western markets or in the Region but the overall pricing of these units still lag replacement by up to 50%. I believe a well-rounded mortgage program would go a long way towards advancing the economy of the Ukraine and create additional equity for its citizens that can be tapped for small/medium enterprise development.

UKRAINE

CONDUCTING A REAL ESTATE PRIVATE PRACTICES
ASSESSMENT IN TRANSITIONAL MARKETS

FEBRUARY 11-21, 2006

Appraisal by: Norman D. Flynn, CRE, CRB, CIPS

Preface:

Quantitative Analysis

1. How many valuers (appraisers) exist in the marketplace?

The State Property Fund lists 6,000 total individual appraisers of which 3,000 are active and independent.

2. Assess the number of companies into which these practitioners are formed. Estimate the relative size of the companies.

There is an estimated 700 appraisal entities in Ukraine of which about ½ work on a regular basis. They range in size from 2 or 3 persons to 20-30 in branch operations. About 100 companies are substantial and highly recognized.

3. Determine the fee practice in the country. Who orders and uses appraisers? How many appraisals does the average practitioner do per year?

Residential appraisals, if ordered by the banks, are between $60 and $100. Individual practitioners on the residential side charge between $120 and $175 with a common fee being $150. Appraisals of larger, more complex commercial ventures are on a flat-fee basis dependent on the complexity and time required. Evaluation of shares (stock equity evaluation) is also on a flat-fee basis and is done approximately every three years for larger international companies..

The banks are required, by bank regulation, to have independent third-party appraisers but most ignore this or add another layer of appraisal and reduce the values accordingly. International corporations need regular re-evaluation and that becomes a major source of appraisal income (in larger companies, up to 30%).

While I could find no companies that international investors or corporations would hire directly, the big three accounting firms would sub-contract with some of the better appraisers to do the preliminary analysis for their review.

There still are commercial properties to be privatized by the state (estimated at between 21% to 30% of the original inventory). This will be a source of substantial income to the appraisal community focusing on commercial properties.

4. Have "standards of practice" passed into law in the country's legislature? Do these standards subscribe to TEGOVA? Do the standards subscribe to world standards?

There is an appraisal law on the books from 2001. It does set out some methodology but does not subscribe to Tegova standards nor the International Valuers Standard (IVSC). In fact, the legislation in some instances are in conflict with the IVSC.

5. Are there any Western valuers/appraisers in the market? What percentage of business do they do?

The major accounting firms are all in Kiev and throughout the Ukraine. They typically have, on staff, valuers who have substantial credentials that could do larger appraisal.

6. Are there appraisal standards for commercial large real estate transactions?

Yes. There has been considerable coursework brought by the UTO into Ukraine to assist them in doing complex appraisal. This education has been going on for 11 years and has been taught by experts from Europe, Russia and the United States.

7. Have valuer associations evolved in the marketplace? What number and percentage of practitioners belong? What is the dues' structure?

Yes. The Ukrainian Appraisal Society (UTO) has been in existence for 11 years. It has 1,400 members which represents slightly less than half of the active practitioners. They contend that they have the "most" active practitioners. They now may be active but are part of either UTO appraiser state valuation committees, banks, or other companies where their primary work is not appraisal. They collect 100 RAH ($60) from approximately 1,200 of their members and their "leading appraisers" and "honorary members," numbering approximately 140, pay $110. There is a continuing education requirement which allows the associations to make substantial monies keeping appraisers abreast of current market conditions and changes. They have an executive vice president and secretary that houses the Association at the State Property Fund office.

Second, the Ukrainian Appraisal Institute had been active and organized to represent corporate membership. At its peak, it had approximately 80 members of which 25 paid. They are no longer active – they strongly support the UTO and its activities.

The Association of Appraisers of Ukraine is a new organization with approximately 300 members, mostly young coming out of the Kiev Real Estate College. It appears that there are only 25-30 overlap members between UTO and the newly formed organization.

8. Are there ongoing training programs to upgrade the quality of valuers in the market?

Yes. There are substantial training programs that are put on both by the Kiev Real Estate College and various other schools and institutes totaling 36 in the country. In addition, UTO sponsors regular continuing education programs through eight institute outlets throughout the country. Additionally, the UTO brings in outside experts to participate in seminars with meaningful topics.

9. Is there an enforcement mechanism in place for standards that may exist?

The UTO has an enforcement policy where, if a member complains, there can be a peer review of reports. If the reports are found to be deficient, the member is asked to upgrade their practice and improve their report writing.

This peer review has been a source of frustration and is one of the reasons why UTO members feel that the new splinter appraisal group was formed because they didn't either have the skills nor wanted the discipline.

10. Are there "designations" for higher quality practitioners?

There is a higher designation in UTO called "Leading Appraiser" and "Honorary Member." This represents somewhat less than 10% of their members.

Unfortunately, it is viewed by the outside world that these are the people who have the great option to do appraisal work when the country is privatizing particularly commercial ventures.

Qualitative Analysis

1. What is the quality of appraisal reports generated by the practitioners? Would reports generated by the practitioners meet Western standards and expectations?

I have viewed appraisal reports over the years in Ukraine and the leading appraisers definitely subscribe to Tegova standards and Western practice in report writing. It is sophisticated and has substantial mathematical tables and discount analysis.

The reports that the appraisers and the banks prepare, however, are one to two page efforts with very little detail and a portfolio of photographs.

2. How sophisticated is the valuation practice?

   ! Do they have an established data base?

   Most appraisal firms have accumulated their own data base and rely on broker relationships and other leading appraisers to accumulate more.

   There is no data base available in the country or within the cities available to the appraisers to get current and updated market changes. As markets have been moving, particularly in Kiev, at a rapid rate, this puts appraisers at a disadvantage especially on the residential side where some prices are estimated to have increased by over 30% in the last 18 months.

   ! Do they share data base with other practitioners?

   The top leading appraisers, in fact, will share their data base; however, it is not common practice and there is no common data base available.

   ! Is there mutual respect between and among competitors in the marketplace?

   Yes, the UTO has been particularly collegial in their conduct and activities over the years. They have multiple meetings where everyone seems to be getting along extremely well and they work closely together on common projects.

   ! Are they retained by Western buyers and sellers?

   By and large, no, although some appraisers have indicated that they have done substantial work for major investors from the West in Europe and occasionally in America. This, however, is the exception, rather than the rule.

   ! Are their valuations accepted by lenders?

   Every lender interviewed indicated that they had no confidence in the valuation of outside, third-party valuers. That is not to say that the valuations aren't good; it is just that the banks do not trust a system that can be bribed, and therefore, resort to their own, in-house appraisers.

3. How sophisticated is the valuer association?

   ! Is their code of ethics effectively enforced?

   UTO has a code of ethics and it is enforced.

   ! Do they have high quality training programs attended by a large majority?

Training has been and continues to be ongoing both in the Regions and in Kiev. Additionally, the State Property Committee and the Ministry of Education has authorized 36 new education centers. The problem UTO has with that is that there are not enough quality instructors to people these institutions and, therefore, the quality of education, in their view, is dropping.

! Do they have effective communication devices?

Yes, they report regularly on the internet to the appraisers and send out updates and bulletins on upcoming events and changes.

! Do they communicate changes in valuation methodology and regulatory bodies?

They do communicate changes in valuation methodology and regulatory bodies on a regular basis. They meet regularly and discuss these in considerable depth.

! Do they host meaningful conferences?

Yes, not only for their own members within country but also regional conferences are hosted from time to time.

! Do they attend appropriate international and transnational valuers' activities?

The leading appraisers are frequently seen in both Tegova and Russian Conferences.

! Do they have effective leadership? Effective staff?

Olena Koval has been the President of the Association from the beginning. She is an extraordinarily bright person that seems to have a clear vision as to where the Association ought to be going. The current Executive Officer, though unmet, has been with the Association for six years. This probably means that she performs fairly effectively.

It probably is time for Olena to step down from the Presidency. There were complaints that the management of the UTO has stagnated and, therefore, was unresponsive to some of the potential members and existing ones. As a consequence, they are the ones that have suggested that the splinter organization was formed.

! Do they show signs of growth and viability in the future?

The UTO has been around for 11 years and seems to be alive and well. They have not grown substantially in the last 3 or 4 *years. Until the mortgage program becomes more expansive and banks rely on independent, third-party appraisers, the quantity and quality of the market is relatively stagnant. Now that the bulk of the residential privatization is completed, all that remains are some of the larger commercial and land entities that require specific training and will limit many of the companies practice.*

4. What deficiencies in the practice are noted? What meaningful corrective action can or will be taken?

The primary deficiency is that the Association, while it has solid, rational methodology, and, in many ways subscribes to the bulk of TEGOVA Standards of Practice, they do not subscribe to the International Valuers Standards. In a recent program that was hosted by UTO in December 2005, George Badescu of Romania outlined a series of steps that have to be taken to change their law and the method of certification.

There also seems to be a political problem within the Association and the State Property Fund. The new Socialist leader has encouraged the splinter group to form and become active, as opposed to preceding State Property Fund heads who look primarily to UTO for valuation and appraisal services. This probably means that there will be some "political" valuations done in subsequent privatization efforts. Since the new Socialist Party Chairman has arrived, no additional privatization has taken place. One can assume that there is some validity in the fact that they want to delay moving this privatization forward until they have more "flexible" valuers with which to work.

The top appraisers of the UTO are, in fact, a very knowledgeable and stable professional group. They see quite clearly what may be required and appear to have the political will to attempt to accomplish it.

There should be a concerted effort to improve the data base available to all valuers so that a more consistent appraisal can appear both across appraisal lines within the mortgage community as well as the brokers.

Summary

It is time for the Ukrainian Appraisers who have meticulously evolved reasonably strong, Western-style methodology to get to International Valuers Standards. This will require a substantial effort to help convince the State Property Fund that while they can do the basic registering of appraisers and basic certificate that the final certification should be done outside of the government by the public. This is the direction that the Russian Society of Appraisers have prompted the Duma to go which removed itself from the certification process in January 2006.

To accomplish this, we will need both some political expertise to navigate the waters of the State Property Funds, Ministries, and Rada as well as sufficient international and regional experts that can testify as to the benefits and the nature of subscribing to IVSC.

When they reach IVSC standards, this should open additional directives for investors, encourage international banks to continue to move into the marketplace and open the real estate mortgage markets, not only to the major five cities, but to the rest of the Ukraine.

ATTACHMENT 3

IRPF
International Real Property Foundation

March 9, 2006

Mr. David C.M. Lucterhand
Chief of Party
Access to Credit Initiative
PRAGMA Corporation

Dear David:

With this, please find a copy of my Trip Report and the Assessment, which I conducted in Ukraine on February 11th to the 21st. I thank you again for the great support and many courtesies you extended during that assessment.

I am pleased to report that there is considerable progress in the development of both the brokerage community and appraisal community in the Ukraine. While they have a considerable distance to go, the last four or five years have been increasingly productive resulting in a number of firms becoming quite sophisticated and associations that appear to be self-sustaining into the future.

The appraisers have had considerable technical training and fully subscribe to TEGOVA Standards. There is a need, however, to bring them to the International Valuers Standards (IVSC) and they already started to move in that direction. To do so will require certain modifications in the Appraisal Law passed in 2001 and moving away from a governmental certification to a "public certification."

The interventions that we would recommend for Ukraine are as follows:

BROKERS CERTIFICATION PROGRAM

Background
There has been an attempt by the brokers to pass a real estate law, which would both recognize them as a profession and establish licensing. Three of the five major regional associations have opposed the licensing portion because of their inherent fear of corruption and added layers of costs. Efforts to pass this legislation have failed over the past eight to nine years.

The Ukrainian Realtors Association (URA), five years ago advanced a certification program calling for five days of formal education and a sixth day of examination at a cost of $100. They have little to show by way of results for this effort inasmuch as there are 200 individuals certified under this program and only at a maximum 275 could take the course in any given year. They claim that there are more that have passed the certification courses but because they are not members of URA, cannot use the designation. The Kiev Real Estate Union (Union) is now teaching certification and has approximately 120 people certified in their program. They have an objective to gain an additional 600+ in the next 18 months. There is no cost for their program other than the $500 annual dues that the 42 companies who belong pay.

Certification Program
We would recommend that the key players in real estate education in Ukraine be brought together to carefully define the "common body of knowledge." That would define what the certification courses should be teaching. Additional analytical work would be done to devise courses that would be streamlined to both speed the process of education and reduce its costs.

We would secondly recommend that we merge the certification programs between URA and the Union. In informal conversations with the leadership of both, there seems to be an appetite to consider this possibility. Apparently, personalities in the past have precluded this from happening.

We would then recommend that as soon as practicable, a program to substantially increase the numbers of those certified be put into place, which would include but not be limited to: allowing for test-out options for those who have been in the business a considerable period of time, the approval of company training that shows evidence that they have learned the common body of knowledge, and a method to decrease the costs to offer the courses in the regions throughout the country. Partly underwriting the cost of the curriculum development and delivery of courses will be key to achieve program expansion.

Lastly, we would recommend that a public relations effort to inform the general public of the importance of dealing with those that are certified be put into place. This would give incentives for more real estate practitioners to pursue certification and give credibility to the course and concept.

ASSOCIATION DEVELOPMENT

Background
Both the URA and the Ukrainian Society of Appraisers (UTO) have been in existence for eleven years. They have found ways to be self-sustainable and have maintained or grown their organizations to encompass a fairly large portion of the professionals (especially the appraisers) in the country. However, both have the same organizational structures that they had eleven years ago and in the case of the appraisers, the same president.

Presidents of the URA have served on average four years. The regional leadership also does not turn over leading to a stultification of the organization and its leadership as well as resulting in personality conflicts that hinder cooperation and integration.

The Brokers

We would suggest that a strategic planning process and a structural audit be initiated for the URA. This would include examining the value-added nature of the association to the individual agents, developing a streamlined, effective government affairs program, and carefully analyzing the educational offerings that the association produces.

Under the structural audit, careful examination of the governance of the organization with recommendations should be made. Such recommendations should include, but not be limited to, changes in their founding documents to both streamline the operation (there are 30 members of the Board of Directors of URA) and ensure an ongoing turnover in leadership (For example: establishing term limits and a president-elect system).

The Appraisers

During the same intervention, host a strategic planning and structural audit process for the UTO. This would allow them to examine additional programs, products and services to bring additional values to the membership including the possible establishment of a nationwide data base system.

The structural audit would likewise examine possible changes to their founding documents to ensure a reasonable turnover of leadership at each level and streamline its governance operations.

ESTABLISH A VIABLE NATIONAL HOUSING/REAL ESTATE DATA BASE

Background

The appraisers do not have any universal data base nor do the banks. They fundamentally rely on anecdotal evidence and information from certain brokers as well as published advertising.

The banks also have no reliable data on which to look at property valuations. They consequently rely on in-house appraisers whose basic prime objective seems to be to lower the values as much as possible.

There are small pockets of data that are available in the marketplace both through the Unions' early attempts at an MLS, the Regional Odessa Association's informal agreement with 17 companies, Janus firm's data base of 30,000 transactions over the last 14 years, as well as the mortgage associations' early attempts at data collection.

We would propose to develop a data collection mechanism in cooperation with the UTO, the URA, and these component parts to derive a nationwide data collection system. We would enlist the support of a leading expert in data accumulation and regression analysis from the United States. Dr. Richard Green of Washington University has agreed to do this work on a "pro bono" basis. We would hope that this would initially drive quarterly price reports from major markets in Ukraine and eventually monthly. We believe that this data will help the appraisers, the lenders, the brokers and the government better understand price fluctuations and where the markets are in Ukraine.

DEVELOPMENT OF A MULTIPLE LISTING SERVICE

Background

The Union has the beginnings of a Multiple Listing Service (MLS) and some of the larger companies are attempting to establish these. More and more of the firms are moving towards "exclusive listings" and would like to get there to bring clarity to the market and more efficiency. Every major broker interviewed favored the possibility of working with an MLS.

MLS Project

We would propose to establish a prototypical MLS system that has been under development for emerging markets for the past three years. It is a system of cooperation between brokers and the sharing of property information that will allow the market to be much more transparent and pricing easier to determine. Since the multiple listing service is most advanced in the United States, it would take the essential elements of the United States' system which have been indigenized to emerging markets. This would include the necessary agreements, forms, and contracts between and among brokers who participate in MLS.

In addition, rational software has been written that can be inexpensively installed and utilized for MLS transactions. Since many of the brokers in Ukraine have internet access, it would be internet based for both speed and convenience.

The final element of an effective MLS is training of both the brokers and agents in the use of the systems. These trainings would be made available on a regional basis throughout the country.

As a natural extension of MLS, we would recommend that the URA join the International Consortium of Real Estate Associations (ICREA). This would allow the properties on the MLS systems to be transported up to an international site to make them available for international buyers, investors, and brokers. In addition, it would give referral business options and opportunities to the agents and brokers for an additional value-added benefit for the associations.

ESTABLISH INTERNATIONAL VALUERS STANDARDS IN UKRAINE

Background
It is imperative that International Valuers Standards be incorporated into the appraisal community in Ukraine. This will allow for increased direct foreign investment, add credibility to the appraisers, and give confidence to the banking community of both the preparation of and competence of Ukrainian appraisers.

IVSC Program
The program to bring these standards to the Ukraine would be multiply-pronged. It would begin by pulling together a planning group of the key stakeholders in appraisal in Ukraine including representatives of the banks, insurance industry, auditing, real estate, appraisal, the State Property Fund, and other appropriate ministers. They would do a thorough analysis of the IVSC and what is required for the Ukraine to reach IVSC Standards.

We would intend to supply expert support for this group to assist them in this analysis. That would include a summary and articulation of what the IVSC Standards are, a description of the deficiencies in existing regulations and laws impeding the adoption of those standards, and a description of a public certification program.

The International Valuers Standards have been translated into Russian and that may be sufficient. If insufficient, Ukrainian translation might be required. It is anticipated that if the planning body adopts these provisions, training courses would be made available throughout Ukraine teaching what the International Valuers Standards are and what would be required to subscribe to them.

A careful lobbying program is envisioned to help get the necessary amendments passed to the existing regulations and law. We would intend to bring expert advocates to assist in the development of a strategy to pass these laws.

SUMMARY AND CONCLUSION

We would expect that these comprehensive programs articulated above would take between two to three years to accomplish. If these are directions in which both Pragma and the Mission can agree, the IRPF will carefully cost-out and write a proposal, which would articulate goals, objectives, and measurable outcomes annually.

We believe that with an expanded certification program for brokers and increased confidence in both their capacity and capability that the market will move more freely and there would be more competent lending done in the Ukraine.

Additionally, if the appraisal community achieves reaching International Valuers Standards with the appropriate certifications, there would be more confidence in them and their capabilities by every sector both internationally, nationally, and from the lending community.

Lastly, if there were adequate data on the housing market, it would create considerable transparency and more confidence in the consumers as to what the values are. This, in turn, will lead to more liquidity in the market and a much more vibrant dynamic market to help grow the economy in the Ukraine.

I am looking forwarding to working together in Ukraine.

Sincerely,

Norman D. Flynn
President and CEO

cc: Rick Gurley

ATTACHMENT 4

WORKSHOP ON CREATING A MUNICIPAL FINANCE FACILITY FOR UKRAINE

The Workshop is co-sponsored by the Ministry of Finance; the Ministry of Construction, Architecture and Housing and Communal Economy; and the United States Agency for International Development/The Access to Credit Initiative

Date: Friday, January 27, 2006

Place: Academy of Science, Volodymyrska Street 55 (3rd floor), Kyiv

Attendees:

Senior leadership of the Government of Ukraine involved in policy decisions affecting local infrastructure financing and investment; city mayors and finance directors; Association of Ukrainian Cities; communal service enterprise executives; investment bankers; international donor agencies; potential investors.

Purpose:

The workshop will consider the creation of a new finance facility that specializes in making long-term infrastructure loans to cities and communal service enterprises. The institution would raise capital at market interest rates, and lend to creditworthy cities and utilities. Loan repayments would be pledged as collateral to the investors who provide capital to the institution. The institution's staff would become expert in evaluating the creditworthiness of cities and communal enterprises. At the workshop, nine experts from three continents including three former Chief Executive Officers of bond banks, will make presentations. They will describe infrastructure finance facilities that have operated successfully around the world. New research on the creditworthiness of Ukraine's cities and communal enterprises will provide context for evaluating international practice in infrastructure finance. Russia's ongoing effort to create a municipal finance facility will be described. To conclude, all experts will jointly discuss key issues for the proposed finance facility's business plan, including:

- Financial structure, including sources of core capital and lendable funds; credit enhancement
- Operating policies: standardized loan documents, credit evaluation, loan monitoring
- Enabling legislation and regulatory oversight.

Conference Chairman: *Dr. Vitaly Lisovenko, Deputy Minister, Ministry of Finance*

Agenda

Friday, January 27, 2006

8:30 – 9:00 **Registration**

9:00 - 9:20 Welcome and Introduction: *Dr. Vitaly Lisovenko; Earl Gast, Director USAID Regional Mission to Ukraine, Byelorussia & Moldova*

9:00 – 9:10 Dr. Vitaly Lisovenko, *Deputy Minister of Finance*

9:10 – 9:20 Earl Gast, *Director, USAID Regional Mission to Ukraine, Byelorussia & Moldova*

9:20 - 10:15 Introduction to Municipal Finance Institutions, and the Benefits They Offer to Transition Economies

Dr. John E. Petersen, Professor of Public Policy and Finance, George Mason University, USA

10:15 - 11:00 Municipal Finance Institutions in Western Europe: Structure, Operating Policies, and Track Records; Feasibility of Creating a Municipal Finance Facility for Ukraine

Nicholas Anderson, Senior Vice President, Swedish Export Credit Corporation
Lars Andersson, Coordinator for Regional and Local Authorities, Swedish Export Credit Corporation

11:00 - 11:15 **Convenience Break**

11:15 - 12:00 How to Succeed in the Business of Municipal Finance

Johan Kruger, Founder and Former CEO, Infrastructure Finance Corporation Ltd., South Africa:

12:00 - 13:00 Evaluating the Creditworthiness of Ukraine's Cities and Utilities

Part I. Ukrainian Intergovernmental Finance: Theory and Practice

Dr. Wayne Thirsk, Senior Advisor, The Access to Credit Initiative

Part II. Municipal Creditworthiness and Fiscal Decentralization: How does Ukraine Compare with Other East European Countries?

Francis Conway, Senior Associate, The Urban Institute, USA

13:00 - 14:00 **Lunch**

Friday, January 27, 2006, *continued*

14:00 - 14:45 Legal and Regulatory Issues to Consider in Establishing an Infrastructure Finance Facility; Assessment of Ukraine's Draft Law on Local Borrowing

Michael DeAngelis, Municipal Finance Legal Expert / The Access to Credit Initiative

14:45 - 15:30 Lessons Learned from Planning a Municipal Finance Institution for Russia

Dr. Sergey Sivaev, Institute for Urban Economics, Moscow

15:30 – 15:45 **Convenience Break**

15:45 – 16:15 Considering A Municipal Finance Institution for Ukraine: Strengths, Weaknesses, Opportunities, and Threats

Michael Curley, Director, Global Environmental & Technology Foundation, Washington (The presentation is provided under financial support of the Office of International Affairs of United States Environmental Protection Agency)

16:15 - 17:15 **Panel Discussion**

Outlook for Creating a Municipal Finance Institution for Ukraine; Comments on the Proposed Recommendation to the Government of Ukraine

Moderator: John E. Petersen

Panel members: Dr. Vitaly Lisovenko; Pavlo Kachur, Minister of Construction, Architecture and Housing and Communal Economy; Nicholas Anderson, Lars Andersson, Johan Kruger, Francis Conway, Wayne Thirsk, Michael DeAngelis, Sergey Sivaev, Michael Curley

I. Options for Financial Structure
II. Operational Issues for an Infrastructure Finance Institution
III. Legal and Regulatory Issues for a Municipal Finance Institution

17:15 - 17:45 Discussion and Comment by Workshop Participants

17:45 - 18:00 **Closing Remarks**

Dr. Vitaly Lisovenko, *Ministry of Finance*; Pavlo Kachur, *Ministry of Construction, Architecture and Housing and Communal Economy*

18:00 – 19:30 **Reception**

ATTACHMENT 5

Municipal Finance Facility Ownership Structures: A SWOT Analysis

Provided under the Access to Credit Initiative – USAID/Ukraine

March 22, 2006

John E. Petersen

Background

The Government of Ukraine (GOU) is considering the establishment of a municipal finance facility or "bond bank." Such a bond bank would be established to provide a source of long-term capital to finance the infrastructure needs of Ukrainian local governments and their communal service enterprises. The possible ownership structures of a bond bank and how these might affect the scope and scale of a bond bank's operation are the subject of this report. Many models exist for municipal credit facilities around the world. These will be examined as illustrations of various ownership options, and as guidance on appropriate models for Ukraine.

Boundaries and Structure of this Report

As the following discussion will indicate, there are many forms that bond banks may take, and many services they may perform. This analysis of ownership structures is performed taking into consideration several preliminary boundaries regarding the establishment of a bond bank in Ukraine.

- May be capitalized by GOU and international finance institutions such as EBRD and IFC
- May raise lendable funds by borrowing in domestic financial markets
- Will not carry a GOU sovereign guarantee
- Will not on-lend donor funds (but such funds may be used for reserves)
- Will lend (and/or guarantee loans) to cities and communal service enterprises
- May have an indemnity fund to protect investors from loan defaults

This report provides a rapid assessment of the strengths, weaknesses, opportunities, and threats (SWOT) of several possible ownership structures for the bond bank. It considers four possible ownership structures:

1. Majority ownership by "private" non-governmental entities
2. Majority state (central) government ownership
3. Majority communal (city) ownership
4. Multiple owners (no single controlling owner)

These alternatives are examined after a general discussion of bond bank structure and operation providing international examples that offer lessons for Ukraine. The ownership and control alternatives are then subjected to a point-by-point SWOT (Strengths, Weaknesses, Opportunities, Threats) analysis. The report concludes with findings and a recommendation for the preferred ownership structure.

This report will not consider the legal format of the bond bank, except to note that the bank could either be formed under existing laws or by new legislation.

Rationale for Bond Banks and Bond Pooling

Bond banks are financial intermediaries that raise funds in the capital markets to finance local government capital spending. Bond banks can deliver a number of credit-related products, including the following:

- Long-term loans for infrastructure
- Short-term lending (debt due within one year)
- Loans matched by grants from GOU infrastructure programs
- Lease Financing
- Credit enhancements
- Technical assistance / oversight

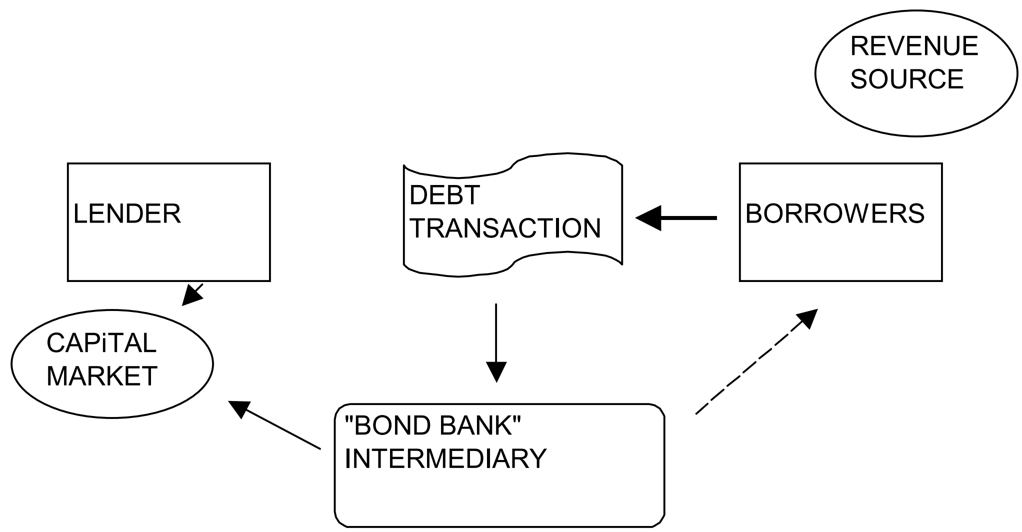
Bond banks can lend directly, or they can buy qualifying loans from local banks, thus acting as an apex (wholesale) bank.

A common characteristic in sub-national government borrowing is that local government borrowers and the individual loans they take are small, frequently too small to interest private capital markets that are oriented to larger (and fewer) borrowers. In Ukraine, almost all cities and communal enterprises are inexperienced in marketing debt obligations to the capital market. This typical emerging market situation suggests pooling small city or utility borrowings into larger, more efficient groups or "pools" in order to achieve various economies of scale that are possible with larger issues of bonds.

Pooling also brings a reduction in risk through portfolio diversification, resulting in reductions in the cost of borrowing to the participating local borrowers. The technique of bond banking – in which a financial intermediary pools together small loans, and itself borrows in the financial markets, pledging loan pools as collateral – has seen extensive use in developed markets, but only limited use in developing country financial markets.[1] Common impediments to broader adoption are 1) reluctance of central government on-lending agencies (including government-owned banks) to relinquish control over the borrowing by subnational governments and 2) limited capacity of local markets to finance longer-term debt transactions. The first factor is not now a limitation in Ukraine. However, at present, there is an effective five-year term maximum on Ukrainian city borrowings, which is a very short period for infrastructure finance. A bond bank might be able to quickly and effectively extend that maturity horizon.

[1] See John Petersen (2002). Given their small size and lack of market experience, local government issuers face high transaction costs in individual bond sales. Aside from just delivering economies of scale, the bond bank intermediary provides on-going oversight of loan performance and helps to establish uniform, transparent accounting and reporting norms at the local government level.

Figure 1: BOND BANK (POOLING)



The essential relationships in the bond bank approach are depicted in Figure 1 above. The bond bank in effect bundles the underlying sub-national debt and then sells its own bonds to investors in the capital markets.[2] The basic idea behind the pooling concept is to develop a portfolio of loans that can then be remarketed in bulk to the securities markets as bond bank obligations. Bond bank obligations almost always have one or more credit enhancements, such as added reserves, intercept provisions that grant creditors access to cash flows, or bond insurance.

Pooling also provides a number of inherent credit enhancements because of the size and diversity of the pool's portfolio, which protect it from both individual "event" risks and systemic risks. This means that with appropriate design, a debt service problem with one borrower (or even a class of borrowers) can be successfully handled with reserve funds and other credit supports, and by the pool's diversity. The loan pool itself mitigates credit risk. It has inherent financial stability.

The pooling intermediary also achieves economies of scale, which are especially important in financial markets. There are economies when the bond bank makes a sizeable borrowing in its own name (reducing legal, advisory, investment and trustee fees); and also when it monitors loan performance for its investors. The Tamil Nadu Urban Development Fund has pioneered a credit pooling approach in India and is a leading example in developing markets. The bond bank concept has seen great use in the developed financial markets of North America and Europe, as is illustrated below.

Variations in Bond Bank Financial and Managerial Structures

[2] There are legal distinctions between "pools" or "funds" that represent the resale of interests in the underlying portfolio and in bond banks that sell their own obligations that represent undivided shares in their "business." These distinctions can be important in matters of securities regulation and taxation.

This section reviews how the financial and managerial aspects of a bond bank interact. Figure 2 depicts several options for organizing bond bank operations. An important design question is which services will be provided by the Bank's permanent staff, and which will procured by contract. Most bond banks have very small staffs. Many banks contract with private sector asset managers for day-to-day operations.
Bond banks may approve individual loans, but contract with commercial banks for loan origination and servicing. In such cases, the bond bank acts as an "apex bank" selling its own securities and using the proceeds to purchase loans from originating banks.[3] Banks may be paid a fee, or may markup the interest rate. The bond bank may also use the contract to share risk with originators, either through partial guarantees from the originating bank, or by having the originator retain a fractional interest in the individual loans.[4]

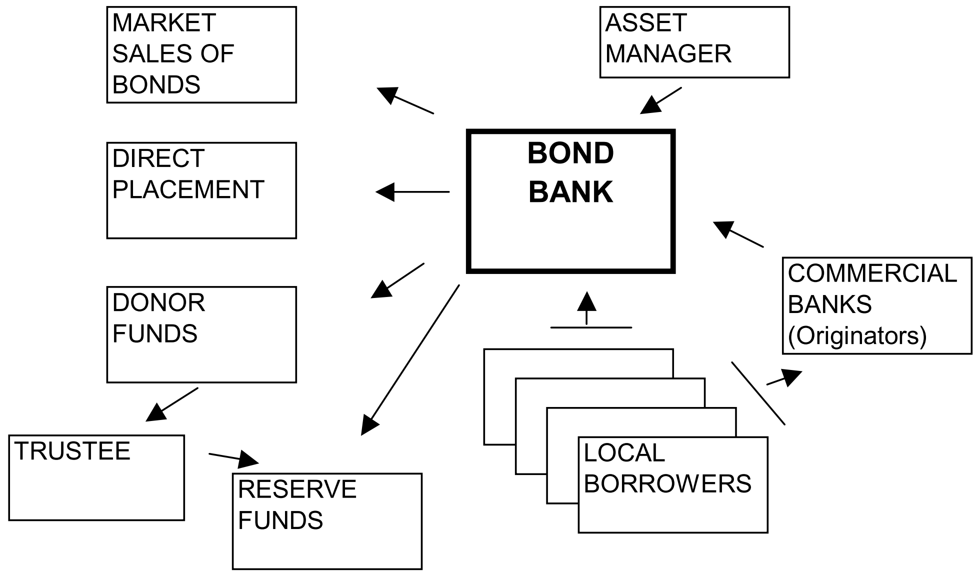
Generally, bond banks sell their securities publicly in the financial markets. However, there also can be direct (private) placements. For example, the Alberta (Canada) Financing Authority frequently places its bonds directly with the Provincial Public Employee Pension System, which holds about a third of its debt. The use of reserve funds, indemnity funds, and trustees to secure bond bank debt raises important design considerations. Adroit design of these funds can help to circumvent issues with international donor organizations that cannot (or will not) deal directly with public-sector institutions unless they carry a sovereign guaranty.

By and large, the ownership and control of the bond bank should not *per se* be the decisive issue, so long as the bank is operated for the public benefit. But the bank's ownership and control do of course influence how the bond bank operates, and ownership structure must support three major operational objectives:

- the bond bank must be *professionally and competently run*
- it must be *transparent and accountable*
- it must have *operational independence* to meet its policy goal of raising capital at low cost for legitimate public purposes.

[3] A common practice is for a bank to receive bond bank approval of a loan to a commune for inclusion in a bond issue. The bank can then provide short-term financing until such time as the bond bank is ready to sell the bonds and take the commercial bank out of its loan. Among others, this is done by the Maryland Bond Bank.
[4] This is the approach used by FINDETER, the Columbian municipal financing authority. See Kehew, Matsukawa, Petersen (2005) Appendix 1.

Figure 2: BOND BANK FINANCIAL AND MANAGERIAL STRUCTURES



The Ownership Structure and its Implications for Operations

At the outset, it was noted Ukraine can consider four major ownership models for bond banks:

1. Majority ownership by "private" non-governmental entities
2. Majority state (central) government ownership
3. Majority communal (city) ownership
4. Multiple owners (no single controlling owner)

Within these arrangements, there are a variety of ways to balance the various possible controlling interests and capital contributors that comprise "ownership" of the bond bank. It is important to understand that the "ownership" concept breaks into two separate issues: who provides equity capital, and who governs (sets policy for) the bond bank. The entities holding equity in the bond bank as a corporation will own it, but the purpose and profitability of equity ownership can vary greatly depending on the nature of the corporation and its chartered purposes.

Bond banks may be created as "special purpose vehicles" or "funds" that are dedicated to a public purpose, or they may be established under the general laws that cover financial corporations. Generally, their charters specify purposes, enumerate legal powers, and describe the bank's governance and initial capitalization.

To a large degree, the ownership structure will be driven by how the bond bank intends to finance its operations. Thus, a major concern is how the bond bank can be configured to tap into various sources of capital and, accordingly how the bank's operation and ownership may interlock. The bond bank can be funded in a variety of ways, but the predominant model is that the bank will serve as a *financial intermediary*, raising funds in the market by its own borrowing (or through the use of enhancements) in order to acquire the loans made to cities and their communal enterprises. As noted at the outset, in

Ukraine this activity is to be undertaken without a sovereign guaranty. The bank is to be self- sustaining. This places a great premium on its ability to act (and be perceived) as a prudent and creditworthy organization.

Among the four ownership models mentioned above, there is a broad range of international experience. In several bond banks, ownership structure has evolved over time.

There are few examples of wholly or predominantly private bond bank ownership, and these are both recent and special situations. A purely private, profit-making structure seems very unlikely for Ukraine, given the risk involved in new market development and the underlying public-purpose of the bank's operation.[5] (It is possible that a state-protected monopoly could induce creation of a private bank.) Both South Africa's INCA and Western Europe's Dexia are special situations.[6] On the other hand, a substantial minority private-sector participation is not unheard of, and this is found in some bond-bank funds India that are designed as special-purpose trusts.[7]

An alternative, represented by the Local Government Unit Guaranty Corporation (LGUGC) in the Philippines is to have predominantly private sector ownership as represented by a non-profit association (the Philippine Bankers Association, 51 percent owner) combined with a minority governmental ownership. The Philippine example is also of interest in that a development finance institution, the Asian Development Bank, now holds 25 percent equity ownership. (Similar structures are found internationally in associations of major banks that own bank clearing facilities, like Ukraine's MFS depository, or financial firms that associate to own and operate securities exchanges.)

In North America, there is considerable precedent for bond bank ownership by provincial or state (oblast level) government. In Canada, local governments are "shareholders" that participate in bank governance, although the Province usually holds the majority of seats on the board. In the case of Alberta Province in Canada, the local governments, which are normally required to borrow through the bond bank, have a minority of seats on the Board and make minimal stock subscription payments. Since the bond bank is a Crown Corporation of the Province (and carries the Province's guaranty) it has very low borrowing costs.

In the United States, almost all bond banks are owned and operated by state (oblast-level) governments, usually as separate corporations or authorities. Their debt is usually <u>not</u>

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[5] The question always is raised that were the bond bank as a private entity a good idea, why has not a private firm (or group of firms) created one? The answer is that without the needed governmental powers and financial "deep pockets," the bond bank business model is not profitable enough to offset the risks.

[6] INCA was created to restructure institutional portfolios and largely has acquired already outstanding debt in the context of South Africa's highly developed capital markets. Dexia was a privatization of state-owned and operated "specialized banks" that lent to local governments in Belgium and France. The state retains a minor interest in the firm, which now acts as a private underwriter and banker.

[7] The Indian trust structure, which is very flexible, allows for mixed ownership and the private firms are both members of the board and may serve as "asset managers." The International Finance Corporation, the private-financing arm of the World Bank, has served as a partial owner of an Indian asset management firm (ILFS).

directly guaranteed by the state.[8] In the United States, there are several legal and tax impediments to a mixed public private structure.[9] A specialized type of bond bank in the United States, the State Revolving Fund, also is prevalent for financing environmental and water supply projects.

In Scandinavian countries, bond banks are run by governmental "cooperatives," often with combined national and subnational government ownership, including ownership by local government insurance and pension institutions. In the case of Sweden, the local governments belong to a co-operative, which owns the bond bank. In Finland the localities and the local government employee pension system share ownership of the bond bank, which also carries a state guarantee. An association of local governments owns the bond bank in Denmark, whereas the central government has dominant ownership in Norway. In cases of majority local government ownership in the Scandinavian systems, for example in Sweden, the local government shareholders bear "joint and several liability". This means that any city's default must be absorbed on a pro rata basis by the members (usually up to a cap of each city's respective capital share). Joint and several liability reportedly creates a culture of creditworthiness and imposes peer pressure on borrowers.

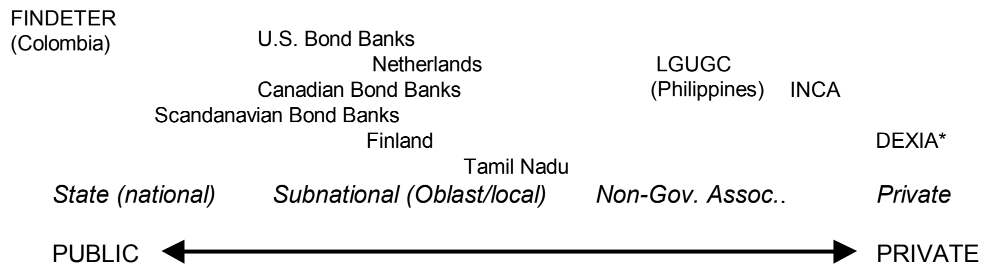
Figure 3 sets out an array of actual ownership configurations. Given the differing definitions of public and private entities in the respective countries, it is difficult to formally divide the public and private sectors. In some cases, bond banks are owned by an association of private firms, like the Philippine Bankers Association. In other cases, some of the shareholders of a "for-profit" bond bank are themselves non-profit entities (as in the case of INCA in South Africa).

The point is that there are many possible ownership configurations that include private sector participation. Private participants may opt to subordinate profit maximization in the near term to build a viable mechanism for local government participation in the securities markets. In other words, private companies, acting in concert through an association and taking a longer-term view, may wish to promote the financial strength and independence of local governments apart from the possible profits achievable from bond banking in the near-to-medium term.

[8] There are a few examples of bond banks owned and operated at the local government level by consortias of local governments. The U.S. bond banks use a large range of credit enhancements to bolster security and typically carry ratings slightly lower than the respective sovereign states (oblast-level).

[9] A major factor in the United States is the tax treatment of securities, which if issued by subnational governments or their corporations, are exempt from federal and most U.S. state income taxes. This does not preclude having private firms work for such institutions, but private firms cannot have an equity interest in the institutions.

Figure 3: Bond Bank Ownership
Arrayed by Nature of Ownership:



*/ has minority government stock ownership

A final point has to do with the financial role of equity ownership in a bond bank. Normally, the role of equity (as opposed to debt and reserves) will be very limited in the capital structure of a bond bank. As a financial intermediary, the bond bank is designed to be a conduit to the financial markets. The major purpose of equity capital is to create a core of capital to "start the ball rolling" and to provide a cushion in case of financial difficulties. The creditworthiness of the bond bank will depend on the quality of its underlying portfolio of loans and whatever reserves it may hold or have access to. These sources provide the primary security to holders of its obligations.

Bond banks typically are highly geared or leveraged on their equity capital base. In the case of INCA in South Africa, the allowable gearing (borrowed funds to equity) is specified depending on the credit quality of the underlying loans. The Philippine bond insurer, LGUGC, has a maximum leverage specified in its trust agreement with the holders of the bonds it insures. In the Alberta Capital Financing Authority, local governments make small subscriptions known as "representational" equity. Annex B provides examples of the differences in equity gearing. Ratios vary greatly, depending on the nature of the bond bank and the degree to which it is run on a commercial basis.

The state (oblast level) revolving funds in U.S. use a combined Federal and state capitalization structure (80% and 20%, respectively).[10] The capitalization fund can be used either for leveraging market borrowings or as a source for loan funds (and therefore eliminating the need for borrowing by the bond bank itself). State revolving funds are wholly owned by the states, and the Federal contribution is a restricted capital contribution that carries legal requirements that restrict its use to environmental purposes.

The relative importance of equity in the overall capitalization of the bond bank and the concept of leveraging equity are discussed in Annex B.

A SWOT Analysis

A SWOT Analysis deals with the "**S**trengths, **W**eaknesses, **O**pportunities and **T**hreats" faced by an institution in accomplishing its mission. Such an analysis needs to cover a broad range of concerns. Many key issues of bond bank design are operational ones that

[10] The revolving fund means that any repayments of interest and principal must be repaid to the fund and may only be used for its purposes. Since administrative expenses are permissible, and under federal law there is no need to repay the capital contribution and no prohibition on lending at zero interest rates, the fund can ultimately fade away.

are unrelated to ownership structure, *per se*. Crucial issues are: 1) the degree to which bank operations are accountable to the owners, and 2) whether bank owners are executing a core strategy of preserving capital, and earning an adequate return on capital. Possible ownership structures range from private (unlikely as a sole source), to mixed ownership (some private ownership in conjunction with management contracts, etc.), to a mixture of local and central government ownerships.

Strengths Related to Various Ownership and Control Structures

- *Promotes high standards of borrower creditworthiness:*
  This relates both to the lending criteria used by the bond bank and the strength of its own security. The ability to achieve creditworthiness of the bond bank is dependent upon the independence, integrity and prudence of its lending criteria. Essentially, the bond bank must lend only to those borrowers that will pay debt service (principal and interest) in full and on time. This is not to say that credit assistance or even subsidies cannot be used, but that they must be explicit, transparent, dependable and carefully designed not to be politically motivated or predatory. The institutional focus of the bond bank will provide technical resources to support improvements to local government financial management. as is discussed below.

- *Financial sustainability*
  This relates to the ability of the bond bank to maintain its capital base and, to the degree necessary, to earn a sufficient return of it. That should be a product of its properly charging for risk, its diversification, and the depth of its reserves.[11] Dividend policies, for example must be such as required to build up reserves. This militates against an initial "profit motive" in the operation of the bond bank. [12]

- *Facilitates high credit rating*
  This question runs to two levels: rating of the bond bank, and ratings of the cities and communal enterprises that it lends to. First, at the level of the bond bank itself, the credit rating will be determined by the bank's capital structure, its portfolio and other characteristics of its organization and operation. In the domestic Ukrainian market, the bank's credit rating should be as close to the sovereign ceiling as possible in the absence of a sovereign guaranty. At the local government and communal enterprise level, the bond bank will need to have its own "credit scoring" system to assess loans and bonds. This will attach internal scores (or ratings) to borrowers. That system of internal reporting and scoring

[11] An initial problem is lack of diversification in the early years of operation. Risk assessments rely on some experience and on probability distributions of "events" occurring for given periods. In the first few loans there is necessarily high-concentration. In the beginning, reserves (or recourse to added capital) must be at higher levels.

[12] INCA has been able to pay out competitive dividend rates to its equity holders. It is a special case however in that it bought out institutional portfolios of already existing South African municipal bonds. The banks and insurers were anxious to unload the bonds, which lost their ratings when the sovereign guaranty was withdrawn were believed to be too difficult to monitor. By creating INCA and selling off the bonds (and buying the INCA bonds), the South African financial institutions were able to "swap" un-rated bonds for the more secure ones represented by INCA. This process was helped because INCA has been the recipient of helpful donor-based capital injections.

will prepare borrowers to report information that will meet requirements of the private capital markets.

- *Promotes positive perception of local government credits by capital markets*
  The bond bank, by bundling and overseeing local credits, to some degree obviates the need of the financial market participants themselves to obtain that information from the underlying governments. However, the successful operation of the bond bank will no doubt enhance the reputation of local governments in the markets. As the credit markets deepen and governments mature, there is the likelihood that larger municipal borrowers may elect to enter the financial market directly.[13] This depends on the policies of the bond bank and the success of its operation.

- *Improves access to capital (core capital and lendable funds)*
  The bond bank, for a variety of reasons, will improve access to capital. That is an essential part of its rationale. Attracting loan capital is the more important consideration since bond banks typically rely on high leverage to be successful. A commercially-oriented ownership and governance structure that understands and protects the quality of the bank's underlying assets (loans to cities and communal service enterprises) will best serve this purpose.

Possible Weaknesses of Various Ownership and Control Structures

- *Creates obstacles to efficient management*
  Public ownership always raises the issue of efficient and objective operation as opposed to politically motivated, self-serving and subjective activity. In other words, loans may be lent on weak projects at favorable rates, staff may be too large, and facilities may be extravagant. Although these problems can also occur in private sector operations, they are mitigated by the imperatives to make profit and earn a market-competitive return on capital. More fundamental than ownership structure in either case are the integrity and independence of bond bank management, and the transparency and accountability of its operations. Above all, the ownership structure must provide strong incentives for efficient management. Standard tools in corporate management are independent external audits that are publicly released, public reporting of audited accounts, and boards of directors that are independent of day-to-day management and effectively oversee it. Another approach is to hire a private-sector asset manager that reports to the bond bank's governing board. Last, and very important, is the fact that the bond bank will itself be entering and reporting to the private capital market. Its securities will be rated and scrutinized by prospective bondholders.

- *May inhibit bond bank's access to capital (core capital or lendable funds)*
  A weakness of state government control is that some private investors (such as IFC) will not invest in state government-controlled entities. (IFC will consider

[13] Eligibility to borrow through the bond bank (by size or type of governmental or communal enterprise unit, purpose of loan, size of loan) will be a design issue. At inception, it appears best to apply a broad net and apply strict credit quality standards that all deals that are financially viable can be considered for inclusion. Individual loan terms may be tailored to reflect variations in risk and size and, therefore, promote wider use of the bond bank.

investing in municipal finance facilities that include both state and city ownership, as well as private ownership, so long as the facility operates on a commercial basis.)

- *Increases city/utility costs of borrowing*
  A weakness of private sector ownership is that the bond bank must satisfy private sector targets for return on equity invested. In an unsubsidized bond bank, these higher costs will be passed on to borrowers as higher spreads over the bank's cost of funds. The weakness may be less significant when the private investors have a public purpose orientation (like IFC, EBRD, or Dexia) and when the investors' own cost of funds is low, as with AAA-rated international finance institutions.

- *Creates regulatory problems or uncertainty*
  The exact legal structure of the bond bank is beyond the scope of this report. The type of ownership of the bond bank itself, if properly constituted, should not create regulatory problems or uncertainties. It is presumed that it will have appropriate legal powers to conduct its business. However, the legal nature of its ownership may pose important issues as regards the regulatory and tax treatment of its own securities and its interest earnings. For example, will it be deemed as a not-for-profit entity, and be able to use tax-free interest income from loans to pay interest on its own debt? What will be the requirements for registering and selling its own securities? How will its own securities be treated for purposes of legal investment by banks (capital adequacy requirements) and other institutional investors (prudential portfolio restrictions and requirements). It can be presumed these issues can be solved by appropriate clarifying legislation and regulation. However, that may be more difficult where there is a private sector involvement in the ownership that necessitates the payment of dividend or other returns on private investment.

Possible Opportunities Related to Ownership Structures

- *Increasing leverage of capital over time*
  A bond bank must have the capacity to borrow by issuing its own securities in the financial markets. The term "bank" infers that it has the capacity to create liabilities for purposes of acquiring assets, so long as it meets certain prudential and liquidity requirements. In private sector operations, this is essentially the requirement that after adjusting for the quality of its earning assets, it must hold a certain level of equity or subordinated debt and reserves. Government operations, backed by various governmental powers, often have less stringent requirements, although liquidity and financial condition of the sponsoring/parent government can be of concern.

  Leveraging refers to the ability to reduce the share of paid-in equity in the capital structure in relationship to borrowed funds. A non-leveraged bank essentially lends only up to the amount of equity and contributed capital (such as government appropriations or donor grants and loans). Leveraging means that the entity borrows funds and then lends those funds to grow its asset base. As a bond bank grows, it is likely to see its leverage increase if it does not make claims on its reserves to cover bad loans and expenses. For the bond bank the most meaningful measure of leverage will be the volume of its lending in relationship to reserves, equity, and subordinated debt. Many credit programs begin with low levels of leverage. A capital grant or donor loan may simply be on-lent. Leveraging in the domestic credit market increases as experience is gained and/or effective demand for loans picks up. The degree of acceptable leverage depends on the credit quality of the assets (the underlying loans made), the presence of adequate reserves, and the bond bank's ability to match cash flows between its assets and liabilities.

- *Attraction of new capital by the Bond Bank*

  The ownership of the bond bank can influence its ability to raise new capital. In the absence of a sovereign guaranty, donor organizations, at least initially, have been reluctant to provide loans directly to local governments. This policy has been changing in the last few years, but still follows the general principal that until experience is gained, there is reluctance to deal directly with the local governments on the basis of their own credit standing. There are significant exceptions. The EBRD will enter into direct loans to local governmental bodies and enterprises if it is satisfied as to creditworthiness and the enforceability of contracts. The IFC division of the World Bank will enter into loans (and equity) with private institutions dealing with local governments. USAID's Development Credit Authority is restricted to dealing only with private institutions, but can assist subnational governments through them. It is important to recognize that in all the above cases, it is the *financial soundness and integrity of the underlying projects and the borrowing governments* that condition their participation. An ownership and governance structure that assures these donor organizations of the credibility and creditworthiness of the bond bank's operations will increase access to capital, and access to terms that make long-term investments possible.

- *Creativity and financial innovation*

  The ownership structure is not directly relevant to creativity and innovation except as it may have bearing on the management and "culture" of the bond bank's operation. To the extent that qualified individuals and efficient procedures are believed to be inconsistent with government ownership and operation, then the services of technically qualified and innovative personnel may be secured through personal contracts or the hiring of an "asset manager" firm from the private sector. In such a case, the bond bank's governing body (whatever its capital structure) will have policy and operations oversight, and the technical work can be carried out by the contracted party. While this relieves the Board of managing and staffing day-to-day operations, it does require writing appropriate contracts and effectively overseeing them. When contracting for asset management, it is imperative that the board have access to its own experts independent of the contract. Contracts must be negotiated professionally.[14]

- *Maintain lean organization by contracting for services*

[14] Contracting out raises several other issues such as the tenure of a contract and how often to bid it out.

One difficulty in a free-standing, self-contained bond bank structure is that the volume of loans may not justify the employment of the skilled persons needed to evaluate and process loan transactions and to handle the bond bank's own interface with the private credit markets. Bond banks in the United States, Canada and Scandinavia tend to be small, specialized organizations that have a few highly skilled staff and contract out for many services. (The bond bank may also handle a number of credit programs, so as to maximize efficiency)[15] A great advantage of a lean bond bank organization is reducing administrative costs (while paying competitive compensation) and building a results-oriented culture. This means keeping the size of the organization small by outsourcing many skilled activities. This outsourcing of activity also helps "seed" the private sector with skills that will help broaden the market for local government securities.

- *Develop expertise in specialized credit evaluation of cities and utilities*
  As has been noted, the bond bank must have its own internal credit evaluation system (credit rating or scoring) in order to achieve an objective basis for making loans and deciding on loan terms and conditions. Typically, the bank will require borrowers of a minimum credit quality, below which the bank will require contributions to its own reserves and make requirements on borrowers to mitigate risks.[16] As a creditor, the bond bank requires continuously updated information about borrower finances, conducts ongoing oversight, and has a creditor's rights to require remedies that will cure or, preferably, prevent default. One of the major strengths of the bond bank is its on-going familiarity with local government and company finance. The ownership structure that is strongest on this score is likely to be mixed, comprising both national and local governments, and, if possible, private sector lenders.

- *Provide focal point for identifying and acting on obstacles to or opportunities for city and city enterprise borrowing*
  One of the most useful attributes of the bond bank is to act as a focal point for collecting and assessing information about how local governments and communal service enterprises finance their operations, and about their borrowing capacity. This is for three reasons: first, as a creditor, it has a business interest in national and local developments that affect its portfolio of loans and the market for its own securities. Second, it has both focus on and expertise in the local government sector. Third, as an institution with national coverage, it has knowledge of and access to a large number and variety of local governments and enterprises.
  Aside from these positive attributes, which are independent of its ownership structure *per se*, it is possible that the ability of the bond bank to express opinions and disseminate information and its viewpoints may be inhibited

[15] The Bond Bank in the U.S. state of Virginia, the Virginia Resources Authority, has a staff of five professionals that handles the bond bank's loan programs (there are three), as well as that state's State Revolving Loan Program (environmental projects) and a couple of smaller loan programs. Maryland's smaller bond bank program has two staff persons and hires outside legal counsel and relies in part on the local commercial banks to administer its loans.

[16] These requirements are written into the loan agreements with the underlying local borrowers. For example, a local borrower may be prohibited from taking additional loans without the Bond Banks' prior permission or may do so only if they are subordinated to the Banks obligations. Likewise, disposal or sale of collateral may be prohibited, as may be minimum balances in the debt service fund, and so forth.

if it is a government line agency or under government ownership without a clear mandate to act (and speak) with independence.

- *Aggressively monitor borrowers and help resolve borrower financial problems*
  The bond bank is a creditor, and under most configurations will rely on capital market acceptance of its portfolio of assets, the underlying city and communal enterprise loans. Simply as a matter of financial survival, the bond bank will need to have good security on its loans and act to protect that security. There must be ongoing monitoring of borrowers' finances and financial operations. Monitoring will trigger enforcement of security provisions in loan contracts. The bond bank will need to take steps to gain as much assurance as possible of the viability of activities funded and its ability to access funds needed for debt repayment. The fruits of this will be improved local government financial management and financial reporting practices. A bond bank ownership structure that promotes on-going internal and external monitoring of operations is best. Exposure of the bond bank to market investor scrutiny is the best way to accomplish this objective.

Possible Threats Related to Ownership Structures

- *Avoiding Corruption*
  Corruption can invade all forms of ownership structures, but the question, is, which ownership structures resist corruption? Corruption is ultimately a societal issue that legal and ownership structures can make more or less likely, but it is either endemic to a political and financial system, or it is not. Corruption is acknowledged to be a major problem in Ukraine, which ranks low on the corruption perception index worldwide. Fundamental tactics to combat bond bank corruption include making the dealings of the entity as transparent and accountable as possible. These tactics will of course be directed by the bank's owners, and their effectiveness can be enhanced by designing the ownership structure to be corruption-resistant. An ownership structure that comprises multiple owners from different organizations and different sectors can induce owners to exercise oversight on one another. Private, international investors would bring extremely valuable discipline and oversight to the governance of a Ukrainian bond bank. Independent and qualified "public" governing board members who do not represent a particular ownership stake can also be considered.

  The fact that the bond bank will issue securities held by institutional investors is also an important deterrent to corruption. Bondholders invested in the bond bank's securities will be outside parties who depend on honest and efficient operation of the bank. Standard reporting processes and independent audits will help guard against corrupt behavior, and the lack of a sovereign guaranty should reinforce those requirements. If the bank eventually achieves sufficient sophistication to tap longer-maturity debt in the Eurobond market, it will have to meet international disclosure and credit rating norms.

  Competitive wages for bank employees and independence of operation will combat corruption, but at the end of the day, avoidance of corrupt behavior will depend on the culture of the bond bank and the character of its employees. However, there is no *a priori* reason to believe that corruption is more or less likely as a result of the ownership structure, since both private sector and public sector employees are equally liable to seduction.

- *Systemic investment risks (tariffs set by local radas; all cities rely heavily on Inter-governmental transfers)*

  An inherent problem in securing communal enterprise debt is that tariff policy is subject to local political decision, making it difficult for enterprises to react quickly to changes in their costs. A systemic risk for cities is that most local revenue sources are effectively beyond the control of the local government and local governments are heavily reliant on shared revenues and grants from the central government that are beyond their control. The danger is that changes at the national level will affect all local governments at the same time, causing a systemic risk that defies effective diversification. There can be some protections against this, the major one being to limit the proportion of transfers that can be pledged to debt service. In many counties (including the United States) transfer payments or a limited share of transfer payments that can be pledged to debt service is limited to 20 per cent or so of the total payments.[17]

- *Politicization of lending decisions*

  There may be a higher risk of politicizing lending decisions and terms where there is controlling government interest in the bond bank. This has not been the case on the United States, Canada or Western Europe, in large part because of the transparency of the institutions and the fact that subnational governments borrow in well-developed private capital markets.[18] Government institutions elsewhere that do not borrow in the private markets and are not accountable to them have succumbed to the "political imperative."[19] Private-sector involvement as an equity holder or asset manager will help insulate bond bank decisions from politics, but this is by no means assured. Involvement of an international financial institution can bolster the independence of the bond bank operation to avoid undue pressure. A foreign institution could participate as a partial owner of the bond bank, or as an asset manager, perhaps in co-operation with a Ukrainian bank. The risk of politicization may be reduced where different levels of government represented on bond bank governance have different perspectives on local borrowing. For example, the Ministry of Finance has a

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[17] In the Philippines, no more than 20 percent of shared taxes in the form of transfer payments can be devoted to debt service. In the United States this is often expressed as a coverage ratio, which the number of times that debt service is covered by pledged revenues. A "five-times" requirement is fairly standard. The longer that a shared revenue/ grant program goes without major modification, the more it is accepted as a dependable source of revenues, as the coverage factor may be lowered. State payments to school districts have a long history of no severe cutbacks, which makes them very highly rated backing for local school bonds.

[18] Especially in the United States and Canada (and increasingly in Europe), the need to raise capital in the private markets and the role of the rating agencies has been critical to the transparency of the process, accountability, and lack of scandal in the markets. The threat of downgrading and the loss of a rating can be financial (and political) disasters. The privately owned rating agencies, meanwhile, have retained autonomy and credibility. Subnational governments are forced to face a hard budget constraint because of the rating system and their need to borrow in the private capital markets.

[19] This is a problem noted by international donor organizations that have supported on-lending operations that have not encouraged either private-market access or hard budget constraints. See Petersen (2005A)

strong interest in ensuring that local borrowing and guarantees are carefully controlled, while cities could be expected to favor relatively more permissive controls.

- *Changes in GOU political and legal environment adverse to local government creditworthiness*

  A potentially important role of the bond bank is to act as a sentinel for possible changes in national or local laws and regulations that would either diminish communal enterprise or city creditworthiness, or erode the quality of the bank's own obligations. So long as the bond bank is itself borrowing in the markets, it must abide by its debt contracts with investors. And so long as its own ability to live up to its own debt contracts is dependent on the quality of the underlying loans in its own portfolio, then it must be mindful of the quality of the underlying credits. This perspective will be reinforced by the lack of a sovereign guaranty and, also, by independence from dominant ownership by any single governmental level.

- *Reliance on market interest rates and maturities may make loans unaffordable*

  A risk for any institution that enters the domestic markets is that there may be times and circumstances that will make the loans it extends unaffordable to its market, in this case cities and their enterprises. This risk is largely unavoidable and has to do with the volatility of the domestic markets as opposed to any particular ownership structure. Although a state-controlled bank might have better access to subsidies to restore affordability and maintain its lending activity, the remedy is likely to be short-lived. High interest rates and unreceptive markets are a signal to shut down further growth in credit. This is applicable to both private and public lending. A bond bank per se cannot assure that markets will be accommodative or interest rates low. However, bond banks, because of their scale and sophistication, typically do have more options available to weather the storm and to sell debt instruments that can accommodate higher interest rate environments.

Summary Findings & Conclusions Regarding Bond Bank Ownership Structure in Ukraine

The above SWOT analysis has provided a detailed discussion of the various factors that enter into decisions regarding the ownership structure of a bond bank.

Following is a summation of these SWOT findings on what should be the general operating policies, powers and ownership structure of a Ukrainian bond bank:

- A key role for bond bank owners will be to invest sufficient core capital to enable the bank to build capital market confidence and borrow efficiently in its early years, while building a sound track record of prudent lending to cities and communal enterprises. It should increase leverage of equity over time.

- The bond bank's own creditworthiness and its transparent, objective lending criteria will be *critical*. The more creditworthy the underlying cities and utilities to which it lends, the more successful the bond bank can be in raising long-term funds at lower cost.

- The bond bank will be a focal point for local government financial expertise and for promoting reform in communal enterprise and city finance.

- A reserve or indemnity fund can protect investors who buy the bank's bonds. If the bond bank is properly and credibly designed and is itself creditworthy, then donor organizations can be counted upon to help fund such reserves.

- The bond bank structure must promote professional management, transparent operations, and its operation must be insulated from political pressure at both the national (state) and subnational (city) levels.

- The bond bank could be structured, if possible, to enable city governments and communal enterprises to make equity investments in the form of land holdings transferred to the bond bank.

- Special legislation would be highly desirable to establish the creation of the bond bank in order to clarify its public purpose, to establish the basis of its ownership, to provide it with appropriate corporate powers, and to create the required regulatory and tax treatments to facilitate its businesslike operation. Such legislation should be liberal in giving the bond bank powers to evolve over time as the Ukrainian governmental and financial structure evolves.

Recommendations

The bond bank's primary mission will be to lend on a financially sustainable, businesslike basis to communal service enterprises and cities for infrastructure. It would borrow in its own name in the capital markets without a sovereign guarantee.

1. These bond bank objectives can best be achieved with a mixed ownership model, with a balance of ownership shares distributed among 1) the state (national) government; 2) city governments and communal service enterprises that choose to invest in the bank; and 3) one or more private entities, most probably international finance institutions or European commercial banks with municipal finance expertise. A desirable ownership structure would be roughly one-third ownership: each by the state, by cities and communal enterprises, and by private banks/international finance institutions. This balance would incorporate state support and financial strength; city and communal enterprises, the bank's customer base; and private sector business discipline. Multiple owners from these three different sectors will create a counter-balance of different interests in bank governance. Checks and balances in governing authority will promote competent operation, transparency, and independence from political influence.

2. The bond bank will likely fall under the regulatory jurisdiction of the State Commission for Financial Services Markets Regulation. Appropriate regulations should be formulated as needed to accommodate its mission.

3. The bond bank should be designed to allow the contractual utilization of a private-sector asset manager.[20] Strong consideration should be given to using commercial banks as loan originators and loan servicers.

4. Bond banks usually have small staffs, and contract for legal services, loan servicing, and so forth. The design should reflect the need to hire a few very capable full-time staff to run its operations, market its services to local governments, and perform recurring loan administration services.

[20]An example of a contract oriented structure would parallel the mortgage bond structure now being developed by GOU with ATCI assistance

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ANNEX A: Legal Format and Ownership Structures of Local Funding Agencies

Name of Bond Bank of Local Gov. Funding Agency	Legal Format	Ownership Structure
Credit Communal de Belgium	Bank (Public limited company)	Cities
KommunKredit Denmark	Credit Association	Cities and counties
Bank Nederlandse Gemeenten Holland	Statutory two-tier company	50% central gov't 50% cities
Kommunalbanken Norway	Special law since 1999; has government guarantee	80% central gov't 20% KLP (mutual pension and life ins. company for local gov't)
Nederlandse Waterschapsbank Holland	Bank which can lend only to public sector clients, or to clients whose loans are guaranteed by a public entity	81% local water boards 17% central gov't 2% provinces
Japan Finance Corp. for Municipal Enterprises	Government financial institution, has gov't guarantee	Government of Japan
Municipal Finance Authority of British Columbia Canada	Special law-"corporation without share capital;" independent organization operates like credit union; has power to tax property anywhere in the province	Governed by all regional districts of province; board members have votes proportional to district population. Regional districts have joint and several liability for each other's borrowings.
Kommuninvest Sweden	Joint stock company	Cities and counties own Kommunivest via a cooperative society; cities have "joint and several obligation" to pay loans.
Credit Local de France*	Specialized financial institution	8% Central gov't 12% Caisse des depots* 80% Private shareholders (*state-owned financial institution)
Municipality Finance PLC Finland	PLC; shareholding restricted to public entities; debts are guaranteed by state-created Municipal Guarantee Board	57.5% Cities and Ass'n of Local and Regional Authorities 42.5% Local Gov't Pension Fund Institute

*/ Replaced by the formation and privatization of Dexia in 1996.

Dexia- Europe	Bank focusing on municipal finance in several countries	Formed from Former state-owned systems. Private shareholders (including Caisse de Depot and some cities in Belgium)
Inca-South Africa	Special Purpose Vehicle	Private shareholders, as follows: 2% Chanson Investment 4.42% Dexia 17.68% FirstRand Bank Ltd. 4.95% INCA Share Inventive Trust 43.96% Kagiso Financial Svcs Ltd 26.98% Momentum Group
Tamil Nadu (India) Urban Development Fund	Trust created under India Trust Act of 1882	51% Tamil Nadu State Gov't 49% three private investors (asset managers)
Bond Banks in United States	Most US bond banks are independent authorities created by special state laws; some provide for state guarantee; some are part of a state agency or commission with other responsibilities.	Most are state-owned, and self-supporting with revenues from operations; and usually independent of state government
Local Government Unit Guaranty Corporation-Philippines	Private financial services corporation organized under Trust Act; does not lend, but guarantees municipal loans. USAID DCA program reinsures the company.	51% Association of Philippine Banks 49% public and private investors (including 25% ($1.3 million) from Asian Development Bank)

Sources: Bank websites; Moody's Investor Service reports; SEK Advisory Services/EBRD *Assessment of Transferability of Local Government Funding Agency Concepts to Ukraine and Romania,* 2005. John E. Petersen, *Analysis of State Bond Banks*. 1997. Table Provided by Richard Genz, March 15, 2005

ANNEX B: Illustrative Equity Gearing Ratios

Ownership and control of a corporation is usually evidenced by "equity," which is the residual interest in its assets and income after liabilities and the interest due on them have been accounted for. In a profit-making activity, increasing the value of equity and the income derived form it are the motivating factors in ownership. In governmental and non-profit activities, the "equity" interest has a public-purpose rationale. Control of management and policy decisions are associated with equity ownership. But, the nature of the organization, as well as limitations placed on the ownership by creditors, can limit the discretion of the equity owners. By the same token, the equity interests may be divided among various parties and itself by subject to limitations. Generally, majority ownership vested in a particular class of stock will determine operational and policy control. Thus, the majority owner will have control, but this control may itself be limited, depending on the details of the articles of incorporation.

Bond Banks can have several ownership structures (corporate forms). These can have a bearing on the significance of the equity component, which is typically a minor fraction of the overall capital raised. Below are illustrated some capital structures of bond-bank type organizations. The degrees of leverage (debt in proportion to equity) are illustrated.

Examples of "Bond-Bank-Type" Capital Structures and Leverage

INCA (effective gearing 22.8 to 1)
3,400 R assets
3,200 R. market debt
60 R. subordinated debt
140 R. equity and retained earnings

LGUGC (effective gearing: 6.3 to 1)
1,900 million Peso outstanding insured debt (contingent liability)
300 million P. paid in capital and retained earnings
250 million P. subscribed uncalled

Alberta Capital Finance Authority (effective gearing: 25.66 to 1)
4.00 billion C$ assets
3.85 billion C$ debt
0.15 billion C$ in equity and retained earnings

Tamil Nadu Fund (effective gearing: 3.7 to 1)
3500 Crore Rps. assets
2750 C. Rps debt (including World Bank loan)
750 C. Rps. in equity

Source: Kehew, Matsukawa, Petersen 2005

As may be seen, the leverage varies dramatically. Where there is a direct or de facto sovereign guaranty, there is high leverage (Alberta) where the underlying creditworthiness of the sovereign is very high quality. INCA, a private corporation, carries a high leverage, which is geared to the quality of underlying assets (it carries no sovereign guaranty). The developing country funds (India and Philippines) carry lower leverage ratios. The leverage will depend on the quality of the underlying loans and what reserves can be assembled to support the Bond Bank's debt.

Annex C: *Assessment of GOU Actions and Decisions Required to Establish Bond Bank*

(Prepared by the Access to Credit Initiative/USAID-Ukraine)

1. ESSENTIAL ACTIONS FOR IMMEDIATE STARTUP

A. Develop Consensus on Bond Bank Strategy

The Ministry of Construction, Architecture and Housing and Communal Economy, the Ministry of Finance, the Ministry of the Economy, and the Association of Ukrainian Cities will comprise the core group of key stakeholders in bond bank formation. With leadership of the Minister of Construction, this core group should agree on a broad action plan for bond bank development, beginning with agreement on an ownership structure as recommended in the John Petersen SWOT report.

B. Develop Business Plan

A detailed business plan should be prepared that addresses bond bank capitalization, financial management, lending and loan monitoring operations, marketing, staffing, contracting for services. The Access to Credit Initiative/USAID-Ukraine is available to provide technical assistance to the GOU in developing its business plan.

C. Evaluate Options for Immediate Formation of the Bond Bank Under Current Law

Because of the unique nature of the bond bank, special legislation and regulation should be the goal. However, it will be possible for the bank to begin operations on an interim basis under current law. A legal evaluation of the options should be undertaken as soon as the GOU makes a political decision to proceed with establishing the bank.

With the recommended mixed state/city/private ownership, it appears that the following interim legal structure for the bond bank might be appropriate:

Legal Status Under the Civil Code:	Legal Entity
Legal Status Under the Financial Services Law:	Financial Institution
Organized Under:	Company Law (Law on Business Associations) as Joint-Stock or Limited Liability Company
Founded by:	Decision of founders meeting (equity investors)
Regulated by:	State Commission on Financial Services Markets Regulation

D. Amend 2006 Law on Budget to Raise GOU Capital Stake in Bond Bank

Amend the 2006 State Budget Law, Line 54, and the related Cabinet of Ministers Resolution, and use a portion of the UAH 1 billion that is now earmarked for modernization of infrastructure as GOU equity investment in the bond bank.

E. Seek Equity Participation by International Finance Institutions, and Commercial Banks Specializing in Municipal Finance

Based on the interim legal structure agreed upon by the core group of stakeholders, and after securing firm investment commitments from the GOU and cities, the next step will be to secure additional equity investments or lines of credit from international finance institutions and commercial banks. Candidates include IFC, EBRD, Dexia, and Raiffeissen.

2. NECESSARY STEPS FOR OPERATIONAL SUCCESS

A. Enact Special Legislation for the Bond Bank

Lending exclusively to communal service enterprises and cities entails special and unique risks. There is no other financial institution in Ukraine that lends exclusively to communal service enterprises and cities, as the bond bank will do. The bond bank must be astutely regulated if it is to maintain the confidence of capital markets and accomplish its infrastructure finance mission in decades to come. Although the bank can start operation immediately under existing law, this should be considered an interim solution. Effective bond bank operations should be enhanced and protected by a legal and regulatory framework that fits the specific operational demands and risks of a prudently managed municipal finance facility.

Special legislation should be enacted to define the powers and fundamental operating principles of a bond bank, including: preservation of capital; earning market returns on capital; strong and transparent creditworthiness standards; financial sustainability; annual external audit; full operational independence; and authority to contract for services.

The State Commission for Financial Services Markets Regulation should enact special supervisory regulations for the bond bank in accordance with the special legislation, and taking account of the bond bank's unique business.

B. Enact the Law on Local Borrowings and Guarantees

The Ministry of Finance has formally asked for comment on the draft Law on Local Borrowings and Guarantees. Comments are due by April 6, 2006, and the draft law will probably be introduced into the Verhovna Rada in May 2006.

The law should promote and simplify responsible use of municipal guarantees for city-owned communal service enterprises. The current draft makes it doubtful whether such guarantees could practically be made.

The annual Law on State Budget should not prohibit cities from guaranteeing debts of creditworthy communal enterprises.

The law should provide GOU assurance to creditors that an approved local borrowing is valid under Ukrainian law for the full term of the borrowing. The enforceability of local loans and guarantees should be incontestable after the GOU has approved them.

There should be no pre-election bans on local borrowing, such as the current draft law's 12-month ban on local borrowing before any local election. A lending ban would require a bond bank to suspend operations. (Super-majorities to approve local borrowing in pre-election periods may be desirable.)

Provisions in the draft law that obligate local governments to repay debt and that give repayment of local borrowings legal priority over other expenditures should be retained.

Provisions removing the Ministry of Finance from evaluating creditworthiness should be retained.

A borrowing application should be deemed approved in the event that the Ministry of Finance fails to respond to an application within 10 days.

C. Change Legal and Regulatory Framework to Promote Creditworthiness of Communal Service Enterprises

To promote creditworthiness of communal service enterprises, implement full cost-recovery tariffs that automatically adjust for operating cost changes. GOU should allocate funding to pay debts incurred by state-owned enterprises to communal enterprises. Develop a mechanism to facilitate enforcement of the Law on Communal Services (2004) that requires cities to compensate communal enterprises for the difference between approved tariffs and full-cost recovery tariffs. GOU should initiate introduction of annual, external audit reviews of communal service enterprises.

D. Change Legal and Regulatory Framework to Promote Creditworthiness of Cities

To promote creditworthiness of cities, modify city revenue structure so as to increase the share of city revenue that can be modified by local radas. Stabilize the proportions of shared taxes. Restore the Budget Code's incentives for cities to promote economic development, increase local tax revenues, and retain the revenue increases generated by economic growth. Make equalization transfer grant formulas transparent. Suspend the State Treasury's practice of making medium-term loans to cities. Allow cities to maintain debt service reserve accounts in commercial banks. Institute transparent financial reporting standards and regular external audits for cities.

KEY FINANCIAL RISK FACTORS FOR UKRAINE'S CITIES

Francis Conway
The Urban Institute
February 2006

Scope of the Analysis

This analysis considers the financial risks of cities in the Ukraine. Along with the State, they are the only bodies of government authorized to borrow by the Budget Code. The report does not look specifically at risks affecting other local self-governments nor oblasts or rayons that are not authorized to borrow.

Credit risk analysis seeks to identify financial and other factors that could affect adversely the ability of a borrower to repay its debt obligations fully and in a timely manner. It also considers the ability of the borrower to limit or mitigate that risk over time.

This reports looks at systemic or structural aspects of the finances of cities that may impair the ability of the city itself and of external analysts to identify credit risks. It also looks at factors that may constrain the ability of cities to mitigate or limit that risk over time. This includes:

- The system of financial reporting and accounting
- The local budget process and structure
- Local revenue and expenditure authority

The report concludes with a review of the current ATCI credit risk methodology in light of the risks that cities face in the management of their finances and makes recommendations for possible adjustments to that methodology.

The System of Financial Reporting and Accounting

Disclosure – ideally based on clear rules consistently applied – is a key factor in credit risk analysis. The financial statements prepared and issued by the potential borrower are the primary source of information for any credit risk analysis. When looking at those statements it is vitally important to understand the underlying system of financial reporting and accounting – what it measures, when assets and liabilities are recognized and recorded, the rules on the content and presentation of the statements. The key issue is whether the financial statements provide a comprehensive picture of the finances of the reporting entity that shows all its assets and all its obligations. When it appears that not all assets and/or obligations are reflected in the financial statements, or if supporting information is not available through notes to the financial statements, disclosure is incomplete. This of and by itself adds an element of risk.

Cities in the Ukraine must deposit all their funds and keep all their accounts in a unified national treasury. The State Treasury handles all their receipts and payments. Ti also prepares and issues the financial statements for the cities. It was not possible during the short trip to establish clearly either the measurement focus or the basis of accounting used in the public sector in Ukraine. Information provided by the former director of local budgets in the Ministry of Finance suggests that transactions are recognized when actual funds are received or paid, that is, on a cash basis. There is a uniform chart of accounts for all the public sector, including cities. The State Treasury records a commitment against the city budget when the city issues a contract or purchase order. By comparing outstanding commitments with payments, the State Treasury can estimate payables at the end of the year (a feature not normally available in cash accounting).

The focus of financial reporting is on legal and budgetary compliance. By law and regulation, each city must issue the following financial reports:

1. Report on financial state (balance) (a summary of accounts balances)
2. Report on local budget execution (based on budget classification – social protection, education, communal economy, etc.)
3. Report on local budget execution results (based on economic classification – operating revenues, operating expenditures)
4. Cash flow report
5. Budget indebtedness report (accounts receivable/payable)
6. Special fund revenues and expenditures report as regards own revenues of budget institutions financed by the local budget;
7. Information on execution of protected expenditures of local budgets;
8. Information on reserve fund utilization
9. Information on changes in goods and foodstuffs of budget institutions financed by the local budget;
10. Report on changes in fixed assets of budget institutions financed by the local budget;
11. Report on lack of and pilferage of cash and valuables in budget institutions financed by the local budget;
12. Information on changes to the local budget general fund figures during the year;
13. Report on revenues and other receipts (international donor assistance) of the special fund;
14. Report on receipt and utilization by local budgets of the State Budget grants and subventions;
15. Explanatory note to the annual report

The Budget Code requires that the budget include all city revenues and other sources of financing and all city expenditures. There are no off-budget funds. The information in the reports is consolidated accordingly. This is a positive feature of the system of financial reporting in the Ukraine.

The Treasury issues the reports monthly, quarterly and annually. The reports are designed for internal users. There are no notes to the financial statements that normally would inform external users of key facts and information underlying the figures in the various reports. This limits the value of the financial statements. It is a practice common to all transition countries where the very notion that someone outside the public authorities would want to read and understand the reports was inconceivable.

A specialized office in the Ministry of Finance conducts a limited audit of these financial reports. These audits generally look at some specific aspect of local finances and do not cover the entire scope of those finances. There are no other independent external audits of city financial reports.

ATCI financial analysts that have been conducting the credit risk assessment of target cities indicate that in reality not all of the reports listed above are available from the cities and not for all years. They face considerable difficulties collecting the reports and other financial and economic information from cities.

The lack of notes to the financial statements to inform external users, the limited external audit review and the difficulty in obtaining all reports for all years adds up to limited disclosure of city finances. This is a risk that lenders or investors interested in Ukraine cities must accept.[i]

Cities maintain their own records but these are not kept together by one office in one place. Rather each "key spending unit" (as defined in the Budget Code) maintains its own revenue and expenditure records. The City Finance Department is but one of several such spending units that also include the various line departments (responsible for education, culture and so on).

There are indications that the records of the key spending units may not always reconcile fully with the information kept and reported by the State Treasury. The differences may represent 3 to 5 percent of aggregate figures. While not that significant, ***the fact that internal records of the city may not reconcile with those of the State Treasury adds to the risk of uncertain disclosure of city financial information***.

The Local Budget Process and Structure

Even the most solid local governments in any country can and do encounter circumstances that affect their finances adversely. What differentiates one local government from another is its ability to manage the problem. What differentiates the system of local government in one country from that in another is the extent to which the rules and procedures for managing local finances provide a reasonable basis for managing such problems. The first set of rules and procedures to consider are those on the local budget process and structure.

The Budget Code of the Ukraine defines the city budget process and structure. The Code establishes a process that allows city officials to plan, adopt, amend and execute their budget independently of other budgets. This is a positive aspect of the system of local finances in Ukraine – one that is not found commonly in other transition countries.

The Ministry of Finance provides information that cities need to prepare their budgets once at the beginning of the process and again after the Council of Ministers has adopted the draft State Budget. The second instance is particularly important. It includes "the estimated amount of intergovernmental transfers, the methodology for their definition, other amounts as necessary for development of draft local self-government budgets and other parameters needed for formulation of local budgets." (Article 75 (7)) This effectively allows cities in the Ukraine to develop their own budget on the basis of an estimate of all their revenues and other sources of financing. Further, city budgets are not subject to review by any external body prior to adoption. As noted above, the Budget Code requires that the budget include all revenues and other sources of financing and all expenditures. There are no off-budget funds. Together these features promote sound, independent budgeting by cities.

The Budget Code provides a clear classification of revenues, other sources of financing and expenditures that simplifies the task of calculating the operating (or current) balance in city finances separate from the overall or total balance. This facilitates the credit risk assessment by identifying the recurring funds that might be available to service debt.

The Budget Code divides the city budget (and all budgets) in "general" and "special" budget funds. The special budget fund includes all earmarked or special purpose revenues, related expenditures and any fund balances. The general fund includes all other revenues and related expenditures. By authorization of the City Council it is possible to transfer resources from the general to the special budget fund. In 2004, actual end-of-year expenditures of the general budget fund accounted for 82 percent of aggregate local expenditures. The special budget fund accounted for the remaining 18 percent.[ii]

The Budget Code also establishes a Local Development Fund that includes all earmarked capital revenues and other sources of financing for capital expenditures. These include proceeds from the sale of assets and dividends on investments. They also include all the proceeds from any bond or loan. The revenues and expenditures of the Development Fund are recorded and reported as part of the special budget fund.

The prevailing interpretation of the Budget Code is that it requires that any repayment of principal on a bond or loan be made from resources available to the Development Fund. Interest payments are made from resources available in the general budget fund.

Finally, of interest to this report, the Budget Code also provides for certain "protected items" in the budget that may not be sequestered.

The rules and procedures governing the budget process in Ukraine are a positive factor when considering credit risk of cities. The segregation of capital expenditures in the Development Fund, the provision dividing debt service between the general and special budget funds and the protected items all add rigidity to the local budget that could become a constraint in times of severe budget stress (more on this below).

Local Revenue and Expenditure Authority[iii]

Aside from those governing the budget process and structure, the other set of rules and procedures to consider when assessing the ability of local governments to manage problems that may arise in their finances are those regarding revenues and expenditures, that is, the ability of a local government to raise revenues and/or decrease expenditures if needed. In looking at this question the focus has to be on the general budget fund, as by definition the revenues and expenditures of the special budget fund are all earmarked or dedicated.

On the expenditure side of the general budget fund, there are two factors that limit the discretionary authority of cities to manage their finances. Protected items, as defined by the Budget Code, are one. These are types of expenditures that may not be sequestered in times of budget constraints. At present they include wages and related social insurance payments as well as certain items such as medicines. In 2004 in aggregate such items accounted for 79 percent of general budget fund expenditures.[iv] The second factor limiting the ability of cities to manage the expenditure side of the general budget fund is the fact that a large share of their responsibility is to implement State programs in areas such as education, health and social assistance. For all of 2004, these "delegated" expenditures accounted for 84 percent of general budget fund expenditures.[v] To the extent that service policy in these sectors is a central government function, it suggests that cities have limited discretion in managing a large share of the general budget fund.

If we consider these two limitations on the expenditure side of the general budget fund and the absolute constraints on all special fund expenditures, then local governments have limited discretion to manage roughly 87 percent of their total expenditures

(including both budget funds).[vi] Or, conversely, local governments in aggregate have full discretionary control over approximately 13 percent of their total expenditures.
The rigidity of local expenditures – be they "delegated" or "protected" – suggests that cities would find it difficult to adjust expenditures to meet debt service obligations if they found themselves in a situation of financial distress. In fact, the source of financial distress could easily be a change in central government policy affecting one or more of the "delegated" functions in health, education or social assistance.

There are even greater constraints on the revenue side of the general budget fund. Local governments are heavily reliant on shared taxes. Their share of the PIT and the tax on small businesses and entrepreneurs accounted for 75% of all general budget fund revenues in 2004. Conversely, local taxes and fees (those over which the local government has discretionary authority) represented 3% of total general budget fund revenues in the same period. They declined by 6% in nominal terms from 2003 to 2004. Local governments have virtually no ability to make adjustments on the revenue side of the general budget fund. In fact, as with their expenditures, a change in central government policy – in this case regarding one or more of the various shared taxes – could easily become the source of financial distress for cities.

The ATCI Credit Risk Assessment Methodology

ATCI has developed and applied a sound methodology for assessing the credit risk of cities in Ukraine. It focuses on the recurring or operating surplus (deficit) as the key variable when considering the debt service capacity of cities. It uses various financial indicators or ratios to identify specific characteristics of the structure or trends in revenues or expenditures that may signal current or future problems in the finances of the cities. The following recommendations are intended solely as a complement to the existing methodology. They are intended to reflect some of the systemic problems discussed in the preceding sections. They are not meant to suggest that the assessments prepared to date do not meet the needs of the program. ATCI staff already adopted several of the recommendations.

Obtain additional information to that provided in the financial reports on possible obligations or liabilities. ATCI should ask the city to provide full and current information on the following:

- Outstanding loans or other debt obligations of the city and the current and historical status of compliance with the terms of those obligations
- Arrears as reported by key spending units (for comparison with arrears as shown in the financial reports)
- Arrears of key locally owned enterprises and trends in those arrears
- Ongoing capital projects and their claim on future revenues
- Investments or ownership shares of the city in private or mixed capital enterprises
- Outstanding guarantees or other financial commitments of the city to any other institution or enterprise
- Fines assessed by other public authorities (such as for environmental issues) and not paid
- Pending litigation and its potential financial impact
- Other contingent liabilities

Develop and monitor indicators of "rigidity" on the expenditure side of the general budget fund. ATCI should review the extent to which a city is constrained in managing the expenditure side of its general budget fund using indicators such as the following (some already in use, others new):

- Expenditures for delegated functions as a percent of recurring revenues
- Percent change in expenditures for delegated functions over percent change in recurring revenues
- Protected items as a percent of recurring revenues
- Percent change in protected items over percent change in recurring revenues
- Percent change in city payroll over percent change in national wages
- Operating surplus as a percent of expenditures for delegated functions
- Operating surplus as a percent of protected items

The last two ratios are very important and should serve as a complement to the ration of operating surplus to recurring revenues. The threshold value of the ratios should reflect historical experience. What has been the largest one-year increase in real terms of aggregate delegated expenditures? What has been the largest one-year increase in real terms of expenditures for protected items? The ratio of the operating surplus to each type of expenditure should be some multiple – probably not less than twice – the rate of the corresponding one-year increase.

So, for example, if aggregate national delegated expenditures increased by up to 10 percent in one year, the operating surplus should be no less than 20 percent of total city delegated expenditures. This will provide a cushion against possible changes in central government policy regarding health, education or social assistance that may not be accompanied by a corresponding increase in transfers from the State budget. There is a precedent for this when Parliament ordered an across-the-board increase in public sector wages in 2004. Many cities faced immediate serious financial problems.

Identify potentially troublesome ratios or trends in advance of interviews with city officials as the basis for assessing a) the city's own understanding of its current financial condition and b) the willingness and ability of the city to address and resolve current or future causes of fiscal stress.

Aside from providing a quantitative assessment of the finances of a city, the indicators and ratios that are part of the ATCI credit assessment methodology provide an opportunity to develop an approximate qualitative assessment of the city's financial management capacity. After ATCI staff have completed the entry of data in the financial model and identified areas of potential problems, they should conduct an interview of key decision makers in the city regarding these problem areas. Are the officials aware of the problem? Do they have a reasonable explanation for the underlying causes of the problem? Are they taking steps to mitigate the risks?

The following is an example of how this might work:

> The analysis of the finances of city X shows that rate of change year-to-year in operating expenditures in city X is greater than the corresponding rate of change in its recurring revenues. A further look at the indicators shows that this has been driven in large measure by increases in the payroll of city X at a higher rate than the corresponding national average.

The interview with officials in city X would seek to find out more about these two trends. Is the change in payroll the result of having hired more people or having increased the wages of current staff? If the latter is the response, is this part of a plan to retain good staff? Or, has city X simply been adding staff for essentially political motives. Is the increase in operating expenditures part of a plan to improve city services? Or, is it driven, as with the payroll, by political motives? What steps is the city planning to take to bring the trend under control before it incurs an operating deficit?

Following such an interview, ATCI staff will be in a better position to interpret the straight-line projection of trends in key city indicators. They also will have the basis to assess the willingness and ability of city officials to manage their finances prudently going forward. If that assessment is not fully positive, they may want to compensate by reducing the estimate of debt carrying capacity.

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[i] There are precedents in other transition countries such as the Czech Republic for an *ad hoc* request by lenders or investors for a complete independent audit of a given city's finances. Normally this would be limited to a very large bond issue or loan, given the substantial cost of such an audit.

[ii] Data is from *Budget Monitoring: Analysis of Execution of Consolidated and theState2004 State Budget*, RTI, May 2005

[iii] All figures in this section of the report are from RTI 2005

[iv] Payroll 45%, Subsidies and current transfers 29%, Foodstuffs 3% and Medicines 2%

[v] Of these expenditures (less transfer and social protection payments to the population), 73 percent were for wages and related costs.

[vi] Calculated as share of general fund in total expenditures X share of delegated expenditures in the general budget fund plus share of special fund in total expenditures or

$$(.82 \times .84) + .18 = .87$$

WORKSHOP ON CREATING A MUNICIPAL FINANCE FACILITY FOR UKRAINE

The Workshop is co-sponsored by the Ministry of Finance; the Ministry of Construction, Architecture and Housing and Communal Economy; and the United States Agency for International Development/The Access to Credit Initiative

Date: Friday, January 27, 2006

Place: Academy of Science, Volodymyrska Street 55 (3rd floor), Kyiv

Attendees:

Senior leadership of the Government of Ukraine involved in policy decisions affecting local infrastructure financing and investment; city mayors and finance directors; Association of Ukrainian Cities; communal service enterprise executives; investment bankers; international donor agencies; potential investors.

Purpose:

The workshop will consider the creation of a new finance facility that specializes in making long-term infrastructure loans to cities and communal service enterprises. The institution would raise capital at market interest rates, and lend to creditworthy cities and utilities. Loan repayments would be pledged as collateral to the investors who provide capital to the institution. The institution's staff would become expert in evaluating the creditworthiness of cities and communal enterprises. At the workshop, nine experts from three continents including three former Chief Executive Officers of bond banks, will make presentations. They will describe infrastructure finance facilities that have operated successfully around the world. New research on the creditworthiness of Ukraine's cities and communal enterprises will provide context for evaluating international practice in infrastructure finance. Russia's ongoing effort to create a municipal finance facility will be described. To conclude, all experts will jointly discuss key issues for the proposed finance facility's business plan, including:

- Financial structure, including sources of core capital and lendable funds; credit enhancement
- Operating policies: standardized loan documents, credit evaluation, loan monitoring
- Enabling legislation and regulatory oversight.

Conference Chairman: *Dr. Vitaly Lisovenko, Deputy Minister, Ministry of Finance*

Agenda

Friday, January 27, 2006

8:30 – 9:00 **Registration**

9:00 - 9:20 Welcome and Introduction: *Dr. Vitaly Lisovenko; Earl Gast, Director USAID Regional Mission to Ukraine, Byelorussia & Moldova*

9:00 – 9:10 Dr. Vitaly Lisovenko, *Deputy Minister of Finance*

9:10 – 9:20 Earl Gast, *Director, USAID Regional Mission to Ukraine, Byelorussia & Moldova*

9:20 - 10:15 Introduction to Municipal Finance Institutions, and the Benefits They Offer to Transition Economies

Dr. John E. Petersen, Professor of Public Policy and Finance, George Mason University, USA

10:15 - 11:00 Municipal Finance Institutions in Western Europe: Structure, Operating Policies, and Track Records; Feasibility of Creating a Municipal Finance Facility for Ukraine

Nicholas Anderson, Senior Vice President, Swedish Export Credit Corporation
Lars Andersson, Coordinator for Regional and Local Authorities, Swedish Export Credit Corporation

11:00 - 11:15 **Convenience Break**

11:15 - 12:00 How to Succeed in the Business of Municipal Finance

Johan Kruger, Founder and Former CEO, Infrastructure Finance Corporation Ltd., South Africa:

12:00 - 13:00 Evaluating the Creditworthiness of Ukraine's Cities and Utilities

Part I. Ukrainian Intergovernmental Finance: Theory and Practice

Dr. Wayne Thirsk, Senior Advisor, The Access to Credit Initiative

Part II. Municipal Creditworthiness and Fiscal Decentralization: How does Ukraine Compare with Other East European Countries?

Francis Conway, Senior Associate, The Urban Institute, USA

13:00 - 14:00 **Lunch**

Friday, January 27, 2006, *continued*

14:00 - 14:45 Legal and Regulatory Issues to Consider in Establishing an Infrastructure Finance Facility; Assessment of Ukraine's Draft Law on Local Borrowing

Michael DeAngelis, Municipal Finance Legal Expert / The Access to Credit Initiative

14:45 - 15:30 Lessons Learned from Planning a Municipal Finance Institution for Russia

Dr. Sergey Sivaev, Institute for Urban Economics, Moscow

15:30 – 15:45 **Convenience Break**

15:45 – 16:15 Considering A Municipal Finance Institution for Ukraine: Strengths, Weaknesses, Opportunities, and Threats

Michael Curley, Director, Global Environmental & Technology Foundation, Washington
(The presentation is provided under financial support of the Office of International Affairs of United States Environmental Protection Agency)

16:15 - 17:15 **Panel Discussion**

Outlook for Creating a Municipal Finance Institution for Ukraine; Comments on the Proposed Recommendation to the Government of Ukraine

Moderator: John E. Petersen

Panel members: Dr. Vitaly Lisovenko; Pavlo Kachur, Minister of Construction, Architecture and Housing and Communal Economy; Nicholas Anderson, Lars Andersson, Johan Kruger, Francis Conway, Wayne Thirsk, Michael DeAngelis, Sergey Sivaev, Michael Curley

I. Options for Financial Structure
II. Operational Issues for an Infrastructure Finance Institution
III. Legal and Regulatory Issues for a Municipal Finance Institution

17:15 - 17:45 Discussion and Comment by Workshop Participants

17:45 - 18:00 **Closing Remarks**

Dr. Vitaly Lisovenko, *Ministry of Finance*; Pavlo Kachur, *Ministry of Construction, Architecture and Housing and Communal Economy*

18:00 – 19:30 **Reception**

ATTACHMENT 6

KEY FINANCIAL RISK FACTORS FOR UKRAINE'S CITIES

Francis Conway
The Urban Institute
February 2006

Scope of the Analysis

This analysis considers the financial risks of cities in the Ukraine. Along with the State, they are the only bodies of government authorized to borrow by the Budget Code. The report does not look specifically at risks affecting other local self-governments nor oblasts or rayons that are not authorized to borrow.

Credit risk analysis seeks to identify financial and other factors that could affect adversely the ability of a borrower to repay its debt obligations fully and in a timely manner. It also considers the ability of the borrower to limit or mitigate that risk over time.

This reports looks at systemic or structural aspects of the finances of cities that may impair the ability of the city itself and of external analysts to identify credit risks. It also looks at factors that may constrain the ability of cities to mitigate or limit that risk over time. This includes:

- The system of financial reporting and accounting
- The local budget process and structure
- Local revenue and expenditure authority

The report concludes with a review of the current ATCI credit risk methodology in light of the risks that cities face in the management of their finances and makes recommendations for possible adjustments to that methodology.

The System of Financial Reporting and Accounting

Disclosure – ideally based on clear rules consistently applied – is a key factor in credit risk analysis. The financial statements prepared and issued by the potential borrower are the primary source of information for any credit risk analysis. When looking at those statements it is vitally important to understand the underlying system of financial reporting and accounting – what it measures, when assets and liabilities are recognized and recorded, the rules on the content and presentation of the statements. The key issue is whether the financial statements provide a comprehensive picture of the finances of the reporting entity that shows all its assets and all its obligations. When it appears that not all assets and/or obligations are reflected in the financial statements, or if supporting information is not available through notes to the financial statements, disclosure is incomplete. This of and by itself adds an element of risk.

Cities in the Ukraine must deposit all their funds and keep all their accounts in a unified national treasury. The State Treasury handles all their receipts and payments. Ti also prepares and issues the financial statements for the cities. It was not possible during the short trip to establish clearly either the measurement focus or the basis of accounting used in the public sector in Ukraine. Information provided by the former director of local budgets in the Ministry of Finance suggests that transactions are recognized when actual funds are received or paid, that is, on a cash basis. There is a uniform chart of accounts for all the public sector, including cities. The State Treasury records a commitment against the city budget when the city issues a contract or purchase order.

By comparing outstanding commitments with payments, the State Treasury can estimate payables at the end of the year (a feature not normally available in cash accounting).

The focus of financial reporting is on legal and budgetary compliance. By law and regulation, each city must issue the following financial reports:

1. Report on financial state (balance) (a summary of accounts balances)
2. Report on local budget execution (based on budget classification – social protection, education, communal economy, etc.)
3. Report on local budget execution results (based on economic classification – operating revenues, operating expenditures)
4. Cash flow report
5. Budget indebtedness report (accounts receivable/payable)
6. Special fund revenues and expenditures report as regards own revenues of budget institutions financed by the local budget;
7. Information on execution of protected expenditures of local budgets;
8. Information on reserve fund utilization
9. Information on changes in goods and foodstuffs of budget institutions financed by the local budget;
10. Report on changes in fixed assets of budget institutions financed by the local budget;
11. Report on lack of and pilferage of cash and valuables in budget institutions financed by the local budget;
12. Information on changes to the local budget general fund figures during the year;
13. Report on revenues and other receipts (international donor assistance) of the special fund;
14. Report on receipt and utilization by local budgets of the State Budget grants and subventions;
15. Explanatory note to the annual report

The Budget Code requires that the budget include all city revenues and other sources of financing and all city expenditures. There are no off-budget funds. The information in the reports is consolidated accordingly. This is a positive feature of the system of financial reporting in the Ukraine.

The Treasury issues the reports monthly, quarterly and annually. The reports are designed for internal users. There are no notes to the financial statements that normally would inform external users of key facts and information underlying the figures in the various reports. This limits the value of the financial statements. It is a practice common to all transition countries where the very notion that someone outside the public authorities would want to read and understand the reports was inconceivable.

A specialized office in the Ministry of Finance conducts a limited audit of these financial reports. These audits generally look at some specific aspect of local finances and do not cover the entire scope of those finances. There are no other independent external audits of city financial reports.

ATCI financial analysts that have been conducting the credit risk assessment of target cities indicate that in reality not all of the reports listed above are available from the cities and not for all years. They face considerable difficulties collecting the reports and other financial and economic information from cities.

The lack of notes to the financial statements to inform external users, the limited external audit review and the difficulty in obtaining all reports for all years adds up

to limited disclosure of city finances. This is a risk that lenders or investors interested in Ukraine cities must accept.[1]

Cities maintain their own records but these are not kept together by one office in one place. Rather each "key spending unit" (as defined in the Budget Code) maintains its own revenue and expenditure records. The City Finance Department is but one of several such spending units that also include the various line departments (responsible for education, culture and so on).

There are indications that the records of the key spending units may not always reconcile fully with the information kept and reported by the State Treasury. The differences may represent 3 to 5 percent of aggregate figures. While not that significant, ***the fact that internal records of the city may not reconcile with those of the State Treasury adds to the risk of uncertain disclosure of city financial information***.

The Local Budget Process and Structure

Even the most solid local governments in any country can and do encounter circumstances that affect their finances adversely. What differentiates one local government from another is its ability to manage the problem. What differentiates the system of local government in one country from that in another is the extent to which the rules and procedures for managing local finances provide a reasonable basis for managing such problems. The first set of rules and procedures to consider are those on the local budget process and structure.

The Budget Code of the Ukraine defines the city budget process and structure. The Code establishes a process that allows city officials to plan, adopt, amend and execute their budget independently of other budgets. This is a positive aspect of the system of local finances in Ukraine – one that is not found commonly in other transition countries.

The Ministry of Finance provides information that cities need to prepare their budgets once at the beginning of the process and again after the Council of Ministers has adopted the draft State Budget. The second instance is particularly important. It includes "the estimated amount of intergovernmental transfers, the methodology for their definition, other amounts as necessary for development of draft local self-government budgets and other parameters needed for formulation of local budgets." (Article 75 (7)) This effectively allows cities in the Ukraine to develop their own budget on the basis of an estimate of all their revenues and other sources of financing. Further, city budgets are not subject to review by any external body prior to adoption. As noted above, the Budget Code requires that the budget include all revenues and other sources of financing and all expenditures. There are no off-budget funds. Together these features promote sound, independent budgeting by cities.

The Budget Code provides a clear classification of revenues, other sources of financing and expenditures that simplifies the task of calculating the operating (or current) balance in city finances separate from the overall or total balance. This facilitates the credit risk assessment by identifying the recurring funds that might be available to service debt.

The Budget Code divides the city budget (and all budgets) in "general" and "special" budget funds. The special budget fund includes all earmarked or special purpose revenues, related expenditures and any fund balances. The general fund includes all other revenues and related expenditures. By authorization of the City Council it is possible to transfer resources from the general to the special budget fund. In 2004, actual end-of-year expenditures of the general budget fund accounted for 82 percent of aggregate local expenditures. The special budget fund accounted for the remaining 18 percent.[2]

The Budget Code also establishes a Local Development Fund that includes all earmarked capital revenues and other sources of financing for capital expenditures. These include proceeds from the sale of assets and dividends on investments. They also include all the proceeds from any bond or loan. The revenues and expenditures of the Development Fund are recorded and reported as part of the special budget fund.

The prevailing interpretation of the Budget Code is that it requires that any repayment of principal on a bond or loan be made from resources available to the Development Fund. Interest payments are made from resources available in the general budget fund.

Finally, of interest to this report, the Budget Code also provides for certain "protected items" in the budget that may not be sequestered.

The rules and procedures governing the budget process in Ukraine are a positive factor when considering credit risk of cities. The segregation of capital expenditures in the Development Fund, the provision dividing debt service between the general and special budget funds and the protected items all add rigidity to the local budget that could become a constraint in times of severe budget stress (more on this below).

Local Revenue and Expenditure Authority[3]

Aside from those governing the budget process and structure, the other set of rules and procedures to consider when assessing the ability of local governments to manage problems that may arise in their finances are those regarding revenues and expenditures, that is, the ability of a local government to raise revenues and/or decrease expenditures if needed. In looking at this question the focus has to be on the general budget fund, as by definition the revenues and expenditures of the special budget fund are all earmarked or dedicated.

On the expenditure side of the general budget fund, there are two factors that limit the discretionary authority of cities to manage their finances. Protected items, as defined by the Budget Code, are one. These are types of expenditures that may not be sequestered in times of budget constraints. At present they include wages and related social insurance payments as well as certain items such as medicines. In 2004 in aggregate such items accounted for 79 percent of general budget fund expenditures.[4] The second factor limiting the ability of cities to manage the expenditure side of the general budget fund is the fact that a large share of their responsibility is to implement State programs in areas such as education, health and social assistance. For all of 2004, these "delegated" expenditures accounted for 84 percent of general budget fund expenditures.[5] To the extent that service policy in these sectors is a central government function, it suggests that cities have limited discretion in managing a large share of the general budget fund.

If we consider these two limitations on the expenditure side of the general budget fund and the absolute constraints on all special fund expenditures, then local governments have limited discretion to manage roughly 87 percent of their total expenditures (including both budget funds).[6] Or, conversely, local governments in aggregate have full discretionary control over approximately 13 percent of their total expenditures.

The rigidity of local expenditures – be they "delegated" or "protected" – suggests that cities would find it difficult to adjust expenditures to meet debt service

obligations if they found themselves in a situation of financial distress. In fact, the source of financial distress could easily be a change in central government policy affecting one or more of the "delegated" functions in health, education or social assistance.

There are even greater constraints on the revenue side of the general budget fund. Local governments are heavily reliant on shared taxes. Their share of the PIT and the tax on small businesses and entrepreneurs accounted for 75% of all general budget fund revenues in 2004. Conversely, local taxes and fees (those over which the local government has discretionary authority) represented 3% of total general budget fund revenues in the same period. They declined by 6% in nominal terms from 2003 to 2004.

Local governments have virtually no ability to make adjustments on the revenue side of the general budget fund. In fact, as with their expenditures, a change in central government policy – in this case regarding one or more of the various shared taxes – could easily become the source of financial distress for cities.

The ATCI Credit Risk Assessment Methodology

ATCI has developed and applied a sound methodology for assessing the credit risk of cities in Ukraine. It focuses on the recurring or operating surplus (deficit) as the key variable when considering the debt service capacity of cities. It uses various financial indicators or ratios to identify specific characteristics of the structure or trends in revenues or expenditures that may signal current or future problems in the finances of the cities. The following recommendations are intended solely as a complement to the existing methodology. They are intended to reflect some of the systemic problems discussed in the preceding sections. They are not meant to suggest that the assessments prepared to date do not meet the needs of the program. ATCI staff already adopted several of the recommendations.

Obtain additional information to that provided in the financial reports on possible obligations or liabilities. ATCI should ask the city to provide full and current information on the following:

- Outstanding loans or other debt obligations of the city and the current and historical status of compliance with the terms of those obligations
- Arrears as reported by key spending units (for comparison with arrears as shown in the financial reports)
- Arrears of key locally owned enterprises and trends in those arrears
- Ongoing capital projects and their claim on future revenues
- Investments or ownership shares of the city in private or mixed capital enterprises
- Outstanding guarantees or other financial commitments of the city to any other institution or enterprise
- Fines assessed by other public authorities (such as for environmental issues) and not paid
- Pending litigation and its potential financial impact
- Other contingent liabilities

Develop and monitor indicators of "rigidity" on the expenditure side of the general budget fund. ATCI should review the extent to which a city is constrained in managing the expenditure side of its general budget fund using indicators such as the following (some already in use, others new):

- Expenditures for delegated functions as a percent of recurring revenues
- Percent change in expenditures for delegated functions over percent change in recurring revenues
- Protected items as a percent of recurring revenues
- Percent change in protected items over percent change in recurring revenues
- Percent change in city payroll over percent change in national wages
- Operating surplus as a percent of expenditures for delegated functions
- Operating surplus as a percent of protected items

The last two ratios are very important and should serve as a complement to the ration of operating surplus to recurring revenues. The threshold value of the ratios should reflect historical experience. What has been the largest one-year increase in real terms of aggregate delegated expenditures? What has been the largest one-year increase in real terms of expenditures for protected items? The ratio of the operating surplus to each type of expenditure should be some multiple – probably not less than twice – the rate of the corresponding one-year increase.

So, for example, if aggregate national delegated expenditures increased by up to 10 percent in one year, the operating surplus should be no less than 20 percent of total city delegated expenditures. This will provide a cushion against possible changes in central government policy regarding health, education or social assistance that may not be accompanied by a corresponding increase in transfers from the State budget. There is a precedent for this when Parliament ordered an across-the-board increase in public sector wages in 2004. Many cities faced immediate serious financial problems.

Identify potentially troublesome ratios or trends in advance of interviews with city officials as the basis for assessing a) the city's own understanding of its current financial condition and b) the willingness and ability of the city to address and resolve current or future causes of fiscal stress.

Aside from providing a quantitative assessment of the finances of a city, the indicators and ratios that are part of the ATCI credit assessment methodology provide an opportunity to develop an approximate qualitative assessment of the city's financial management capacity. After ATCI staff have completed the entry of data in the financial model and identified areas of potential problems, they should conduct an interview of key decision makers in the city regarding these problem areas. Are the officials aware of the problem? Do they have a reasonable explanation for the underlying causes of the problem? Are they taking steps to mitigate the risks?

The following is an example of how this might work:

> The analysis of the finances of city X shows that rate of change year-to-year in operating expenditures in city X is greater than the corresponding rate of change in its recurring revenues. A further look at the indicators shows that this has been driven in large measure by increases in the payroll of city X at a higher rate than the corresponding national average.
>
> The interview with officials in city X would seek to find out more about these two trends. Is the change in payroll the result of having hired more people or having increased the wages of current staff? If the latter is the response, is this part of a

plan to retain good staff? Or, has city X simply been adding staff for essentially political motives. Is the increase in operating expenditures part of a plan to improve city services? Or, is it driven, as with the payroll, by political motives? What steps is the city planning to take to bring the trend under control before it incurs an operating deficit?

Following such an interview, ATCI staff will be in a better position to interpret the straight-line projection of trends in key city indicators. They also will have the basis to assess the willingness and ability of city officials to manage their finances prudently going forward. If that assessment is not fully positive, they may want to compensate by reducing the estimate of debt carrying capacity.

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[1] There are precedents in other transition countries such as the Czech Republic for an *ad hoc* request by lenders or investors for a complete independent audit of a given city's finances. Normally this would be limited to a very large bond issue or loan, given the substantial cost of such an audit.

[2] Data is from *Budget Monitoring: Analysis of Execution of Consolidated and theState2004 State Budget*, RTI, May 2005

[3] All figures in this section of the report are from RTI 2005

[4] Payroll 45%, Subsidies and current transfers 29%, Foodstuffs 3% and Medicines 2%

[5] Of these expenditures (less transfer and social protection payments to the population), 73 percent were for wages and related costs.

[6] Calculated as share of general fund in total expenditures X share of delegated expenditures in the general budget fund plus share of special fund in total expenditures or
(.82 x .84) + .18 = .87

ATTACHMENT 7

AMACO Finance
Introduction &
Executive Summary

I. Introduction

AMACO Finance will be the first specialty finance company in Ukraine directed at the agricultural equipment market. AMACO Finance expects to begin organization on October 1, 2006 and plans to start full operations on January 1, 2007. Based on AMACO's forecasted equipment sales for FY 2007, as well as rapidly increasing demand for foreign manufactured agricultural equipment in Ukraine, AMACO Finance expects to originate of between $25 and $30 million in its first 12 months of operation.

AMACO Finance is to be organized as a continuation of credit sales for agricultural equipment, currently being undertaken by American Machinery Co. ("AMACO") a company that, over the last 13 years, has been the leader in the importation and distribution of agricultural equipment in Ukraine. AMACO Finance will be an entirely separate company from AMACO, with separate offices. AMACO Finance expects to address the substantial opportunities currently available in the financing of agricultural equipment in Ukraine, as well as the limited financing options for farm operators presently offered by Ukrainian banks and other financial institutions.

AMACO Finance, while operating independently of AMACO, will utilize AMACO's extensive customer base as well as AMACO's proven capability of handling a large increase in credit sales while, at the same time, keeping losses at less than 1% of credit balance outstanding. AMACO Finance plans to start full operations on January 1, 2007, in time to support AMACO's equipment sales cycle that normally starts with the Farm Equipment Expo. in Kiev, held every February.

II. Goals For AMAKO Finance

- **To become the leading originator of agricultural equipment financing in Ukraine, while maintaining a superior return on invested capital and continuing the superior loss performance on credit extensions currently experienced by AMACO.**

- **To offer pricing at or below what is currently being offered on "hard currency" loans by Ukrainian banks while, at the same time, offering flexible terms and conditions not widely available in the Ukrainian market.**

- **To offer maximum convenience by minimizing documentation requirements, especially on smaller transactions (less than $75,000.00).**

III. AMACO

AMACO has, over the last 13 years, been Ukraine's leading importer and distributor of foreign made agricultural equipment, and supports its sales with a comprehensive parts department and service program. AMACO represents a number of major US, Canadian and EU manufacturers of agricultural equipment, in addition to a number of international manufacturers of parts and farm inputs. AMACO is a subsidiary of SABA, Inc., of Memphis, TN, which has been in the business of distributing agricultural equipment, worldwide, for over 20 years.

IV. Operation of AMACO Finance – Independent of AMACO

AMACO Finance will be operated as an entirely separate, and independent, entity from AMACO. AMACO Finance will make its own credit decisions, independent from AMACO. AMACO Finance will, at least initially, operate solely within the borders of Ukraine.

V. Initial Capitalization of AMACO Finance

It is expected that AMACO Finance will have an initial capitalization of at least $30 million, consisting of at least $5 million in equity, contributed by AMACO and SABA, Inc. who, initially, will be the 2 shareholders in AMACO Finance. The contribution by SABA, expected to be $5 million in cash, will be primarily used for the operation of the business with the balance used to fund leases and financings originated by AMACO Finance. The contribution by AMACO will consist of AMACO's existing credit portfolio (equipment only), information on its existing customers, and its existing credit procedures that have resulted in AMACO experiencing an extremely low loss ratio on its existing credit portfolio.

The balance of the capitalization of AMACO Finance, $25 million, will come in the form of a credit facility from one or more lenders, most likely one or more Western banks or financial institutions. The entire credit facility will be used to fund financings, or leases, originated by AMACO Finance.

VI. Expected Volume – FY 2007 (First Year of Operations)

AMACO Finance expects to originate between $25 and $30 million in new financings in FY 2007, and that these originations, at least initially, will come almost entirely from AMACO's approximately 7,000 existing customers in Ukraine. These 7,000 customers include 2,800 customers who have purchased equipment from AMACO in the past, as well as 4,200 customers who have only previously purchased parts from AMACO. AMACO Finance expects to concentrate initially on the equipment financing needs of those of AMACO's customers with the strongest credit histories.

VII. Key Assumptions

- **Demand for foreign manufactured agricultural in Ukraine is substantial, and increasing rapidly, as a result of cropping patterns used on most Ukrainian farms, age of existing equipment, and substantial increase in plantings of capital intensive crops including soybeans, sugar beets and rapeseed.**

- **AMACO's existing customers, especially its customers with strong credit histories, offer a substantial customer base for AMACO Finance for at least its first 2 years of operations.**

- **AMACO's existing credit procedures, very effective for short-term obligations now being offered by AMACO, can be equally effective for medium-term obligations to be offered by AMACO Finance.**

- **That AMACO Finance is able to find one or more debt sources who will give AMACO Finance the freedom to utilize its superior knowledge of the Ukrainian market, in general, and AMACO's existing customers, in particular, to earn a high rate of its return for its investors and, at the same time offer superior products for its customers and the maximum possible security for its lender(s).**

VIII. Selected Financial Information

AMACO's planned equipment sales are expected to be approximately $36 million in FY 2006 and approximately $100 million in FY 2007, which is expected to be the first year of operations for AMACO Finance. In FY 2005 approximately 54.5% of AMACO's equipment sales were made on credit. In FY 2007 it is expected that only 25 – 30% of AMACO's planned sales will be financed through AMACO Finance.

ATTACHMENT 8

LeaseIT™

ЗАТ "Лізинг інформаційних технологій"
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frontoffice@LeaseIT.com.ua
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LeaseIT
Business Plan

Executive Summary

The Opportunity:

LeaseIT has been operational since October 1, 2005 and is currently the only equipment lessor in Ukraine providing "small ticket" leases (average deal size of USD 3,000) for information technology ("IT") equipment, including personal computers and various peripherals. LeaseIT utilizes an expedited approval process based on proprietary technology that analyzes streamlined financial and credit information from each lessee in their application that is provided either through a web interface on the retailer's web site or directly into the LeaseIT website. Potential lessees include any legal entity, a majority of which are expected to be Small & Medium Sized Enterprises ("SME's").

According to estimates of independent market researchers, including GfK-USM and IDC and confirmed by major retailers of IT equipment, 2004 sales of IT equipment to businesses in Ukraine was approximately $600 million, of which approximately $200 million was to SME's. LeaseIT estimates that sales of IT equipment to commercial entities, including businesses and SME's, is growing at approximately 25% per year. We estimate that the sales of IT equipment to commercial entities in Ukraine will be $900 million in 2006 and $1,100 million in 2008.

Presently, almost none of the IT equipment sold to businesses in Ukraine is financed through leasing or other financial instruments. It is estimated that the current market for financing the acquisition of IT equipment by commercial entities on conditions offered by LeaseIT is $10-12 million, almost all of which is financing to SMEs. This represents a penetration rate of 1,3% which compares to 50% in the US, 17% in the UK and 2,3% in a comparable market such as Poland. LeaseIT estimates the penetration rate in Ukraine will increase to 5% in 2008, representing a market demand for financing of at least $60 million.

In most Western countries, much of the IT equipment purchased by businesses is acquired through financing. At a similar stage of development of the Leasing Industry in the US, leasing of IT equipment to SME's, with streamlined financial information, called "application only" leases, was the fastest growing segment of the US equipment leasing market. Leasing of IT and communication equipment has been the largest growing sector of the leasing industry in the United States over the last 5 years and now it takes the largest market segment of equipment leasing industry in US – more than 21% (Source: 2005 Equipment Leasing Association survey of industry activity). According to ELA survey IT leasing is the only one sector of US leasing industry in which high demand comes from all types of customers – large companies, SME, government and non-profit.

The Survey of US Leasing Industry Activity indicated that small ticket leasing experienced healthy volume growth and that it continues to be profitable. Since much of small ticket leasing is point of sale, captives and those companies in the vendor finance business will continue to benefit (Source: The Equipment Leasing & Finance Foundation). Credit scoring is used by 51 of the 91 lessors (56%) surveyed who are active in small ticket leasing. And 38 of those lessors use of auto-decisioning (up to a maximum transaction size). This is an increase from 21 lessors just 2 years ago. The number of lessors that use auto-decisioning increased between 2003-2004 and particularly in 2005. Similarly, the dollar volume of transactions made with auto-decisioning also increased over the same period. In Poland, the total volume of leasing of IT equipment in 2004 was Euro 61,6 million (according to 2004 Leaseurope statistics).

LeaseIT's Product:

The product offered by LeaseIT is a financial lease for IT equipment, for an average amount of USD 3,000.00, with streamlined financial information required from each lessee. Lease terms are usually between 12 and 24 months, with a down payment equal to 30% of the cost of equipment due at lease signing. LeaseIT presently funds all of its leases with an operating credit line with a current maximum exposure of $250,000, soon to be increased to $450,000, of which approximately $200,000 is outstanding. LeaseIT takes a commission of 15% of the equipment cost up-front resulting in a minimum gross profit of 20% of the cost of equipment of each lease.

Once the customer's credit information is received by LeaseIT through its web interface, LeaseIT uses a proprietary algorithm to evaluate the lessee's credit and provide a credit decision within 24 hours of the lessee's submission of its application. Upon credit approval lease documents are then generated by the retailer using a web interface on LeaseIT's web site, which LeaseIT provides to each retailer as part of their exclusive agreement. Once the customer signs the documents, payment to the vendor, for the equipment, is then made directly by LeaseIT.

Currently, LeaseIT receives substantially all of its business through exclusive agreements LeaseIT maintains with large retailers and direct sellers of IT equipment, allowing them to use LeaseIT's web interface in their business. As part of its exclusive agreement with LeaseIT, each retailer may use LeaseIT's logo on its web site, as well as on other sales materials including sales brochures, etc. Each retailer pays LeaseIT a fee, in consideration for using LeaseIT's technology. The "branding" of LeaseIT's name, and its unique services, is considered by LeaseIT to be a critical element of its business model.

Requested Investment in LeaseIT:

LeaseIT is currently seeking a debt financing for a total amount $7 million in the 2006, $11 million in 2007, $13 million in 2008.

LeaseIT also will use $1 million from equity investors, almost half of which will be used for the rapid increasing of number of agreement with IT retailers.

LeaseIT expects to be able to borrow $5.00 for every $1.00 in equity invested or accumulated in LeaseIT. Because the equity investment includes approximately $500,000.00 in equity support for an increased line of credit, it is expected that the size of the line of credit would be $2,500,000.00 to fund new lease transactions.

All debt financing will be directed to fund new lease transactions.

Possible debt financing from EBRD may me as follows:
2006 - $2 million
2007 - $3 million
2008 - $4 million
Total amount from EBRD: $9 million.

Recent Operations of LeaseIT:

LeaseIT has been operational since October 1, 2005. LeaseIT's web interface is currently available through 7 sellers of IT equipment, consisting of 2 retail locations and 5 direct sellers of IT equipment. Currently, most of the retail locations using LeaseIT's technology are located in Metro Kyiv as well as in Lugansk, Lutsk, Chernovtsy. LeaseIT's volume in 2005 is shown in the table below. In addition, the retailers currently using LeaseIT's technology have reported year-over-year sales increases of approximately 30%, much of which they believe is attributable to the availability of LeaseIT's technology.

	Number of new retailers	Number of new clients	Number of deals	Cost of equipment leased, UAH
July	1	1	1	10 667,00
August	1	2	2	31 906,22
September	1	7	10	179 259,70
October	-	7	11	139 236,86
November	-	6	19	353 471,48
December	4	4	7	321 479,82
Total	7	27	43	1,036,021.08

Cost of Equipment Leased in USD ($1.00 = UAH 5.05) - $205,152.69

In addition to the existing retail locations, LeaseIT expects to have its technology available in 200 retail, as well as other types of locations selling IT equipment by the end of Calendar Year 2006. LeaseIT will subsequently add approximately 30 locations in the First Quarter of 2006, 47 locations in the Second Quarter, 60 locations in the Third Quarter and 63 locations in the Fourth Quarter. These locations are owned and operated by approximately 75 retailers and representing an estimated 30-50% of the retail IT market in Ukraine.

Future Markets For LeaseIT's Services:

LeaseIT expects to eventually expand its services to include equipment other than IT equipment, such as medical equipment, HVAC equipment and small agricultural equipment. In each case LeaseIT expects to develop its brand, in the same way it is developing its brand with the leasing of IT equipment, by making its web interface available to the sellers of these types of equipment, as well as using the same credit and documentation model it currently uses. Additionally, LeaseIT expects to increase its transaction size, above the current average transaction size of USD 3,000.00. Future decisions on business expansion will depend on adequate capitalization, and necessary modification of existing credit parameters and procedures deemed necessary to accommodate larger transactions.

Expansion of LeaseIT's services may also be aided by the establishment of a credit bureau in Ukraine, which will provide easier availability of consumer credit information of private entrepreneurs and guarantors enhancing LeaseIT's approval process. It is expected that consumer credit information, similar to what is available today in more developed markets, will be available in Ukraine in 3-4 years. During this period, LeaseIT's algorithm, with which they use to evaluate customers' credit information, provides it with significant value added and constitutes a barrier to entry to anyone else who may want to enter the "small ticket" leasing market.

Existing Risks:

LeaseIT faces the following risks that attracting equity investment of approximately USD 1 million will help address:

1. LeaseIT will not develop sufficient credit and operational capacity and expertise in order to accommodate the expected rapid increase in volume of lease transactions and organizational growth.
2. LeaseIT will not secure the expected large number of retailers and other sellers of IT equipment in the short time projected, thus making it easier for competitors to enter the market.
3. LeaseIT will not maintain relations with leading retailers of IT equipment on which LeaseIT relies for a significant portion of its business.

All of these risks become more acute without adequate capital to support growth in the number of retail locations that offer LeaseIT's services, and the corresponding growth of lease transactions. Without additional capital LeaseIT would have to limit the number of retailers with which they work. Moreover, LeaseIT would be less able to offer incentives to retailers to continue using LeaseIT's services, as opposed to working with a potential competitor or going into the business themselves. Ultimately LeaseIT's success will depend on the level of service it will be able to offer, as well as its ability to expand the number of retailers that offer financing from LeaseIT.

LeaseIT believes that its branding strategy will make it more difficult for a retail location, once using LeaseIT for its customers' leasing needs, to make changes. As customers become more familiar with LeaseIT's brand and services, they will look for LeaseIT's logo and service availability as part of their purchase decision.

Financial Projections (Cash Budget):

A detailed cash budget for Calendar Years 2006-2007 is included with this Executive Summary. The cash budget assumes the successful consummation of the USD 1 million equity investment. These projections are based on the following additional assumptions:

1. Continuation of LeaseIT's operating history for October, November and December, 2005, across additional retail locations.
2. Expected additions to the existing retail locations where LeaseIT's service is available.
3. Gross profit per transaction of approximately 20% of the cost of equipment.
4. Expected cost of funds of 15%.

ATTACHMENT 9

BROKER MANUAL
Phone Call Checklist
(In Chronological Order)

When doing solicitation on the phone, or responding to a telephone inquiry about a leasing request, it is important to get as much information as possible, about the request, and to prequalify the transaction. It is also important to gain the confidence of your prospect. Such a telephone conversation should cover the following:

Particulars of the Deal – I usually like to start with this information, because it develops rapport with the prospect. He/she will then (hopefully) be more comfortable giving you credit information later in the conversation.

A. Amount of Request
    1. The larger the better.

B. Who is the vendor
    1. If you don't already know the vendor you can add the vendor to your prospect list.
    2. If you do know the vendor, then you can tell the prospect that you have worked with this company before, etc., and you had a good experience.
    3. If you know the vendor, and had a bad experience with working with that vendor, you might be able to provide your prospect with valuable information that might be helpful to them when dealing with the vendor.

C. When The Equipment is Going to Be Delivered
    1. If the equipment is going to be delivered in more than, say, 3 months you want to find out why it is taking so long.
        a. Asking this question might also result in finding out that the prospect hasn't yet selected the equipment but is still "shopping around."
        b. Maybe you can be of help in finding equipment (vendor relations).
    2. If the equipment is going to be delivered in 1-2 weeks you want to ask why it took the prospect so long to contact you.
        a. Perhaps he is shopping the deal. In this case he simply might be calling another lessor, to make sure that the pricing he got from the initial lessor he contacted is valid, and really does not have much intention of doing business with you.
        b. Perhaps he was initially going to pay cash, and then changed his mind.
        c. Both of these possibilities are important to know.

D. Why is your prospect getting the equipment.
    1. Let the customer tell you a story, about why they want to get the equipment, what it is going to do for the company, etc. It builds rapport and is a source of valuable information.
        a. Equipment justification is an important credit matter – it is a secondary repayment source.
        b. Try, as much as possible, to get the prospect to attach numbers to the Story, such as "this equipment will save me $10,000.00 a month in direct labor costs," etc.

E. Any other developments?
    1. Is the company going to move locations?
    2. Is the company going to have additional equipment financing needs in the near future (1 year or less)?

a. This could either be an opportunity for additional business, or a potential credit problem, depending on the prospect's financial information, but you don't know which one yet.

F. You are trying to build up rapport, and/or empathy, before you start asking the "tough" Questions about credit, etc.

Initial Credit Information – Basic credit information will tell you a great deal about whether or not you can complete the transaction.

A. Time in business
   1. If it is a new business you can usually stop the conversation right there (at least in the US), be very polite, tell him you will keep his company in your database and wish him luck.
   2. If the company has been in business more than 3 years then it is worth talking more.
   3. Has the company changed hands.
      a. If it is a 10 year-old company under new ownership you might have problems.
      b. The company might have gone from a Partnership to a Corporation, but otherwise is under the same ownership.

B. Sales/Profits.
   1. Hopefully, at this point in the conversation you have built up some empathy with the customer. You are looking for general information.

C. Other credit issues.
   1. You are trying to get the prospect to tell you if there are any issues, such as a bankruptcy, which might cause underwriting problems.

"Ask for the Order" – At this stage in the conversation you want to try to get the prospect to agree to send you his credit information. Try to pin him down as much as possible. If he is located near you, try to arrange an appointment to go out and meet.

A. If the customer wants you to send him an estimate of payments, do so, and make sure you include all the required information on the estimate.

B. Make sure you follow up.

C. If someone else offers lower payments make sure they are proposing on the same basis you are
   1. Often, competition will "play games," such as leaving out the advance payments, etc.

Appendix 2

NORDEN CAPITAL

8217 Beverly Bl., Suite 8
Los Angeles, CA 90048
Ph. 212-555-7070/Fax 212-555-7172
Email – jsmith@nordencapital.com

CREDIT REQUEST

Date:	Month XX, 2006
Prepared By:	John Smith
Lessee:	___________________, Inc., Dba ___________________
Guarantor(s):	Mr. ___________________ President
Transaction Type:	Finance Lease
Equipment Description:	1 – New Packaging Mach. 1 – New Fryer 1 – Used Snack Food Bagger 1 – Used Metal Detector 1 – New Forklift 1 – New Battery
Approximate Equipment Cost:	$173,053.69
Equipment Location:	__________
Rent Factor:	$20.66/$1,000.00 (.02066)
Residual:	$1.00
Advance Rentals:	1st and Last Months' Rent
Lease Term:	60 Months
Special Documents:	1. Proforma Invoices For All Equipment

CONTACTS

For Lessee: Mr. ______, President
Ph. ____________
Email –

Lessor Salesperson or Broker: Mr. John Smith
Ph. 212-555-7070
Email –
jsmith@nordencapital.com

For Vendor(s): To Be Supplied

ATTACHMENTS

1. Application & Secretary of State's Info. (to be supplied)
2. Cash Flow Analysis Prepared by Norden Capital
3. 2 Trade References (Bank Reference to Be Supplied)
4. Company's Interim Financial Statements (6 Months) for FY 2005
5. Company's Federal Income Tax Return for FYE 2004, 2003 & 2002
6. Company's Internal P & L for FYE 2004
7. Guarantor's Personal Financial Statement
8. Guarantor's Federal Income Tax Returns for 2003 & 2002 and all K-1's
9. Guarantor's Federal Income Tax Extension Filing for 2004

THE COMPANY

___________, Inc., dba _________ ("The Company") is an 8+ year-old ________ Corp., engaged in the manufacture of Mexican Food Products.

REVENUE & CASH FLOW

HISTORIAL REVENUE

($000)

ITEM	12/31/2004	12/31/2003	12/31/2002
Total Revenue	6293	6222	6067
Officer's Salary	90	90	90
Net Income	2	(28)	(67)
Depreciation & Other Non Cash Charges	184	233	187
Gross Cash Flow	186	205	120
Existing CPLTD	43	43	43
Less: Proj. Lease Pmts. Incl 2nd Lease	(89)		

Cash flow coverage for this transaction is 2.77/1, as shown on the attached “Financial Statement Summary,” including a 2nd lease with National City Bank, booked in July, 2005, for $195,000.00. According to the lessee the monthly payment, on the 2nd lease, is $3,874.28. The liability of $7,784.56, shown on the lessee’s 6/30/05 Interim Statement, is the 2 advance payments on the National City lease.

Debt/equity ratio, including this lease request and the National City lease of $195,000.00, will be 2.15/1. This is also shown on the attached “Financial Statement Summary.”

According to the lessee FY 2004 depreciation expense, on the tax return, is included in Cost of Goods Sold. On the Company’s 2004 tax return, one of the supporting statements notes “Depreciation on COGS” of $53,010.00. In addition the lessee indicated that there were the following additional non-cash expenses on the tax return: Accrued Vacation - $68,076.00 & Accrued Sick Leave - $48,053.00. These two items total $116,129.00. On the 2004 tax return, on Page 2 of the Supporting Statements, shows “Accrued Expenses and Misc. Payables” of $116,129.00 as of the end of 2004. Therefore, the information on the tax return appears to support the information on the Lessee’s Internally Prepared FYE 2004 P&L.

A review of the tax returns for the Company, for 2004, 2003 & 2002, indicates a fairly predictable operating environment, with consistent cash flow. All balance sheet and income statement ratios are fairly stable.

EXISTING COMMERCIAL TERM DEBT OBLIGATION & ADJUSTED DEBT/EQUITY RATIO

The CPLTD of approximately $43,000.00 consists of an existing equipment lease that is due to be paid off within the next 12 months. According to the lessee this balance is what remains of several equipment leases totaling $603,623.00 that were originated between 1997 & 2000, all of which were for a term of 60 months.

In addition to this lease request there is a 2nd, new lease, of approximately $195,000.00, that is also for new production equipment. According to the lessee the equipment on the 2nd lease, as well as this lease, will constitute a new production line that will substantially replace the company’s existing line.

EQUIPMENT JUSTIFICATION

According to the Lessee the equipment in both leases will save the Company approximately $83,000.00/year, on the Company’s existing business, by allowing for faster throughput and more efficient use of direct labor. In addition, according to the Lessee, the equipment will allow the company to produce a line of tortilla chips, in connection with a contract that the company has recently secured. Finally, the equipment will allow the company to produce tortilla chips in 3 oz. bags, for potential customers who may want to purchase smaller bags.

PERSONAL CASH FLOW

According to Mr. ______, President of ___________________, Inc., his 2004 AGI will be approximately $250,000.00 and his Federal Tax obligation, according to Mr. ___________________’s 2004 extension filing, was $7,669.00. Based on this information Mr. ___________________’s Personal Cash Flow is as follows:

ITEM	AMOUNT
2004 AGI	$250,000
Less: Federal Tax	(7,669)
Less: State/Local Tax (Fr. 2003 Return)	(3,409)
Less: Est. Real Estate Payments (Fr. 2003 Return)	(42,000)
Less: Approximate Personal Expenses	(40,000)
Net Personal Cash Flow	$156,922

OTHER CREDIT MATTERS

Progress Payment on Equipment – According to the attached proforma invoices the following vendors require progress payments: The Blodgett Company (50% Progress Payment on a COE of $63,500.00); Modern Baking Co. (60% Progress Payment on a COE of $60,000.00).

Building Rent – According to the Lessee, FYE 2004 building rent, of $126,000.00 was paid by the Company to a related entity, called VJ 1700 Investments, LLC which, according to Mr. Schofield's PFS, he has a 99% interest. According to Mr. ___________________ the rent payments to VJ are discretionary.

Notes & Bonds Due In Less Than 1 Year (Fr. Company's FYE 2004 Tax Return – According to the Lessee this obligation, $355,715.00 at the end of 2004, is owed VJ 1700 Investments, LLC, in which ___________________ has a 99% interest. VJ 1700 Investments, LLC is also the Owner of the building in which ___________________, Inc. is a tenant. From reviewing the attached spread of the financials, prepared by Norden Capital, it appears that payments have been made on this obligation, by ___________________, as well as additional extensions to SG by the Lender.

VMS & ___________________ Investments (From ___________________'s PFS) – These are both family Partnerships, in which ___________________ has a substantial Partnership Interest. According to ___________________ the investments held in both Partnerships are all liquid investments, consisting mostly of tax exempt securities.

Valuations on ___________________'s PFS – According to Mr. ___________________ all of the valuations shown on his PFS are at cost. As mentioned in the previous paragraph, the assets of both VMS and ___________________ Investments are primarily liquid investments, consisting primarily of tax exempt securities. The valuation of those investments were at cost, at the date the PFS was prepared. Any change in those valuations would be very small, consisting largely of undistributed coupon payments from securities. Mr. ___________________ has signed Norden's PFS form, with a current date, and has attached his PFS by reference.

FINANCIAL STATEMENT ANALYSIS

NAME: __ MEXICAN FOODS, INC

INCOME STATEMENT

	12/31/2004 12 months Tax Return & Int. FS	12/31/2003 12 months Tax Return	12/31/2002 12 months Tax Return	12/31/2005 6 months Int. Fin. Stmt.
Total Revenue	$ 6,292,908	$ 6,222,009	$ 6,067,031	$ 3,266,600
Cost of Sales	3,440,753	3,347,929	3,008,349	2,362,133
Gross Margin	$ 2,852,155	$ 2,874,080	$ 3,058,682	$ 904,467
Stockholder salary	90,000	90,000	90,000	
Other salary	530,369	533,001	584,857	0
Depreciation & Other Non Cash Ch.	184,371	233,337	187,320	
Other Operating Expenses	2,057,112	2,015,712	2,152,345	997,064
Total Operating Expenses	$ 2,861,852	$ 2,872,050	$ 3,014,522	$ 997,064
Operating Income	$ (9,697)	$ 2,030	$ 44,160	$ (92,597)
Interest Income	0	0	0	0
Interest Expense	(12,039)	(65,685)	(118,013)	
Other Income	24,024	35,845	6,917	(22,240)
Pre-Tax Income	$ 2,288	$ (27,810)	$ (66,936)	$ (114,837)
Provision for Income Taxes		0	0	
Net Income	$ 2,288	$ (27,810)	$ (66,936)	$ (114,837)

CASH FLOW

Net Income	$ 2,288	$ (27,810)	$ (66,936)	$ (114,837)
Depreciation & Other Non Cash Ch.	184,371	233,337	187,320	0
Debt Service	(42,621)	(43,178)	(70,006)	(29,026)
Dividends	0	0	0	0
Net Cash Flow	$ 144,038	$ 162,349	$ 50,378	$ (143,863)

FINANCIAL STATEMENT ANALYSIS

BALANCE SHEET

	12/31/2004 12 months Tax Return & Int. FS	12/31/2003 12 months Tax Return	12/31/2002 12 months Tax Return	12/31/2005 6 months Int. Fin. Stmt.
Cash	$ 86,448	$ 219,828	$ 169,724	$ 79,264
Accounts Receivable	416,629	388,148	417,325	421,528
Other Receivables	0	0	0	0
Inventories	205,237	157,343	245,810	170,665
Prepaid Expenses	116,263	0	0	56,183
Other Current Assets	465	7,882	31,391	0
Total Current Assets	$ 825,042	$ 773,201	$ 864,250	$ 727,640
Equipment, Furniture & Fixtures	$ 217,608	$ 194,624	$ 194,624	
Leaseholds	0	0	0	0
Total Property & Equipment	$ 217,608	$ 194,624	$ 194,624	$ 240,000
Less: Depreciation	(190,600)	(172,849)	(153,888)	(190,600)
Net Property & Equipment	$ 27,008	$ 21,775	$ 40,736	$ 49,400
Intangible Assets Less Amort.	91,890	129,255	263,105	91,890
TOTAL ASSETS	$ 943,940	$ 924,231	$ 1,168,091	$ 868,930
Accounts Payable	$ 271,472	$ 143,441	$ 137,335	$ 139,649
Accruals	0	0	0	0
Other current liabilities	214,132	144,618	63,872	181,048
Note Payable	0	0	0	69,483
Current Port. L-T Debt	42,621	43,178	70,006	29,026
Total Current Liabilities	$ 528,225	$ 331,237	$ 271,213	$ 419,206
L/T debt		$ 43,178	$ 86,356	
Note Payable to Related Co.	335,715	472,104	705,000	379,715
Total L/T Liabilities	$ 335,715	$ 515,282	$ 791,356	$ 379,715
TOTAL LIABILITIES	$ 863,940	$ 846,519	$ 1,062,569	$ 798,921
Common stock (Less Treas. Stock)	$ 150,000	$ 150,000	$ 150,000	$ 150,000
Retained earnings	(70,000)	(72,288)	(44,478)	(79,991)
Total Equity	$ 80,000	$ 77,712	$ 105,522	$ 70,009
TOTAL LIABILITIES & EQUITY	$ 943,940	$ 924,231	$ 1,168,091	$ 868,930

FINANCIAL STATEMENT ANALYSIS

SUMMARY DATA

	12/31/2004 12 months Tax Return & Int. FS	12/31/2003 12 months Tax Return	12/31/2001 12 months Tax Return	12/31/2004 6 months Int. Fin. Stmt.
Total Revenue	$ 6,292,908	$ 6,222,009	$ 6,067,031	$ 3,266,600
Stockholder salary	$ 90,000	$ 90,000	$ 90,000	$ -
Operating Income	$ (9,697)	$ 2,030	$ 44,160	$ (92,597)
Net Income	$ 2,288	$ (27,810)	$ (66,936)	$ (114,837)
Net Working Capital	$ 296,817	$ 441,964	$ 593,037	$ 308,434
Total Equity	$ 80,000	$ 77,712	$ 105,522	$ 70,009

KEY RATIOS

% of Revenues				
- Cost of Sales	54.68	53.81	49.59	72.31
- Stockholder salary	1.43	1.45	1.48	0.00
- Operating Expense	45.48	46.16	49.69	30.52
- Operating Income	-0.15	0.03	0.73	-2.83
- Net Income	0.04	-0.45	-1.10	-3.52
Current Ratio	1.56	2.33	3.19	1.74
Days Receivables	24.17	22.77	25.11	30.97
Days Inventory	21.47	16.92	29.42	17.34
Days Payables	28.80	15.64	16.66	14.19
L-T Debt/Equity	0.53	1.11	1.48	0.41
Total Debt/Equity	0.53	1.11	1.48	1.41
Total Liabilities/Equity	10.80	10.89	10.07	11.41
Cash Flow/Debt Service	4.38	4.76	1.72	-3.96

Attachment 9_4

Name: _____ Mexican Foods, Inc.
Amount:$173,053.69
Ann. Debt Svce. ($000): $43
Term: 60 Months

	Fiscal Period Ending:			
($000's)	12/31/2004 year	12/31/2003 year	12/31/2002 year	12/31/05 6 Months
Total Revenue	6,293	6,222	6,067	3,267
Net Income	2	(28)	(67)	(115)
Depr. & Other Non Cash Chgs.	184	233	187	90
Debt Svce/Existing + Oth New Ls	67	42	70	
(Withdrawal)/contribution	0	0		
Partners Net Cash Flow (Net)				
Net Cash Flow	119	163	50	(25)
Cash	86	220	170	79
Current Assets	825	773	864	728
Net Property & Equipment	27	22	41	49
Total Assets	943	924	1,168	869
Current Liabilities	528	331	271	419
Credit line outstanding	0	0	0	69
L/T Debt	336	515	791	380
Total Liabilities	864	847	1,064	799
Total Equity	80	78	106	70
Net Working Capital	297	442	593	309
Current Ratio	1.56	2.34	3.19	1.74
L-T Debt/Equity	4.20	6.60	7.46	5.43
Total Liabilities/Equity	10.80	10.86	10.04	11.41
Cash Flow/Debt Service	2.77	4.88	1.71	#DIV/0!
Intangibles				
Subordinated Debt	336	472	705	380
New Lease Obligations	368			
Tangible Equity	416	550	811	450
Total Liabilities/Tangible Equity	2.15	0.68	0.44	0.93

LEASE SCHEDULE

MASTER EQUIPMENT LEASE AGREEMENT NO. ____________________

LEASE SCHEDULE NO. ____________________

BETWEEN ____ (LESSOR)
and ____ (LESSEE).

1. **DESCRIPTION OF EQUIPMENT**

Quantity	**Item**	**Model/Serial No.**

2. **EQUIPMENT LOCATION:** The above Equipment is to be located and delivered to Lessee's premises at _______.
3. **RENTAL TERM**: _______ months.
4. **RENTAL:** The first payment in the amount of $_______ (plus applicable tax) is due _______, _______. Subsequent rental payments will be in the same amount and due on the same day _______(monthly, quarterly, etc.) thereafter.
5. **NUMBER AND AMOUNT OF ADVANCE RENTAL PAYMENTS:** NUMBER: ______ $_______ .
6. **SECURITY DEPOSIT:** $ _______ .
7. THIS SCHEDULE AND ITS TERMS AND CONDITIONS ARE HEREBY INCORPORATED BY REFERENCE IN THE ABOVE MASTER EQUIPMENT LEASE AGREEMENT. LESSEE PERMITS LESSOR TO INSERT MODEL AND SERIAL NUMBERS OF EQUIPMENT WHEN DETERMINED BY LESSOR.

LESSEE:

____
(Must be signed by Authorized Corporate Officer, Partner, or Proprietor)

____
(Title)

____
(Title)

____
(Title)

____
(Title)

LESSOR:

____

____
(Title)

Accepted this _______ day of _____________ , _____ at Portland, OR

MASTER EQUIPMENT LEASE AGREEMENT

MASTER LEASE AGREEMENT NO. ____________

Lease Agreement made this ____________________ day of ____________________________________, ______________ between _______ ("Lessor") with a place of business located at _______ and _______ ("Lessee") having its principal place of business located at _______.

1. LEASE AGREEMENT. Lessor hereby leases to Lessee and Lessee hereby leases from Lessor all of the personal property ("Equipment") described in Equipment Lease Schedule(s), which are or may from time to time be executed by Lessor and Lessee and attached hereto or incorporated herein by reference ("Schedules"), upon the terms and conditions set forth in this Lease, as supplemented by the terms and conditions set forth in the appropriate Schedule(s) identifying such items of Equipment. All terms and conditions of this Lease shall govern the rights and obligations of Lessor and Lessee except as specifically modified in writing. Whenever reference is made herein to the "Lease", it shall be deemed to include each of the various Schedules identifying all items of Equipment, all of which constitute one undivided Lease of the Equipment and the terms and conditions of which are incorporated herein by reference.

2. SELECTION OF EQUIPMENT; ACCEPTANCE. Lessee will select the type, quantity and supplier of each item of Equipment designated in the appropriate Schedule, and in reliance thereon such Equipment will then be ordered by Lessor from such supplier or Lessor will accept an assignment of any existing purchase order therefore. Lessor will have no liability for any delivery or failure by the supplier to fill the purchase order or to meet the conditions thereof. Lessee acknowledges that Lessor has not participated and will not participate in any way in Lessee's selection of the Equipment or of the supplier. Lessee agrees to inspect the Equipment and to execute an Acknowledgment and Acceptance of Equipment by Lessee notice, as provided by Lessor, after the Equipment has been delivered and after Lessee is satisfied that the Equipment is satisfactory in every respect. Lessee hereby authorizes Lessor to insert in this Lease serial numbers or other identifying data with respect to the Equipment.

3. DISCLAIMER OF WARRANTIES AND CLAIMS; LIMITATION OF REMEDIES. LESSOR, NOT BEING THE MANUFACTURER OF THE EQUIPMENT NOR THE MANUFACTURER'S AGENT, MAKES NO EXPRESS OR IMPLIED WARRANTY OF ANY KIND WHATSOEVER WITH RESPECT TO THE EQUIPMENT, INCLUDING, BUT NOT LIMITED TO, THE MERCHANTABILITY OF THE EQUIPMENT OR ITS FITNESS FOR ANY PARTICULAR PURPOSE; THE DESIGN OR CONDITION OF THE EQUIPMENT; THE QUALITY, Y2K COMPLIANCE OR CAPACITY OF THE EQUIPMENT; THE WORKMANSHIP IN THE EQUIPMENT; COMPLIANCE OF THE EQUIPMENT WITH THE REQUIREMENT OF ANY LAW, RULE, SPECIFICATION OR CONTRACT PERTAINING THERETO; PATENT INFRINGEMENT; OR LATENT DEFECTS. LESSEE LEASES THE EQUIPMENT "AS IS" AND WITH ALL FAULTS. Lessee accordingly agrees not to assert any claim whatsoever against Lessor for loss of anticipatory profits or consequential damages. Lessor shall have no obligation to install, erect, test, service, or maintain the Equipment. Lessee shall look to the manufacturer and/or seller for any claims related to the Equipment.

If the Equipment is not properly installed, does not operate as represented or warranted by the supplier or manufacturer, or is unsatisfactory for any reason, regardless of cause or consequence, Lessee's only remedy, if any, shall be against the supplier or manufacturer of the Equipment and not against Lessor.

Lessor hereby acknowledges that any manufacturer's and/or seller's warranties are for the benefit of both Lessor and Lessee. NOTWITHSTANDING THE FOREGOING, LESSEE'S OBLIGATIONS TO PAY THE RENTALS OR OTHERWISE UNDER THIS LEASE SHALL BE AND ARE ABSOLUTE AND UNCONDITIONAL. To the extent permitted by the manufacturer or seller, and provided Lessee is not in default under this Lease, Lessor shall make available to Lessee all manufacturer and/or seller warranties with respect to Equipment.

Lessee specifically acknowledges that the Equipment is leased to Lessee solely for commercial or business purposes and not for personal, family, or household purposes.

The parties have specifically negotiated and agreed to the foregoing section 3: **Lessee initials:** ____________________

4. STATUTORY FINANCE LEASE. Lessee agrees and acknowledges that it is the intent of both parties to this Lease that it qualify as a statutory finance lease under Article 2A of the Uniform Commercial Code as adopted in Oregon. Lessee acknowledges and agrees that Lessee has selected both: (1) the Equipment; and (2) the supplier from whom Lessor is to purchase the Equipment. Lessee acknowledges that Lessor has not participated in any way in Lessee's selection of the Equipment or of the supplier, and Lessor has not selected, manufactured, or supplied the Equipment.

LESSEE IS ADVISED THAT IT MAY HAVE RIGHTS UNDER THE CONTRACT EVIDENCING THE LESSOR'S PURCHASE OF THE EQUIPMENT FROM THE SUPPLIER CHOSEN BY LESSEE AND THAT LESSEE SHOULD CONTACT THE SUPPLIER OF THE EQUIPMENT FOR A DESCRIPTION OF ANY SUCH RIGHTS.

5. ASSIGNMENT BY LESSEE PROHIBITED. WITHOUT LESSOR'S PRIOR WRITTEN CONSENT , LESSEE SHALL NOT ASSIGN THIS LEASE OR SUBLEASE THE EQUIPMENT OR ANY INTEREST THEREIN, OR PLEDGE OR TRANSFER THIS LEASE, OR OTHERWISE DISPOSE OF THE EQUIPMENT COVERED HEREBY.

6. COMMENCEMENT; RENTAL PAYMENTS; INTERIM RENTALS. This Lease shall commence upon the written acceptance hereof by Lessor and shall end upon full performance and observance by Lessee of each and every term, condition and covenant set forth in this Lease, any Schedules hereto and any extensions hereof. Rental payments shall be in the amounts and frequency as set forth on the face of this Lease or any Schedules hereto. In addition to regular rentals, Lessee shall pay to Lessor interim rent for the use of the Equipment prior to the due date of the first payment. Interim rent shall be in an amount equal to 1/30th of the monthly rental, multiplied by the number of days elapsing between the date on which the Equipment is accepted by Lessee and the commencement date of this Lease, together with the number of days elapsing between commencement of the Lease and the due date of the first payment. The payment of interim rent shall be due and payable upon Lessee's receipt of invoice from Lessor. The rental period under the Lease shall terminate following the last day of the term stated on the face hereof or in any Schedule hereto unless such Lease or Schedule has been extended or otherwise modified. Lessor shall have no obligation to Lessee under this Lease if the Equipment, for whatever reason, is not delivered to Lessee within ninety (90) days after Lessee signs this Lease. Lessor shall have no obligation to Lessee under this Lease if Lessee fails to execute and deliver to Lessor an Acknowledgement and Acceptance of Equipment by Lessee acknowledging its acceptance of the Equipment within thirty (30) days after it is delivered to Lessee, with respect to this Lease or any Schedule hereto.

7. SECURITY DEPOSIT. As security for the prompt and full payment of rent, and the faithful and timely performance of all provisions of this Lease, and any extensions or renewals thereof, Lessee shall pledge and deposit with Lessor the security amount set forth in the section shown as "Security Deposit" on each respective Schedule. In the event any default shall be made in the performance of any of Lessee's obligations under this Lease, Lessor shall have the right, but shall not be obligated, to apply said security to the curing of such default. Within 15 days after Lessor mails notice to Lessee that Lessor has applied any portion of the Security Deposit to the curing of any default, Lessee shall restore said Security Deposit to the full amount set forth in the Schedules. On the expiration or earlier termination of each Schedule to this Lease, or any extension or renewal thereof, provided Lessee has paid all of the rent herein called for and fully performed all other provisions of this Lease with respect to such schedule, Lessor will return to Lessee any then remaining balance of the Security Deposit with respect to such Schedule, without interest. Said Security Deposit may be commingled with Lessor's other funds.

8. LIMITED PREARRANGED AMENDMENTS; AUTHORIZATION; SPECIFIC POWER OF ATTORNEY. In the event it is necessary to amend the terms of this Lease or the terms of any Schedule to reflect a change in one or more of the following conditions:

(1) Lessor's actual cost of procuring the Equipment; or
(2) Lessor's actual cost of providing Equipment to Lessee; or
(3) A change in the Lease payments as a result of (1) and/or (2) above; or
(4) Description of the leased Equipment,

Lessee agrees that any such amendment shall be described in a letter from Lessor to Lessee, and unless within 15 days after the date of such letter Lessee objects thereto in a writing delivered to Lessor, this Lease and any affected Schedules shall be deemed amended and such amendments shall be incorporated herein/therein as if originally set forth herein/therein.

Lessee authorizes Lessor or its designee to file a Uniform Commercial Code financing statement without Lessee's signature, in form and content and from time to time as Lessor deems proper, listing Lessee as Lessee or Debtor. Lessee further grants to Lessor a specific power of attorney for Lessor to sign, endorse or negotiate for Lessor's benefit any instrument representing proceeds from any policy of insurance covering the Equipment.

9. LESSEE'S REPRESENTATION. Lessee represents that its exact legal name, state of incorporation, location of its chief executive office and/or its place of residence as applicable, have been correctly identified to Lessor.

10. USE; EQUIPMENT LOCATION. Lessee shall use the Equipment in a careful manner, shall make all necessary repairs at Lessee's expense, and shall comply with all laws relating to its possession, use or maintenance, and shall not make any alterations, additions or improvements to the Equipment without Lessor's prior written consent. All additions, repairs or improvements made to the Equipment shall belong to Lessor. The Equipment shall be kept at the location specified above, or, if none is specified, at Lessee's address as set forth above and shall not be removed without Lessor's prior written consent.

11. OWNERSHIP; PERSONALTY. The Equipment is, and shall remain, the property of Lessor, and Lessee shall have no right, title or interest therein or thereto except as expressly set forth in this Lease. The Equipment shall remain personal property even though installed in or attached to real property.

12. SURRENDER. By this Lease, Lessee acquires no ownership rights in the Equipment and has no option to purchase same. Upon the expiration or termination of any Schedule or this Lease, or in the event of a default pursuant to Paragraph 20 hereof, Lessee, at its expense, shall return the Equipment in good repair, ordinary wear and tear resulting from proper use thereof alone excepted, by delivering it, packed and ready for shipment, to such place as Lessor may specify.

13. RENEWAL. At the expiration of the term set forth in each Schedule, Lessee shall return the Equipment subject to said Schedule in accordance with Paragraph 12 hereof. At Lessor's option, this Lease, with respect to each Schedule, may be continued on a month-to-month basis until 30 days after Lessee returns the Equipment subject to the Schedule to Lessor. In the event that the Lease, with respect to a Schedule, is so continued, Lessee shall pay to Lessor rentals in the same periodic amounts as indicated under "Rental" on the Schedule.

14. LOSS AND DAMAGE. Lessee shall bear the entire risk of loss, theft, damage or destruction of the Equipment from any cause whatsoever, and no loss, theft, damage or destruction of the Equipment shall relieve Lessee of the obligation to pay rent or to comply with any other obligation under this Lease.

In the event of damage to any item of Equipment, Lessee shall immediately place the same in good repair at Lessee's expense. If Lessor determines that any item of Equipment is lost, stolen, destroyed or damaged beyond repair, Lessee shall at Lessee's option do one of the following:

(a) Replace the same with like Equipment in good repair, acceptable to Lessor; or

(b) Pay Lessor in cash the following: (i) all amounts due by Lessee to Lessor with respect to all affected Schedules up to the date of the loss; (ii) the unpaid balance of the total rent for the remaining term of the affected Schedules attributable to said item, reduced to present value at a discount rate of 6% as of the date of the loss; and (iii) the Lessor's estimate as of the time this Lease was entered into of Lessor's residual interest in the Equipment, discounted to present value at a discount rate of 9% as of the date of the loss. Upon Lessor's receipt of payment as set forth above, Lessee shall be entitled to the Equipment, without any warranties. If insurance proceeds are used to fully comply with this subparagraph, the balance of any such proceeds shall go to Lessee to compensate for loss of use of the Equipment for the remaining term of the Lease.

LESSEE HAS READ AND AGREES TO ALL ITEMS ON THIS PAGE 2 OF 4 ____________________
Initials

15. INSURANCE; LIENS; TAXES. Lessee shall provide and maintain insurance against loss, theft, damage or destruction of the Equipment in an amount not less than the full replacement value of the Equipment, with loss payable to Lessor. Lessee shall also provide and maintain comprehensive general all-risk liability insurance, including but not limited to product liability coverage, insuring Lessor and Lessee with a severability of interest endorsement or its equivalent, against any and all loss or liability for damages either to persons or property or otherwise, which might result from or happen in connection with the condition, use or operation of the Equipment, with such limits and with an insurer as are satisfactory to Lessor. Each policy shall expressly provide that said insurance as to Lessor and its assigns shall not be invalidated by any act, omission or neglect of Lessee and cannot be canceled without 30 days written notice to Lessor. As to each policy, Lessee shall furnish to Lessor a certificate of insurance from the insurer, which certificate shall evidence the insurance coverage required by this Paragraph and shall designate Lessor as loss payee and/or additional insured. Lessor shall have no obligation to ascertain the existence or adequacy of insurance, or to provide any insurance coverage for the Equipment or for Lessee's benefit.

Lessee shall keep the Equipment free and clear of all levies, liens and encumbrances. Lessee shall pay all charges and taxes (local, state and federal) which may now or hereafter be imposed upon the ownership, leasing, rental, sale, purchase, possession or use of the Equipment excluding, however, all taxes on or measured by Lessor's net income.

If Lessee fails to procure or maintain said insurance or to pay said charges or taxes, Lessor shall have the right, but shall not be obligated, to effect such insurance, or pay such charges or taxes. In that event, Lessor shall notify Lessee of such payment and Lessee shall repay to Lessor the cost thereof within 15 days after such notice is mailed to Lessee.

16. INDEMNITY. Lessee shall indemnify Lessor against any claims, actions, damages or liabilities, including all attorney fees, arising out of or connected with the Equipment, without limitation. Such indemnification shall survive the expiration, cancellation or termination of this Lease. Lessee waives any immunity Lessee may have under any industrial insurance act with regard to indemnification of Lessor.

17. ASSIGNMENT BY LESSOR. Any assignee of Lessor shall have all of the rights but none of the obligations of Lessor under this Lease. Lessee shall recognize and hereby consents to any assignment of this Lease by Lessor, and Lessee shall not assert against the assignee any defense, counterclaim or set-off that Lessee may have against Lessor. Subject to the foregoing, this Lease inures to the benefit of and is binding upon the heirs, devisees, personal representatives, survivors, successors in interest and assigns of the parties hereto.

18. SERVICE CHARGES; INTEREST. If Lessee shall fail to make any payment required by this Lease within 10 days of the due date thereof, Lessee shall pay to Lessor a service charge of 8% of the amount due, provided, however, that not more than one such service charge shall be made on any delinquent payment regardless of the length of the delinquency. In addition to the foregoing service charge, Lessee shall pay to Lessor a $100 default fee with respect to any payment which becomes thirty (30) days past due. In addition, Lessee shall pay to Lessor any actual additional expenses incurred by Lessor in collection efforts, including but not limited to, long-distance telephone charges and travel expenses.

Further, Lessee shall pay to Lessor interest on any delinquent payment or amount due under this Lease from the due date thereof until paid, at the lesser of the maximum rate of interest allowed by law or 18% per annum.

19. TIME OF ESSENCE. Time is of the essence of this Lease, and this provision shall not be impliedly waived by the acceptance on occasion of late or defective performance.

20. DEFAULT. Lessee shall be in default of this Lease if:

(a) Lessee shall fail to make any payment due under the terms of this Lease for a period of 10 days from the due date thereof; or

(b) Lessee shall fail to observe, keep or perform any other provision of this Lease, and such failure shall continue for a period of 10 days; or

(c) Lessee has made any misleading or false statement, or representation in connection with application for or performance of this Lease; or

(d) The Equipment or any part thereof shall be subject to any lien, levy, seizure, assignment, transfer, bulk transfer, encumbrance, application, attachment, execution, sublease, or sale without prior written consent of Lessor, or if Lessee shall abandon the Equipment or permit any other entity or person to use the Equipment without the prior written consent of Lessor; or

(e) Lessee dies or ceases to exist; or

(f) Lessee changes its name, state of incorporation, chief executive office and/or place of residence without providing Lessor with 30 days written notice of such change;

(g) Lessee defaults on any other agreement it has with Lessor; or

(h) Any guarantor of this Lease defaults on any obligation to Lessor, or any to the above-listed events of default occur with respect to any guarantor, or any such guarantor files or has filed against it a petition under the bankruptcy laws.

21. REMEDIES. If Lessee is in default, Lessor, with or without notice to Lessee, shall have the right to exercise any one or more of the following remedies, concurrently or separately and without any election of remedies being deemed to have been made:

(a) Lessor may enter upon Lessee's premises and without any court order or other process of law may repossess and remove the Equipment, or render the Equipment unusable without removal, either with or without notice to Lessee. Lessee hereby waives any trespass or right of action for damages by reason of such entry, removal or disabling. Any such repossession shall not constitute a termination of this Lease;

(b) Lessor may require Lessee, at its expense, to return the Equipment in good repair, ordinary wear and tear resulting from proper use thereof alone excepted, by delivering it, packed and ready for shipment, to such place as Lessor may specify;

(c) Lessor may cancel or terminate this Lease and may retain any and all prior payments paid by Lessee;

(d) Lessor may declare all sums due and to become due under this Lease immediately due and payable, including as to any or all items of Equipment, without notice or demand to Lessee;

(e) Lessor may re-lease the Equipment to any third party, without notice to Lessee, upon such terms and conditions as Lessor alone shall determine, or may sell the Equipment without notice to Lessee, at private or public sale, at which sale Lessor may be the purchaser;

(f) Lessor may sue for and recover from Lessee the sum of all unpaid rents and other payments due under this Lease then accrued, plus all accelerated future payments due under this Lease, reduced to their present value using a discount rate of 6%, as of the date of default, plus Lessor's estimate at the time this Lease was entered into of Lessor's residual interest in the Equipment, reduced to present value at a discount rate of 6%, as of the date of default, less the net proceeds of disposition, if any, of the Equipment;

(g) To pursue any other remedy available at law, by statute or equity.

No right or remedy conferred upon or reserved to Lessor is exclusive of any other right or remedy herein, or by law or by equity provided or permitted, but each shall be cumulative of every other right or remedy given herein or now or hereafter existing by law or equity or by statute or otherwise, and may be enforced concurrently therewith or from time to time. No single or partial exercise by Lessor of any right or remedy hereunder shall preclude any other or further exercise of any other right or remedy.

LESSEE HAS READ AND AGREES TO ALL ITEMS ON THIS PAGE 3 OF 4 ____________________

Initials

22. MULTIPLE LESSEES. Lessee and each of them are jointly and severally responsible and liable to Lessor under this Lease. Lessor may, with the consent of any one of the Lessees hereunder, modify, extend or change any of the terms hereof without consent or knowledge of the others, without in any way releasing, waiving or impairing any right granted to Lessor against the others.

23. EXPENSE OF ENFORCEMENT. In the event of any legal action with respect to this Lease, the prevailing party in any such action shall be entitled to reasonable attorney fees, including attorney fees incurred at the trial level, including action in bankruptcy court, on appeal or review, or incurred without action, suits or proceedings, together with all costs and expenses incurred in pursuit thereof.

24. MISCELLANEOUS.
(1) LESSEE HEREBY ACKNOWLEDGES THAT THIS LEASE IS NONCANCELABLE FOR THE ORIGINAL RENTAL TERM SET FORTH IN EACH SCHEDULE.
(2) LESSEE UNDERSTANDS AND ACKNOWLEDGES THAT NO BROKER OR SUPPLIER NOR ANY SALESMAN, BROKER OR AGENT OF ANY BROKER OR SUPPLIER IS AN AGENT OF LESSOR. NO BROKER OR SUPPLIER, NOR ANY SALESMAN, BROKER OR AGENT OF ANY BROKER OR SUPPLIER IS AUTHORIZED TO WAIVE OR ALTER ANY TERM OR CONDITION OF THIS LEASE, AND NO REPRESENTATION AS TO THE EQUIPMENT OR ANY OTHER MATTER BY A BROKER OR SUPPLIER OR ANY SALESMAN, BROKER OR AGENT OF ANY BROKER OR SUPPLIER SHALL IN ANY WAY AFFECT LESSEE'S DUTY TO PAY THE RENTALS AND TO PERFORM LESSEE'S OBLIGATIONS SET FORTH IN THIS LEASE.
(3) Lessee authorizes Lessor, its successors, assigns and potential assigns, to obtain a personal credit profile from a national credit bureau for purposes of update, renewal or extension of credit and for reviewing or collecting this Lease.
(4) Any notices required by this Lease or the UCC shall be deemed to be delivered when a record properly directed to the intended recipient has been (a) deposited with US Postal Service, (b) transmitted by facsimile, (c) transmitted through the internet, or (d) has been personally delivered.

25. SEVERABILITY. This Lease is intended to constitute a valid and enforceable legal instrument. In the event any provision hereof is declared invalid, such provision will be deemed severable from the remaining provisions of this Lease, all of which will remain in full force and effect.

25. ENTIRE AGREEMENT; WAIVER. This instrument and the Schedules executed by Lessor and Lessee constitute the entire agreement between Lessor and Lessee with respect to the Equipment and the subject matter of this Lease. No provision of this Lease shall be modified unless in writing signed by an authorized representative of Lessor. Waiver by Lessor of any provision hereof in one instance shall not constitute a waiver of any other instance.

Lessee initials: ___________________

27. CHOICE OF LAW; JURISDICTION. This Lease shall not be effective until signed by Lessor at its principal place of business listed above. This Lease shall be considered to have been made in the state of Lessor's principal place of business and shall be interpreted in accordance with the laws and regulations of that state.

Lessee agrees to jurisdiction in the state of Lessor's principal place of business in any action, suit or proceeding arising out of this Lease, and concedes that it, and each of them, transacted business in the said state by entering into this Lease. In the event of legal action to enforce this Lease, Lessee agrees that venue may be laid in county of Lessor's principal place of business.

Lessee initials: ___________________

LESSEE:		**LESSOR:**	
____________________________________	**Date** ________	____________________________________	**Date** ________
____________________________________	**Date** ________		
____________________________________	**Date** ________		
____________________________________	**Date** ________		
____________________________________	**Date** ________		

NORDEN CAPITAL
LEASE SALES / BROKER MANUAL
PREPARED BY: ROBERT HOMANS

Objectives:

1. To provide guidelines to salespeople of leasing companies in identifying and qualifying potential lease clients.
2. Guidelines for Brokers and Lessors for preparation of credit packages.
3. To provide banks and other potential funding sources with information that they can use to identify potential lease brokers.

IDENTIFYING & QUALIFYING POTENTIAL LESSEES

2. IDENTIFYING POTENTIAL LESSEES:

ATCI Industry Emphasis – Agriculture & Food Processing

General Comment – The trick in leasing sales is to "be there when you are needed." This means that it is very important to maintaining a systematic approach toward developing prospects and maintaining a prospect list.

Vendors – Manufacturers and distributors of equipment used in agriculture, food processing and healthcare. Vendors can be found through the same contact lists as lessees.

Prospecting Directly to Lessees – Potential lessees can likely be found in the following locations: Industry associations; municipal and oblast registries; chambers of commerce; business listings, such as in Kompass; referrals from professionals, such as CPA's and attorneys; other USAID projects including FTF and the Agricultural Marketing Initiative. In addition salespeople should keep up with local business news, preferably from all parts of the country, as that is often a good source of information on companies moving, building a new facility, etc., that is often an indication of additional leasing needs.

There are also what may be called unconventional means of looking for potential lessees. If you have an industry concentration, such as in the Food and Beverage Industry for example, it is possible to go to supermarkets and take down names and telephone numbers of the companies producing the products carried in the market. Another example is seeing a delivery truck on the street.

Contacting Prospective Lessees – Prospective lessees are usually contacted by phone, by letter, or letter followed up by a phone call.

2. QUALIFYING POTENTIAL LESSEES

Before seeing any financial information potential lessees can be qualified, usually through a telephone conversation, and then added to a lessee prospect list. "Qualified" lessees would include the following, including suggestions on how to get the information:

Vendor Referrals –When the vendor calls and makes a referral the following questions should be asked, of the vendor, in the approximate order given:

- **What type of equipment, how much does the equipment cost, when it is to be delivered, any special needs such as progress payments, and if there are additional equipment requirements** – Before contacting the prospective lessee you will want to know as much as possible about the type of equipment he is acquiring, how much it will cost and when it is to be delivered. The latter is important because you want to know how much lead time the vendor is going to need, to place the order, etc. This information is also important with respect to the financial information you are going to ask the lessee. For example, if there is a 6 month lead time and a progress payment is required, you are going to have to tell the lessee that he will need to provide follow-on financial information in order to maintain the credit approval status.
- **What is the vendor's customer's business?** – Find out a bit about the company, especially how long they have been in business, what their product is, where they sell their product, etc. This will become useful information, when you put together the credit package.
- **Why is the vendor's customer getting the equipment** – This is very important information. Is the lessee getting the equipment to cut operating costs, to replace existing equipment, to add a new product line?
- **Is the lessee buying other equipment, from this vendor, or perhaps other equipment from other vendors**? – If you are getting the referral from the vendor, it is helpful to find out as much as possible about the lessee's equipment acquisition plans.

Lessee Prospects – This section will provide a guide to calling on lessees, either direct calls or follow up calls resulting from vendor referrals. Prospecting directly to lessees is normally done either by phone contact, by a letter, or a letter followed up by a phone call. Results of prospecting calls will populate your Prospect List, described below. A more detailed "Phone Call Checklist, is included in this Manual as Appendix 1. For calling, the following procedures listed in order, are useful:

- **Initiating Call –** Before calling, it is helpful to know the name of a person to contact, preferably the General Director or the Finance ("Commercial") Director. It is very important to call a decision maker. Sometimes the Plant Manager/Plant Engineer is also a useful contact, especially since he/she is going to know if the company has any equipment needs and may well have an input into what those needs are. If you talk to a Plant Manager you have to decide whether or not he/she is a decision maker. If they are not a decision maker, ask him or her to refer you to someone who is, and get transferred to their extension or start the call over again. A sales or marketing person is not a good person to call, because he or she is likely not a decision maker unless there are some special circumstances such as being married to the President, etc.

- **Be Direct –** State the purpose of your call. For example, "My name is __________ from XYZ leasing company. The purpose of my call is to identify manufacturers in the Food & Beverage Industry who are considering acquiring equipment, in order to perhaps help out with their financing needs." There will be several possible outcomes to this call, including:
- **Possible Outcome: Lessee Has No Interest –** Thank the prospect for his time, perhaps ask him/her if it is OK to send some information.
- **Possible Outcome: Lessee Says He Has No Interest but Says Something to Indicate That He Might Have Equipment Needs –** One example might be if a lessee says he has no interest, but also says business is very good and he may be expanding to a new location. Ask some questions about the expansion plans. Is it going to include acquisition of equipment? It is important to keep in mind that education about the value of equipment leasing, among lessees, is very limited in Ukraine. The prospect might be telling you he has no interest, but this might also be the first time he/she has ever considered leasing. A prospect like this should be added to the prospect list.
- **Possible Outcome: Lessee Expresses an Interest, but not for several months, or 1 year –** In this case ask the lessee when would be a good time to call him/her again, and ask to send information. Contacts such as these should go into the Prospect List with a note in the "tickler file" to follow up with the prospect at the appointed time.
- **Possible Outcome: Lessee Has a Current Interest in Buying Equipment and is Considering Leasing –** Find out what the equipment is, what it costs, and approximately when the equipment is to be delivered. Ask about the lease terms he is considering – make the prospective lessee believe he is designing his own financing package. Find out a bit about his business, including how long the company has been in business, products they sell, what the ownership is, general idea of sales & profits. You are trying to "pre qualify" the lessee, prior to asking for financial information. Assuming that there is nothing that the lessee said that contains a potential problem, it is appropriate to send the prospect some general ideas of payment information, as well as a list of financial information you are going to need, in order to prepare a credit package for submission.

2. MAINTAINING LESSEE, INDUSTRY & VENDOR PROSPECT LISTS

The prospect list is a list of potential lessees who have indicated either a current, or potential, leasing need. A lessee prospect list is best kept on contact management software, such as ACT! for Windows, Goldmine, or Microsoft Access. In ACT!, there is a section allowing the user to schedule calls, along with a space for notes where it is possible to include brief notes on what was talked about. If a prospect was contacted about a specific lease transaction, and an estimate was sent, it is useful to include the pricing information in this space, as well as a date/time to check back.

In addition to a prospect list, it is important to keep a separate list(s) by industry, as well as a vendor list if you are planning to call on vendors. Companies in the industry list are usually companies who have expressed a general interest, but have no specific, immediate, needs. The industry list also includes companies that have been added, as the result of going to a trade show, seeing a delivery truck on the street. Companies in the Industry List should be contacted at least twice/year. Lessors should maintain industry lists for each target industry.

If vendor referrals are the primary source of business, a vendor list might be incorporated into the prospect list. In ACT! you have the ability to include 2 or more Groups in 1 database. In a prospect list, one group could be lessees, and another group would consist of vendors.

Stay in Regular Contact With Names on the Prospect List – The first trick of successful selling in the leasing industry is to be there when you are needed. In order to do that it is necessary to keep in touch with prospects on a regular basis.

Keep Adding to the Industry/Vendor Lists – The second trick of successful selling in the leasing industry is that it is a “numbers game.” The more calls that are made, the more leases will be completed. The more good prospects in the Industry & Vendor Lists, the better the “numbers game” will work.

Update Prospect List – If a lessee no longer appears to be interested in leasing equipment, remove the company from the prospect list. If companies in the Industry or Vendor lists, become actual prospects, or refer actual prospects respectively, these should be added to the Prospect List. The Prospect List should be reviewed on a regular basis, to make sure it is up to date, with every entry having a scheduled call back date.

PREPARATION OF CREDIT PACKAGE

A "Model Credit Package" is included in this manual, as Appendix 2.

Objectives of Credit Package – 1. Credit Package should be as complete as possible; 2. Credit package should show how the proposed lease request will be repaid.

Package Should be as Complete As Possible – Lessor salespeople and Brokers should put themselves in the shoes of the Credit Officer who will be reviewing the package. The objective of the person preparing the credit package should be to try to address any potential questions that may be raised by the Credit Officer. The specific elements to be included in a credit package are listed below.

How Will the Proposed Lease be Repaid –

- **Primary Repayment Source –** Historical cash flow of lessee.
- **At Least One Secondary Repayment Source –** Benefits of equipment (cost savings, additional revenue, or a combination), liquidity of lessee; liquidity of guarantor(s); vendor buyback. In Ukraine, secondary repayment source(s) may be as, or more, important than the primary repayment source, due to short time in business of most lessees.

Elements of Credit Package –

- **Completed Leasing Service Application (Prepared on Lessee's Letterhead).**
- **Completed "Lessee Questionnaire."**
- **Completed Credit Write up –** Examples of credit write ups are included in the Model Credit Package. A complete credit write up should include the following:
    - **Important Names and Contact Information –** For lessee and broker.
    - **Amount of Lease Request, Requested Term, Approximate Periodic Payments.**
    - **Summary Analysis of Primary Repayment Source –** Taken from detailed Financial Statement Analysis (see below).
    - **Discussion of Lessee's Liquidity –** Any sources of liquidity, available to repay the lease, not otherwise included in the Summary of Primary Repayment Source (cash position on balance sheet, guarantor(s) liquidity, etc.)
    - **Discussion of Secondary Repayment Sources.**
    - **Discussion of "Other Credit Matters" –** Other Credit Matters include anything that might effect the lessee's ability to repay the proposed lease, including any pending lawsuits.
    - **Summary of Financial Statement Analysis –** Example included in Model Credit Package.

  Completed Financial Statement Summary – Example included in Model Credit Package.

  All Items Requested In Lessee Questionnaire – In the order listed in the Lessee Questionnaire.

Управление рисками в агросекторе

Риск – это вероятность получения убытков в результате влияния неблагоприятных факторов

Однако !!!

Оправданный риск помогает занять конкурентную позицию на рынке и получить дополнительную прибыль

Основной задачей клиент-менеджера является адекватная оценка заемщика, потенциальных рисков и возможной прибыли клиента

Основные группы рисков для производителей

Изменения в законодательстве

Недополучение запланированного количества (качества) продукции (урожайность культур, продуктивность скота)

Нестабильность цен

Потеря трудоспособности собственника или квалифицированного персонала

Роль разных факторов в потерях урожая

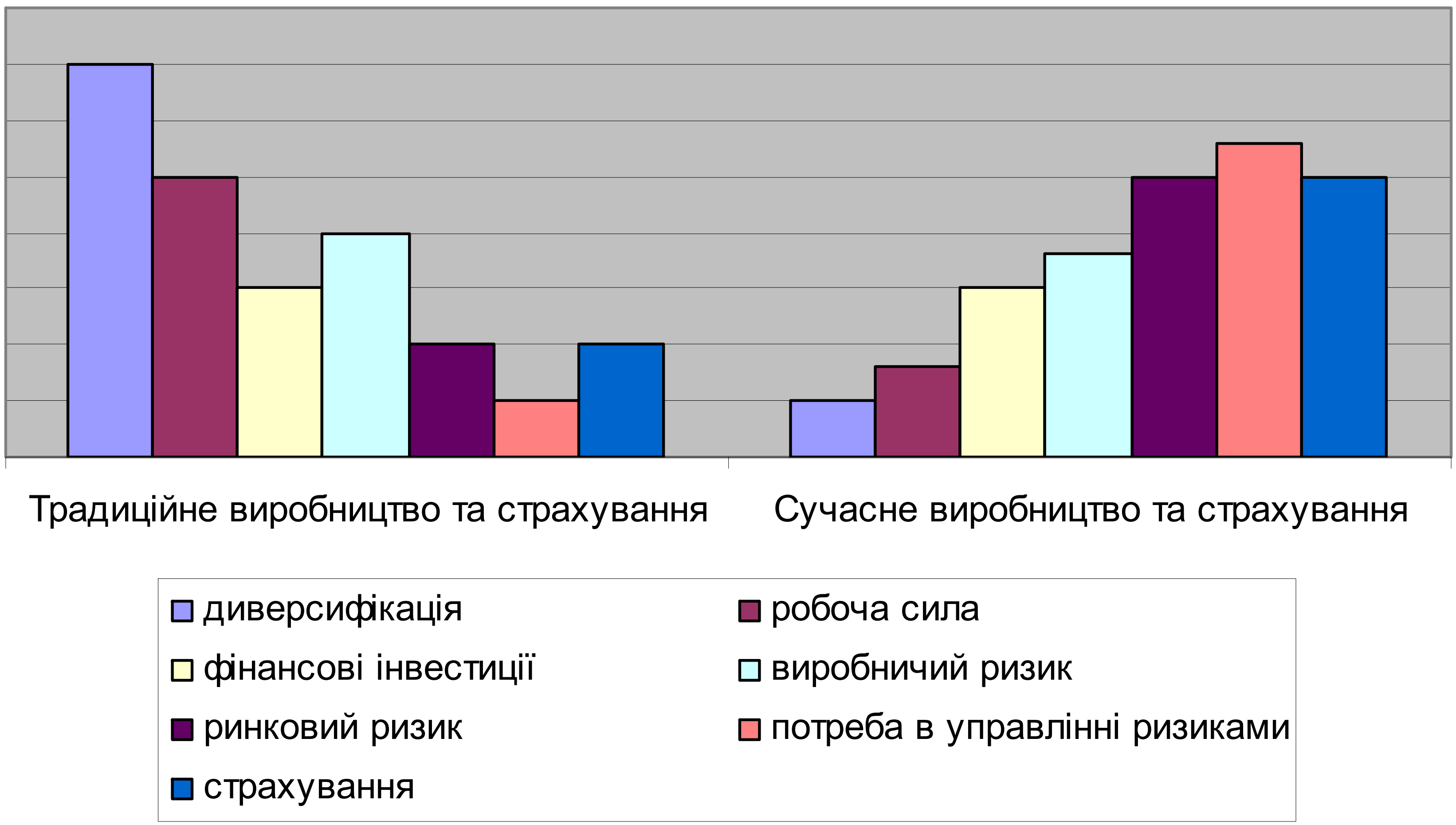
заболевания - 17%

вредители - 10.2%

сорняки - 14.4%

Погодные факторы - 58.4%

Развитие структуры сельскохозяйственного производства и потребность в риск менеджменте/страховании



Урожай картофеля, пораженный 15 минутным градом 1-го июня 2002 в предприятии Деснянское

Сорт: Леди Розета

Типы рисков

Допустимый – недополучение части прибыли

Критический – ущерб от рискового события может равняться или превысить прибыль предприятия

Катастрофический – риск, который может привести к неплатежеспособности предприятия и отсутствию средств для погашения задолженности

Категории рисков

Производственные риски – получение планируемого количества или качества продукции

Рыночные – производство конкурентной продукции и ее эффективная реализация

Финансовые риски – управление финансовыми ресурсами, правильный расчет стоимости производственных ресурсов и тщательное планирование финансовых результатов

Юридические и законодательные риски – контрактные отношения, аренда, использование лизингового имущества, выполнение требований законодательства

Человеческий фактор – адекватная структура предприятия, наличие достаточных ресурсов, репутация

Управление рисками

Производственные риски – диверсификация (специализация), новые технологии, производственные контракты, страхование, наличие МТР

Рыночные – маркетинговый план, упаковка/предпродажная подготовка, прямые продажи, вертикальная интеграция, хранение

Финансовые риски – наличие финансов (кредит), процентная ставка и валютные риски, оптимизация затрат, ликвидность, цены реализации

Юридические и законодательные риски – исторические риски, контрактные отношения, риски управления персоналом, законодательные требования (экология, гражданская ответственность, др.)

Человеческий фактор – структура управления, персонал, партнеры

Эффективность стратегий в порядке убывания (производственные и рыночные риски):

(1) Комбинация хеджирования (использование форвардных и фьючерсных контрактов) и страхования

(2) Страхование дохода

(3) Страхование урожая

(4) Хеджирование

(5) “нулевой” вариант

Примерная прибыльность сельскохозяйственного производства (многолетняя за 5 лет):

Зерновые – 40%

Технические культуры – 20-50%

Масличные культуры – 40-70%

Овощи – 30 – 150%

Фрукты – 30-100%

Мясо – 20-50%

Молоко – 20-50%

Страхование как инструмент по управлению рисками в агробизнесе

Страхование

Суть страхования – передача большей части (стоимости) риска другой стороне за определенную плату на оговоренный срок и на определенных условиях

Функции страхования:

– стабилизация доходов предприятия

– обеспечение выполнения долговых обязательств

– обеспечение выполнения договорных обязательств (поставка сырья, продукции)

– позволяет повысить уровень специализации предприятия

- стабилизация производства и уровня цен

Агрострахование в Украине

- 10-15 компаний работают в сегменте;

- только несколько компаний стабильно собирают премии во всех областях;

- страхуется не более 2,5% площадей;

- 2% сельхозпроизводителей страхуют культуры

- 6,4% озимых застраховано в 2005 году;

- средний тариф по озимых – 3,8%

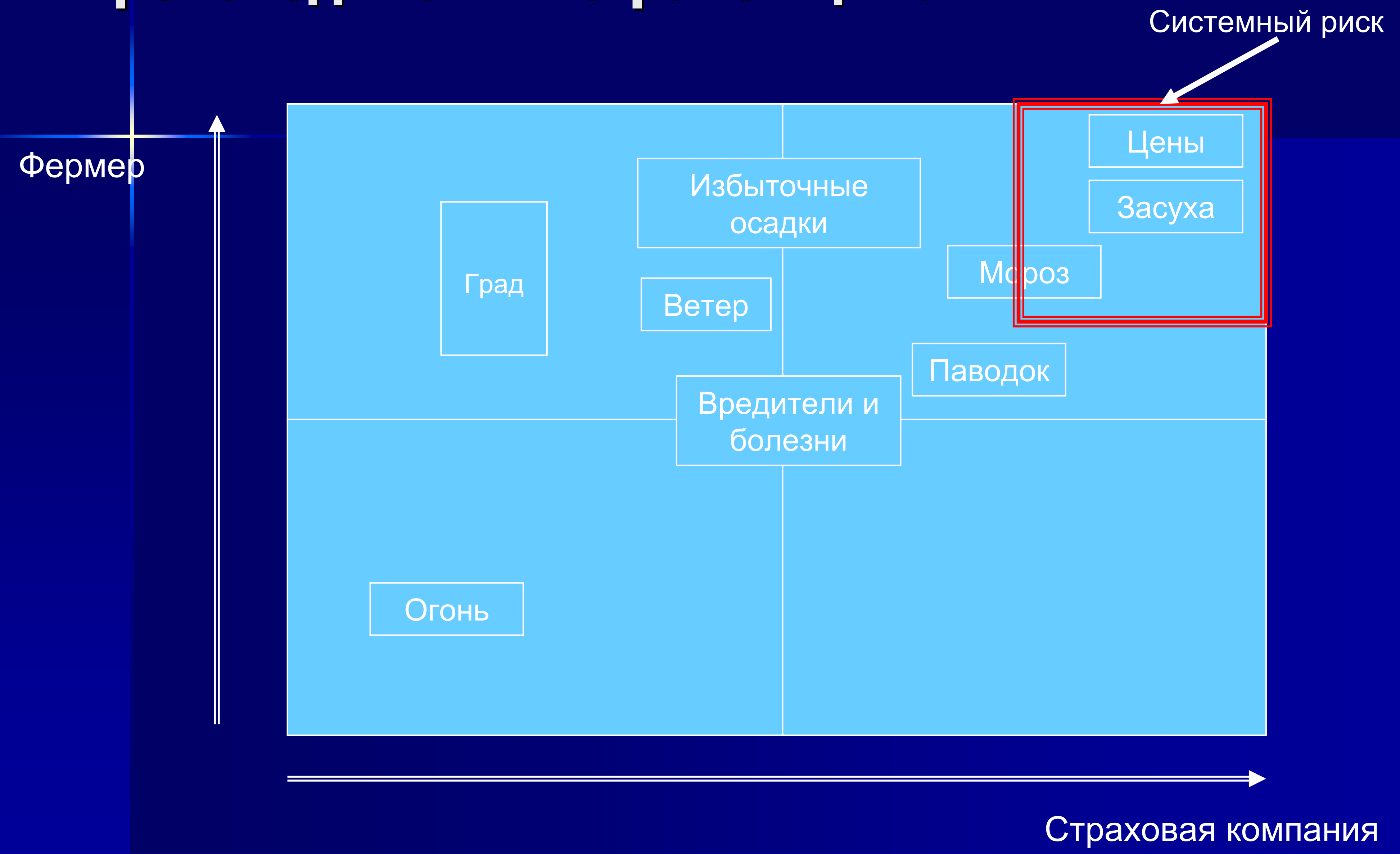
- формальное страхования

- субсидирование премий государством

Основные риски для агропроизводства

Град	Страхование от града является самым развитым видом агро страхования и часто предлагается как отдельный продукт
Вода - паводок - засуха - Избыточные осадки	Паводок, засуха и избыточные осадки имеют наибольшее влияние на производство сельскохозяйственных культур
Огонь	Риск вогня является одним из менее значимых по влиянию и последствиям (ущерб)
Температура	Температура сильно влияет, так как может быть очень высокой (засуха, суховеи, температурный стресс) или очень низкой (заморозки, мороз зимой)
Ветер	Сильный ветер может вызвать большие убытки у производителей овощных и технических культур, а также в садах
Биологические риски - сорняки - вредители - болезни	Биологические риски сильно влияют на производство. Они зависят от менеджмента предприятия и часто их влияние увеличивается на растения, которые пострадали от других рисков. В большинстве случаев этими рисками можно управлять технологически

Потенциальное влияние рисков на производителя и страховщика



Что можно застраховать?

- Сумма затрат на производство
- Ожидаемая стоимость продукции
- Ожидаемый доход (прибыль) от продажи произведенной продукции

Продукты страхования

- Один или несколько рисков
- Комплексное страхование (мульти-риск)
- Индексное страхование (погода, урожайность)

Альтернативные инструменты по управлению рисками

- Диверсификация
  - Производство разных культур
  - Растениеводство + животноводство
  - Разные сроки получения продукции
  - Географическая диверсификация
  - Получение доходов из разных источников
- Новые технологии
- Производственные контракты

Основные технические условия страхования

Страховая стоимость – стоимость продукции (цены реализации, оценочная, договорная)

Страховая сумма – сумма, в пределах которой, страховщик обязывается провести выплату в случае наступления рискового события

Франшиза (безусловная) – часть убытков, которая не компенсируется страховщиком

Покрытие – процент урожая, в рамках которого страховщик гарантирует компенсацию убытков

Премия – плата, которую страхователь обязывается заплатить за услуги страхования

Страховая премия

Простое сравнение уровня тарифов, которые предлагают страховые компании, является недостаточным для сравнения условий страхования. Рекомендуется расчитывать “внутренний” тариф :

$$"Внутренний"\,тариф = \frac{Сумма\_премии}{Максимальная\_выплата} \times 100\%$$

Практика показывает: при покрытии 80% и франшизе 20%, внутренний тариф отличается на 1,3-1,4% в большую сторону при франшизе, т.е. страхователь должен платить больше за ту же услугу страхования

Виды страховых продуктов для производителей сельскохозяйственной продукции

- Страхование затрат на производство
- Страхование перезимовки культур
- Страхование урожая
- Страхование дохода
- Страхование от одного или нескольких рисков
- Индексное страхование (погода, урожайность)
- Комплексное страхование (мульти-риск)
- Государственное субсидирование страхования

Sales and Risk Assessment in Agricultural Leasing

Presentation by:

Thomas W. Meade

Farmer-to-Farmer volunteer

USAID
FROM THE AMERICAN PEOPLE

CNFA

IDENTIFYING CLIENTS AND SELLING THEM ON LEASING

Finding potential leasing clients:

- **Identifying potential clients**
  - equipment suppliers; parts suppliers and repair shops
  - farm size
  - types of products

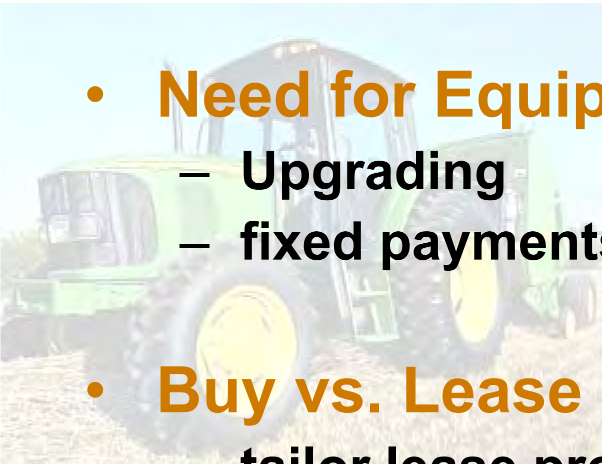
- **Visit potential clients**
  - farms / banks / equipment suppliers & dealers
  - business agreements with suppliers / dealers. Is commission paid?
  - suppliers / dealers guide lease business to lessor company

- **Regional / oblast leasing seminars / meetings**

Benefits & incentives of leasing:

- **Asset management**
  - use of equipment
  - fixed payments
- **Customized solutions**
  - tailor lease program to fit lessee's cash flow needs
- **Flexible end of lease options**
  - return, re-lease, purchase equipment
- **Business flexibility**
  - business grows and lessees need to change equipment
- **Improve cash forecasting**
  - equipment expense is known for future planning

Overcoming Objections



- **Need for Equipment**
  - Upgrading
  - fixed payments
- **Buy vs. Lease**
  - tailor lease program to fit lessee's cash flow needs
- **Cash flow benefits versus pricing**
  - return, re-lease, purchase equipment
- **Access to Additional Financing**
  - business grows and lessees need to change equipment

Understand your client's business:

- **Different types of farms**
  - varying technological levels
  - appraise and analyze farms of different types
  - In Ukraine, be sure you understand the client’s land rights sooner rather than later

- **Be flexible and understanding of client**
  - smaller farms also need equipment

- **Smaller clients can be the BEST clients**
  - they will appreciate the help to them
    - maybe better at making lease payments on time
    - equipment better cared for and less usage
    - maybe better resale value at lease end

  - consider crop yields, contract tillage and harvesting, etc.
    - farm vs custom (for hire) operator
    - does farm also have livestock operation for cash income

Documentation and preliminary credit analysis of client:

- Client completes credit application
- Supplies credit references from suppliers
  - fuel, seed, equipment, etc.
- Client's standing with client's bank
  - good or not good
- Most recent financials
  - Two years minimum is desirable

Difference in working with

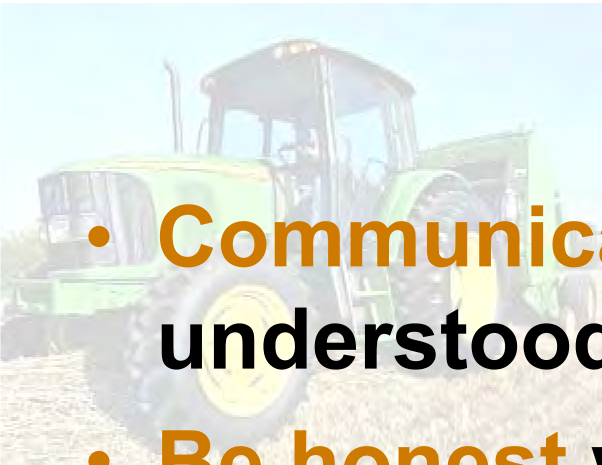
new

and

repeat

clients

NEW CLIENTS



- Communication is KEY – everything is understood
- Be honest with client
- Be clear - lessor expects honesty from lessee

REPEAT CLIENTS

Lessor has a history with repeat clients

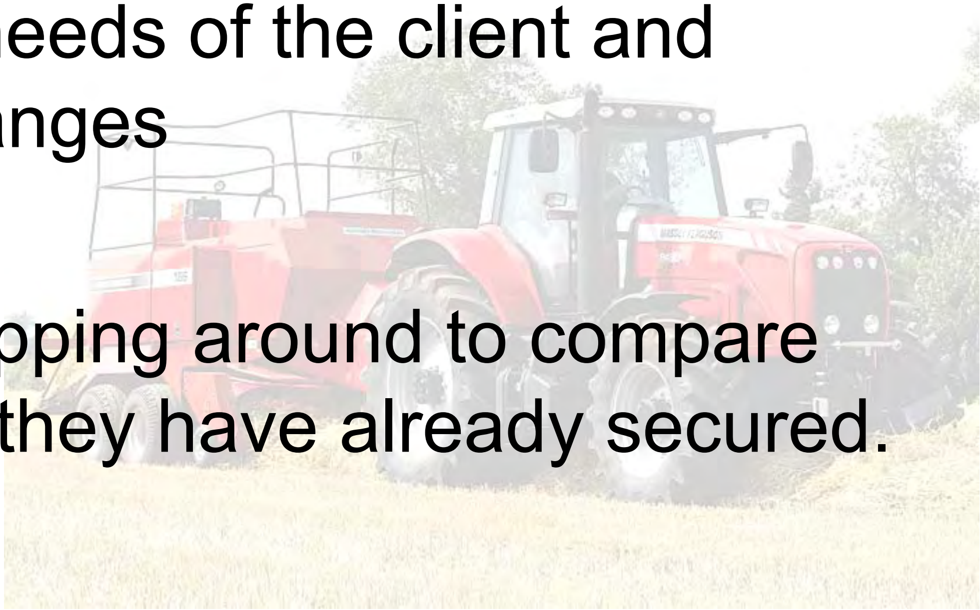
- **If good history**, do more business
- **If bad history**, try to repair business misunderstandings
- **If not repairable**, say good-bye nicely
  - maybe do business again in future

Major Risks at this Stage

Spending time on bad leads, prospects

Pre-qualifying prospects that will get turned down

Not understanding the needs of the client and therefore the deal changes

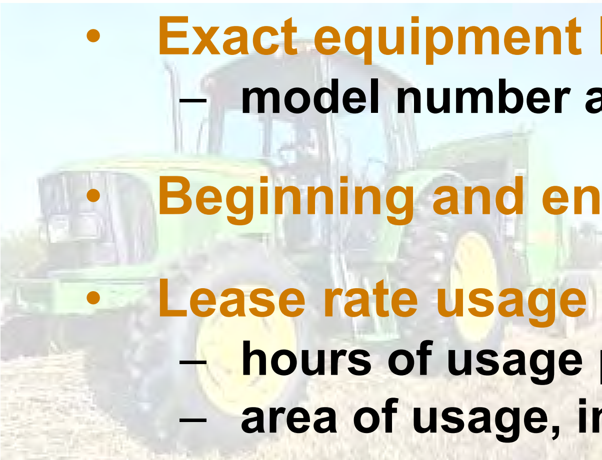


Clients that are just shopping around to compare pricing with financing they have already secured.

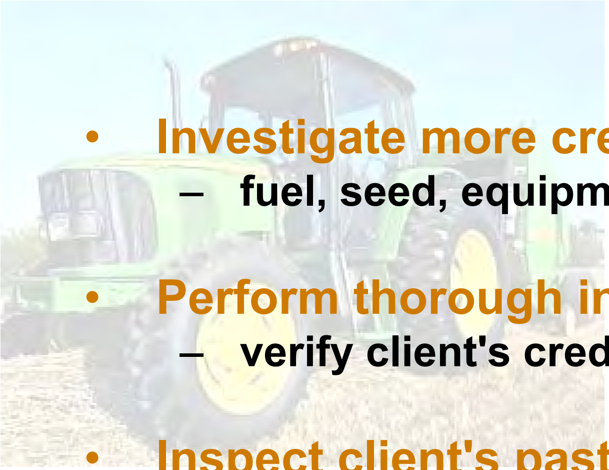
Assessing the Client and Structuring the Transaction

Equipment lease proposal specifies:

- Exact equipment being leased
  - model number and serial number
- Beginning and ending dates of lease
- Lease rate usage restrictions, if any
  - hours of usage per year
  - area of usage, in Ukraine only, etc.
- Advance payment required
  - periodic payments: monthly, quarterly, annually
- Payment due for excess usage
- Purchase option price at lease end
- Miscellaneous terms of the agreement
  - excess wear and tear (or usage)
  - evidence of insurance – protect lessor



Documentation and credit analysis of client:



- Investigate more credit references
  - fuel, seed, equipment, etc.
- Perform thorough investigation of client's credit history
  - verify client's credit worthiness
- Inspect client's past tax records?
- Client's standing with current and past banks
  - good or not good
- Past work financial results for 3 to 5 years
- Any future financial projections that the client may have (optional)

Lessor's internal procedures and company staff:

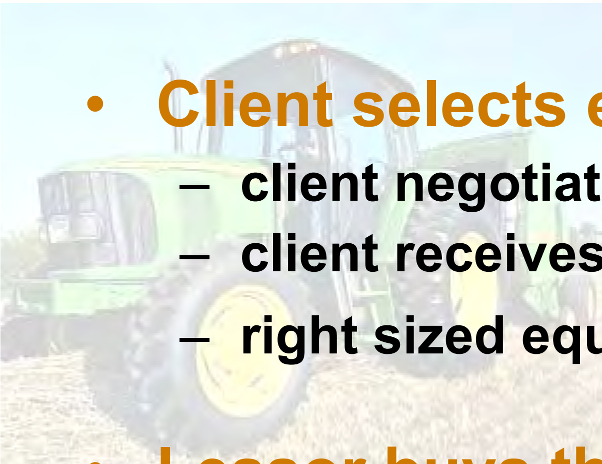
- Have a very good and experienced company credit manager
  - evaluate client's credit worthiness
  - approves lease agreement

- Have a farm equipment expert / manager
  - knows the value of new and used farm equipment
  - sets the residual value of equipment returned at lease end
  - sells equipment returned at lease end
  - finds equipment for lease if needed

- Have leasing sales people that understand farm equipment
  - good communication with clients
  - understands client's needs and desires

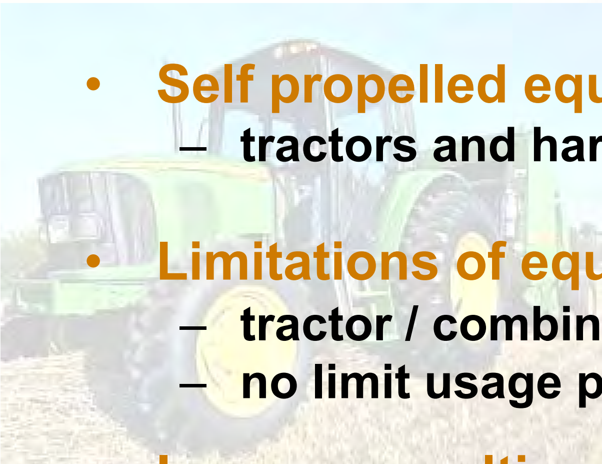
- Security people
  - collect past due lease payments
  - repossess equipment if needed

Choice of equipment options:



- Client selects equipment
  - client negotiates delivered price from supplier
  - client receives repair parts and service from supplier
  - right sized equipment for projected work
- Lessor buys the equipment from supplier
- Establish lease payments
  - payments based on equipment price and lease time period
  - residual amount if any
  - miscellaneous lessor expenses
  - lessee may buy equipment at lease end

Specifics of leasing farm equipment:



- Self propelled equipment versus non-self propelled equipment
  – tractors and harvesters have hour usage clocks
- Limitations of equipment usage
  – tractor / combine lease payments may have usage limits
  – no limit usage payments should be higher
- Impose penalties for over usage
- Require safety measures in lease agreement
  – fire extinguishers in tractors and harvesters
- Require storage conditions in leased agreement
  – equipment stored in secure guarded building
  – parts not stolen
  – preserve equipment appearance for resale at lease end

Client income from leased equipment:

- Projected usage of leased equipment
  - hours of use, hectares to harvest, etc.
  - right lease payment for amount of usage

- Estimate income from leased equipment
  - equipment right size for projections

- Can lessee afford the lease payments?

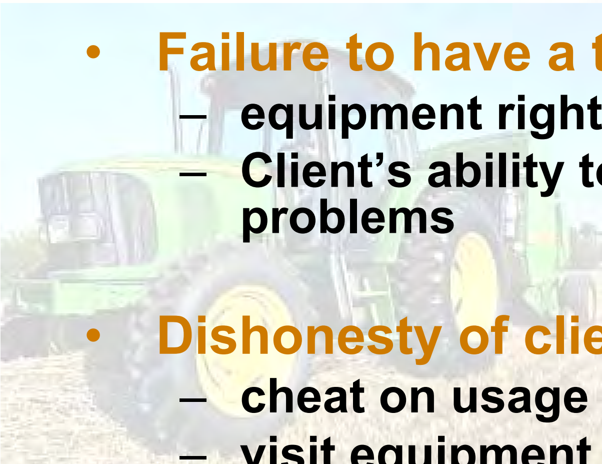
Types of leases:

- **Operating lease**
  - lessee has the usage of equipment
  - lessor may be responsible for maintenance and repairs
  - lessor owns equipment at lease end
- **Financial lease**
  - lessee responsible for maintenance and repairs
  - lease to own equipment
  - payments based on lease end residual amount
- **Optional refundable security deposit**
  - pays for unreasonable work usage and equipment damage (glass, etc.)
    - suggest 1 - 5% of total lease amount
- **First lease payment due before first usage**

Equipment insurance:

- Protect lessor's investment
  - lessee provides proof of insurance to lessor
  - protection from fire, theft, physical damage
- Hold lessor blameless
  - personal injury of client and employees by equipment
- Insurance provided by lessor
  - include lessor paid insurance in lease payments

Major risks at this stage:



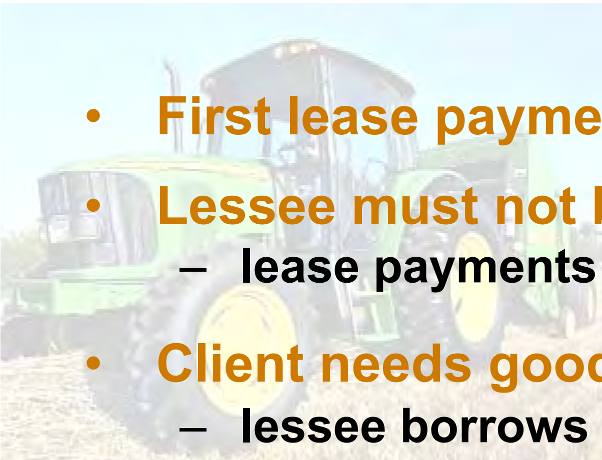
- **Failure to have a thorough knowledge of client**
  - equipment right for the client's work
  - Client's ability to do what they say and deal with unexpected problems
- **Dishonesty of client**
  - cheat on usage - disable hour clock on tractors / combines
  - visit equipment when working, unannounced and SEE clock working
  - accuracy of information provided
- **Client's affordability of lease**
  - enough work and income for desired equipment
- **Equipment is properly insured to protect lessor**
- **Equipment is treated badly by lessee**
  - poor sale value at lease end or repossession

MONITORING YOUR LEASE AND EQUIPMENT

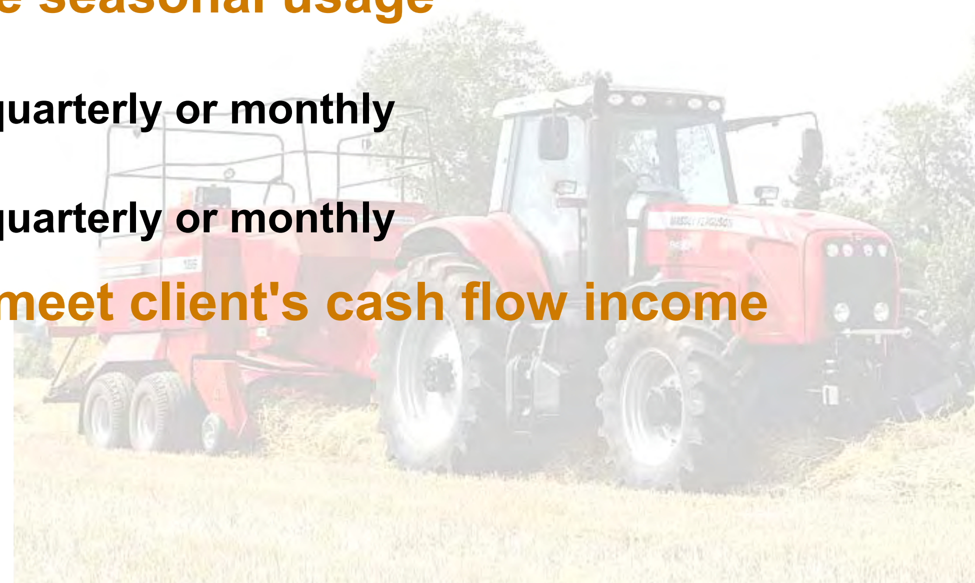
Monitoring client and leased asset:

- Go see client and equipment
  - unannounced visits: 2 or 3 times a year to inspect equipment
    - inspect equipment while working
    - hour clock working on tractors and combines
  - equipment in good condition – inspect for damage
  - equipment stored property
  - parts missing from equipment
  - fill out inspection report: clock hours, damage, etc.
  - take photos, especially of damage
- Client will know you are watching him and equipment
  - lessee will take better care of equipment
- Equipment in better condition at lease end
  - better resale value
  - bad equipment will sell for junk price at lease end
- Higher-risk clients
  - more inspections – more often
  - more communication

Collection of lease payments:



- First lease payment paid before first usage of equipment
- Lessee must not be allowed to "get ahead" of lease payments
  - lease payments must be paid ON TIME
- Client needs good banker
  - lessee borrows money from bank to make payment on time
- Lease payments due before seasonal usage
  - harvesters and tractors
    - annually, semiannually, quarterly or monthly
  - planters and tillage tools
    - annually, semiannually, quarterly or monthly
- Design lease payments to meet client's cash flow income
  - livestock and dairy farms
  - custom grain harvester



Maintaining client relationships:

- Be honest with client
- Lessor tells client that lessor expects honesty from lessee
  - communication is KEY
  - no surprises with lease payments from client
- Schedule client visit shortly before lease payment is due
  - talk about any problems
  - collect the lease payment money

Tax rules:

- Tax rules are always changing
  - lessor and lessee talk to professional tax advisers

Major risks at this stage:

- **Fail to monitor client and equipment**
- **Fail to collect lease payments on time**
- **Fail to maintain a good relationship with client**
  - **communication is KEY**

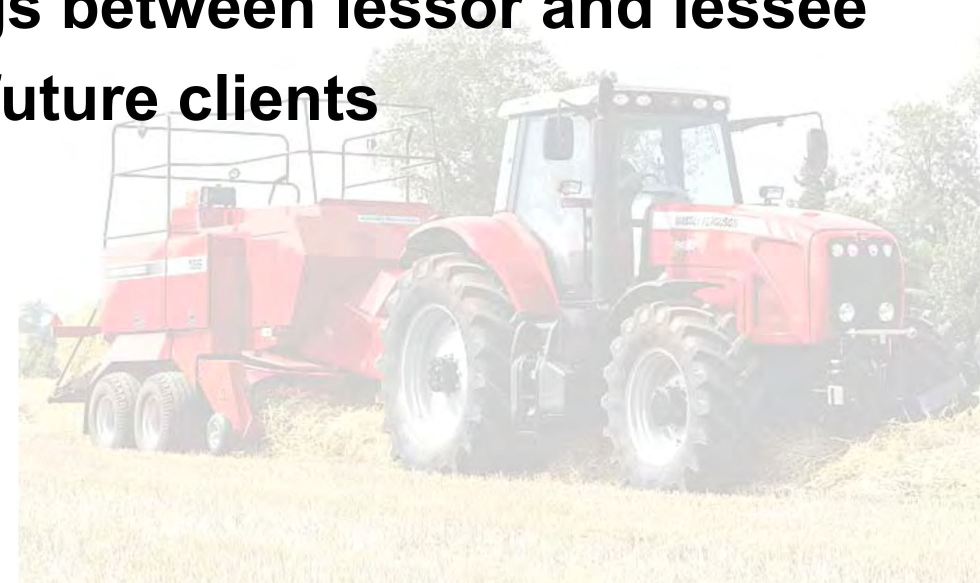
MANAGING CONFLICT SITUATIONS

Late or no lease payments:

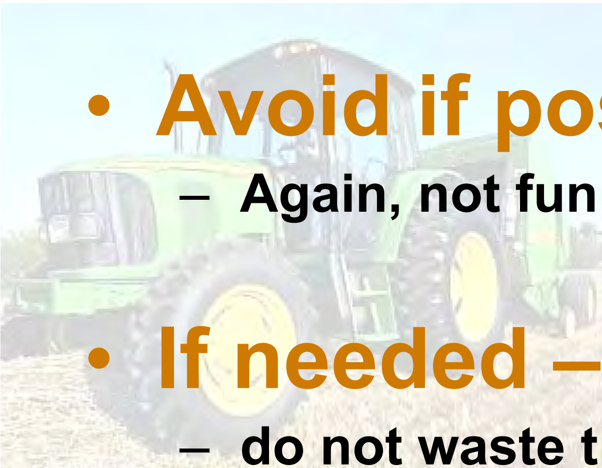
- Lessor WILL be in this situation - sooner or later it will happen...
  - PLAN AHEAD – have plan of action ready
    - to collect lease payment
    - to repossess equipment if needed
- Communicate with lessee
  - what is the problem
- Client payment sources:
  - from bank
  - from client's accounts receivable
  - sell grain or livestock to get payment money
  - lessor takes grain or livestock for lease payment

Litigation:

- Avoid litigation if possible
  - not fun to do
  - is expensive to do
  - causes hard feelings between lessor and lessee
  - bad advertising to future clients



Repossession of leased asset:



- **Avoid if possible**
  - Again, not fun to do
- **If needed – do as quickly as possible**
  - do not waste time
  - equipment may disappear
  - parts may be taken from equipment
  - if angry lessee may damage equipment on purpose
    - run engine with no oil – very expensive to fix
    - cut tires
    - break glass
  - this is the reason for the security deposit

Sale or disposal of repossessed equipment:

- Fix any damage to equipment
  - Clean up? Repaint? New tires? Make it look good!
- Advertise for sale at fair value
- Possible lease again

END OF LEASE

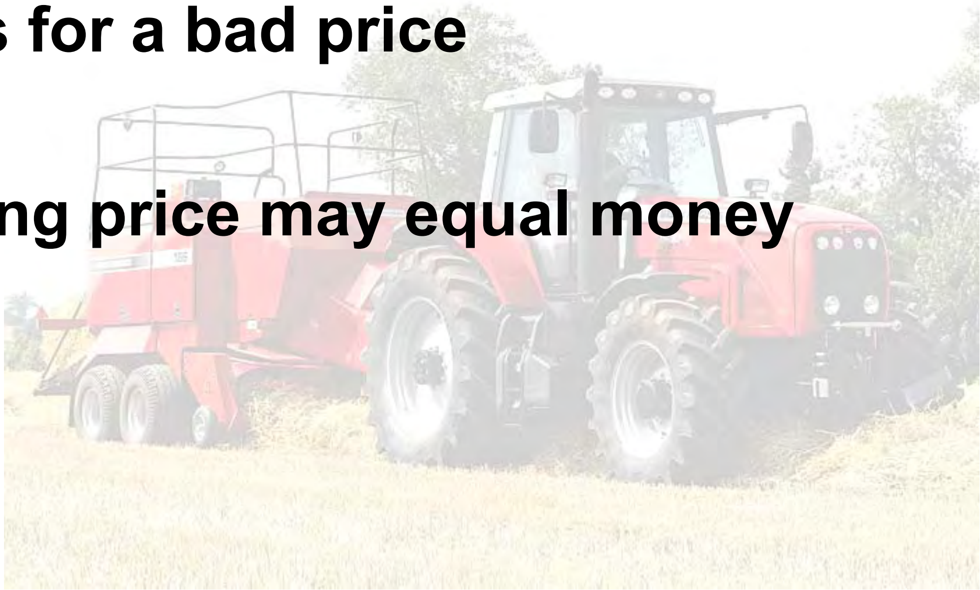
Equipment options:

- **Operating lease**
  - offer sale of equipment to lessee at fair market value
  - sell equipment on open market
  - lease equipment again

- **Financial lease**
  - lessee can own equipment at predetermined price
  - sell equipment on open market
  - lease equipment again

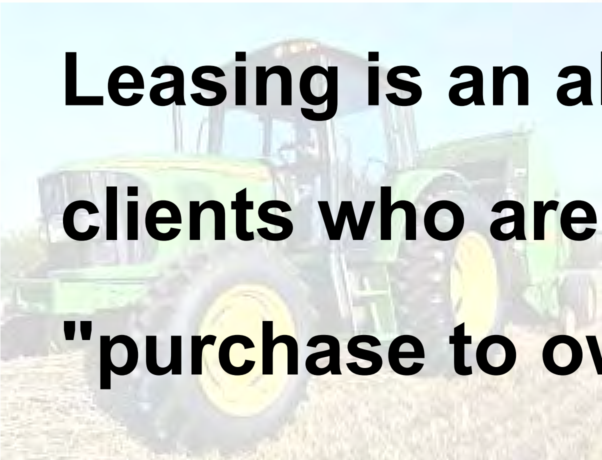
Major risks at this stage:

- Equipment condition
  - equipment returns from lease in bad condition
    - equipment not worth residual value
  - bad equipment sells for a bad price
  - bad equipment selling price may equal money LOST on lease deal



LEASING WORKSHOP SUMMARY

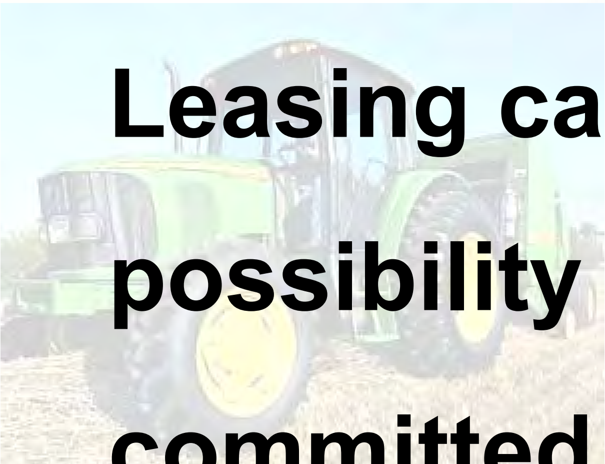
SUMMARY



Leasing is an alternative form of financing for clients who are not in position for a conventional "purchase to own" equipment acquisition.

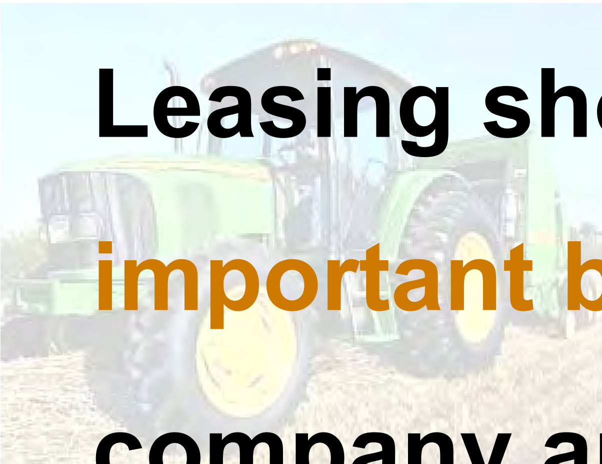
Leasing is particularly good for the agricultural based client who does not have the collateral to finance the purchase of equipment.

SUMMARY



Leasing can be a BIG business, possibility with many millions of UAH committed to the leasing program, BUT this business must be managed with great care.

SUMMARY



Leasing should be considered a very **important business** by the parent company and should have very **qualified employees**.

Leasing can be a very **profitable** business **if properly managed**.

KEY factors for a successful leasing business:

- parent company commitment to the leasing business
- commitment to FIRM leasing business practices and plans
- good quality leasing company employees
- honesty with clients
- good communication with clients
- respect for clients and their needs
- earning client's respect and honesty
- collect the money ON TIME

Thank You !!!

ATTACHMENT 10

TRIP REPORT March 15, 2006

Volunteer: Thomas W. Meade

Host Organizations: Amako, Ukrainian Leasing Company, Leasing House,
Access to Credit Initiative (ATCI)/Pragma Corp.

Date: February 25, 2006 - March 16, 2006

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THE ATCI/CNFA WORKSHOP

Kiev, Ukraine

March 2 and 3, 2006

Volunteer assembled information at home prior to arrival in Kiev...then presented the information at a two-day Workshop...conducted by ATCI/Pragma/CNFA on March 2 and 3, 2006...to approx. 20 leasing company personal from approx. 15 leasing companies. Volunteer's workshop material covered the following subjects:

1. Managing risks of agribusiness portfolio
2. Risk mitigation strategies
3. Principles of risk assessment and rating
4. Knowing client needs
5. Sales marketing tools
6. Desirable lease salespeople skills
7. Principles of client management
8. Client and leased equipment monitoring
9. Risks of dealing with agribusiness clients
10. Stressed ON TIME management of ALL aspects of the leasing business

Volunteer believes the Workshop was conducted in a very good and professional manner by the ATCI/Pragma/CNFA personnel...and was very well received by the Ukrainian attendants.

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UKRAINIAN LEASING COMPANY - ULC

Meetings with ULC held on March 4 and 6, 2006.

Saturday...March 4,2006....met with the Ukrainian Leasing Co (ULC).
Sasha and Andriy were at this meeting.

Nikolay Soroka, who was at the ATCI/Pragma seminar for the 2 days...was the host of the meeting. There were approx. 10 ULC people attending the meeting...managers from about 6 different areas of Ukraine.

Nikolay said he wanted Tom to do an abbreviated version of the Pragma seminar....go through the BPs of the seminar...and they would ask questions on subjects that were of interest to them. We did that....meeting lasted approx. 4.5 hours.

Members of ULC asked many relevant questions on ALL aspects of the "farm equipment leasing business". They asked how things were done in the USA....we covered a LOT of ground....it was a good meeting.

We met again on Monday, March 6, 2006....for further discussions.

Meeting was at the Ukrainian Leasing Company's office....same as Saturday.

The meeting was with Nikolay Soroka, Manager of the Agricultural Lease Business.

Sasha...my interpreter...and I went through the CNFA supplied Check-list of suuggested topics to discuss with Nikolay. Some subjects covered were:

1. ULC has 5 Ag leases now. Ag leases can be for any Ag related equipment...not just farm equipment. No problem leases were mentioned by Nikolay.

2. Nikolay said Ukraine banks have "eased up somewhat" on the practice of asking for "extra collateral" for Equipment Purchase Loans. Banks also get a Government "subsidy" to help reduce the loan costs for Ag related clients...this subsity is not offered to leasing companies. Both of these items make it tougher for the leasing companies to compete with the Banks for the "lease vs purchase" equipment business.

3. Contacting leasing clients. Nickolay said 70% of clients are refered to ULC by equipment dealers. About 15% are referred to ULC by ULC's parent Bank. About 10% come from Advertising. About 5% come from the Internet.

4. ULC has a Lease Application process...requiring extensive financial data and information from the client. Nickolay all information is checked and verified...clients have been rejected for "bad credit".

5. Lease payments. Currently ULC only writes leases with Monthly lease payments. ULC is working on a program to have lease payments for longer peroids of time...such as Quartly, Semi-annual, and Annually.

It was surprising to this volunteer how well this Company is prepared to do...and IS doing now...the leasing business. I believe ULC is already following good analyzing practices in qualifying prospective leasing clients. I think this Company has a good knowledge of the leasing business...although more experience with "farm equipment" may be desirable.

Summary: I believe the Ukrainian Leasing Company - ULC is well managed...and has the employee talent and knowledge to go forward with a profitable leasing company business.

VOLUNTEER SUGGESTIONS FOR ULC:

1. More "Agricultural print advertising" in the rural areas...directly to the Farms, Farm Directors, Ag equipment dealers, Ag input suppliers, smaller banks, etc.

2. Flexible lease payment dates/schedules, based on the Ag client's cash flow income.

3. Lease salespeople with true Agricultural knowledge and/or background.

4. Enforcement of FIRM leasing company guidelines and business practices.

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AMAKO UKRAINE - American Machinery Company

First meeting with AMAKO was on March 9, 2006.

The meeting was with Ivan I. Kovach...Financial Administrator of AMAKO. Mr. Kovach is a new employee of Amako...having worked at Amako for just two weeks.

Amako is a Ukrainian branch of American Machinery Company...based in the USA. Amako offers machinery, equipment, service and spare parts for approx. 20 leading world manufacturers of equipment...including Massey Fergusson, Wil-Rich LLC, Great Plains, Kuhn, Terra Marc.

Amako is in the process of forming it's own finance company, which will include the leasing of farm equipment. The stated reason is to provide "better financial service to our clients". Amako currently has contacts and contracts with banks and leasing companies...Amako sends it's clients that want or need equipment financing to these finance companies. Amako wants to do it's own in house financing, this will provide Amako with more options in the selling and leasing of their equipment.

Mr. Kovach was very interested in the leasing business practices in the USA. We discussed at length the American ways of leasing...we went through several examples of:

1. Sample lease deals
2. Late lease payments
3. Repossessing equipment
4. Sale of repossessed equipment
5. Sale of equipment at lease end

This volunteer thinks Mr. Kovach is very knowledgeable in the financial matters of the farm equipment business...including leasing.

Second meeting with AMAKO was on March 10, 2006

The meeting was with Ivan G. Nesterov...Seeds Sales Manager of Amako. Mr. Nesterov said Amako wants to become a "one stop shop" for all of their agricultural client's needs. Mr. Nesterov was most interested in knowing about the selling of seeds, and the credit arrangements between USA farmers and their seed suppliers.

Other Amako personnel were unavailable for meeting with this volunteer...and Saturday the 11th was not a working day for Amako.

VOLUNTEER SUGGESTIONS FOR AMAKO:

1. Develope a workable used farm equipment trade-in program

    A. Take more used farm equipment in trade for new equipment
    B. ALL used farm equipment has "some value"...even if it is only worth a junk price...allow accordantly

2. Consider importing late model used equipment...including equipment from the USA

   A. Some Ag clients cannot afford new equipment
   B. Amako will sell more Parts and Service
   C. Amako will have more customers

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LEASING HOUSE (LH) - L'viv

Meetings with LH were held in L'viv, Ukraine on March 13 and 14, 2006.

Meetings were with Oleg Sitiuk, Director, Kateryna Nevynna, Manager, and 2 other LH personnel.

Discussions covered manys areas, but mostly they wanted to know how USA leasing companies did the leasing business. Points covered were:

1. Evaluating some of LH's leasing portfolio
2. Talked about their one Ag lease contract
3. Discussed lease sales techniques
4. Reviewed lease client application process
5. Discussed client risk assessment/analysis practices
6. Reviewed delayed payments procedures
7. Talked about Finance and Operating leases

Leasing House has a portfolio of over 80 contracts...but only one Ag lease, on a Case/IH combine.

This volunteer believes Leasing House will move forward into the agricultural leasing business.

VOLUNTEER SUGGESTIONS FOR LEASING HOUSE:

1. Develope Ag lease contracts that INCLUDE "usage limits" on the payments
2. Include penalty payments for over usage in the lease contract
3. One member of LH should become an expert on farm equipment values
4. Contact the leasing client's Bank for information on the client
5. Be aggressive in collecting late lease payments

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Volunteer comments and suggestions to CNFA:

This volunteer found the CNFA personnel that I had daily contact with to be "the best". Andriy Yastreb, Project Coordinator...and Alexandra Kishko, my translator...were both EXCELLENT. I could not have asked for any better people to have helped me on my assignment. They are both to be highly commended. Boris...car driver for CNFA...also did an excellent job.

The Laptop computer in my apartment...with Internet access on a private telephone line...was GREAT. IF a hi-speed hookup could somehow be arranged...even at the volunteer's extra expense...it would be even better and appreciated. The Laptop also allowed this volunteer to do his trip report during the assignment...which I found to be very helpful.

The volunteer apartment is quite suffecent in:

1. Located 100 meters from the Metro...2 stops to the City Center & Khreschatyk St.
2. Modern and big enough...including the bathroom and kitchen (has microwave oven)
3. Reliable hot water...for me
4. Good cable TV with western CNN/BBC news.
5. Clothes washing machine
6. Private telephone line...with long distance (# 8) dialing...needed for most UKR cell phones, and some Kiev apartments...and other UKR cities
7. Reliable elevator, for me anyway...to the 8th floor apartment
8. GREAT...BIG...food market 300 meters from the apartment...everything needed can be purchased there
9. Many restaurants close to the apartment

All things considered, it is a good assignment apartment to stay in.

Projects Join Forces to Support Rural Finance

On March 2-3, 2006, two USAID-sponsored projects, the mission-funded Access to Credit Initiative (ATCI) and the global Farmer-to-Farmer Program (implemented in Moldova, Ukraine and Belarus by CNFA), held a two-day seminar on Sales Techniques and Risk Assessment for Ukrainian leasing companies. Over 20 leasing professionals attended the seminar, held at the Ukrainian Grain Association's conference facility, to learn about sales and risk management techniques particular to agricultural leasing.

The seminar is part of a joint effort by CNFA and ATCI to enhance the capacity of Ukrainian lessors to provide lease financing to agribusiness clients, especially small and medium-sized enterprises (SMEs).

The two-day seminar targeted leasing company credit and sales managers and included presentations by CNFA-FtF volunteer and retired John Deere dealer Tom Meade, along with ATCI experts Richard Caproni and Roman Shykarenko. Information was presented on how to:

- Attract the best clients and sell the benefits of lease financing
- Evaluate potential clients' needs and financial capacity
- Select appropriate equipment and contractual terms for each client
- Manage client relationships to ensure payment and repeat business
- Monitor and protect the leased assets

Following the seminar, volunteer Tom Meade conducted additional 2-day site visits with three of the targeted companies to help them apply the theory of the training to the practice of their specific businesses. For the purpose of establishing replicable business models, CNFA and ATCI have selected Ukrainian Leasing Company (a bank-owned lessor), Amako (an in-house dealer finance company) and Leasing House (an independent lessor).

To date, leasing companies have not been eager to target SMEs or the agricultural sector because many other, more attractive sectors such as transport, real estate, construction and manufacturing still remain underserved by Ukraine's developing credit markets. Agribusiness lending and leasing require special programs and procedures and, in Ukraine, this segment does not offer easy returns and has seen high default rates.

In order to increase the chance of success in promoting such programs, the two projects will continue to work together to develop capacity and encourage financing for agricultural companies. This is the first of three such trainings planned in 2006 through the ATCI/FtF partnership. The remaining two events will cover issues of strategic planning, as well as marketing and new product development.

ATTACHMENT 11

National Bank of Ukraine
Association of Ukrainian Banks

With support of
IFC's Ukrainian Leasing Development Project
USAID Access to Credit Initiative

International Conference

Banking Sector & Leasing Market
Business & State Regulation

February 21, 2006
Kiev, Andreevska St, 1/1,
NBU Training Center

9:00 – 9:30	***Registration of Participants***	
9:30 – 10:00	Opening of the Conference	**Mr. Vasyl Pasichnyk,** *National Bank of Ukraine, Member Board of Directors, Director of Legal Department* **Mr. Andrey Litvin,** *State Commission for Regulation of Financial Services Markets, the First Deputy of Head*

Session 1:

General Overview end Legal Environment of Leasing.
Moderator – Dmitro Sviatosh – Member of the Parliament, Honored President of Corporation «АИС»

10:00 – 10:20	Current State of the Ukrainian Leasing Market	**Mr. Ernst Mehrengs,** *Project manager* *Ukrainian Leasing Development Project* *International Finance Corporation*
10:20 – 10:40	Leasing market in Europe	**Mr. Jean Marc Mignerey** *Chairman Leaseurope and* *CEO Société Générale Equipment Finance (France)*
10:40 – 11:00	Survey on Court Practices and Legislation as to Leasing in Ukraine	**Mr. Vitaliy Riznyk,** *National Bank of Ukraine,* *Legal Department, Chief Lawyer*
11:00 – 11:20	Tax and Legal Environment with respect to Leasing	**Mr. Jorge Intriago,** *Partner Tax and Legal, PricewaterhouseCoopers and Vice-President, European Business Association*
11:20 – 11:40	Discussion, Summary of the First Session	
11:40 – 12:00	***Coffee-break***	

Session 2:

Banks and Leasing Companies – Natural Partners.

Moderator ***– Roman Ivanenko –*** *Head of Supervisory Board of Ukrainian Association of Lessors, General Director of Leasing Company "Євро Лізинг"*

12:00 – 12:20	Leasing as a Financial Mechanism	**Mr. Randal Petersen,** *Senior Operations Manager,* *International Finance Corporation*
12:20 – 13:00	Cooperation of Ukrainian Banks and Leasing Companies: Views and Perspectives of Bankers (2 speakers)	**Mr. Vitaliy Golovkin,** *First Ukrainian International Bank,* *Deputy Director of Corporate Business*
13:00 – 14:00	***LUNCH***	
14:00 – 14:40	Cooperation of Ukrainian Banks and Leasing Companies: Views and Perspectives of Leasing Companies (2 speakers)	**Mr. Alexander Zubanyov,** *Vice President of Leasing Association "Ukrleasing",* *General Director of leasing company "Ukrincomlease"* **Mr. Martin Elling** *Investor and former shareholder of First Lease Hertz*
14:40 – 15:00	Leasing Transactions: How Banks Work with Leasing Companies in Europe / Strategy of Banks Entering the Leasing Market - Examples from Europe	**Mr. Pascal Bouillon** *Deputy CEO Société Générale Equipment Finance (France)*
15:00 – 15:20	Non-bank Financing of Leasing: Purchase and Sales of Lease Contracts	**Mr. Andre Kyyak.** *Advisor to the Minister of Economy.* *Head of Board of Directors of Credit Bureau.*
15:20 – 15:40	Financial Sources for Leasing Companies: Foreign Experience.	**Mr. Richard Caproni** *Senior Advisor* *Ukraine Access to Credit Initiative / USAID*
15:40 – 16:00	Sourcing Financing: A Lessor's Experience	**Lazzat Asabaeva** *President BTA Orix Leasing, Kazakhstan*
16:00 – 16:20	Equity Investment for Leasing Companies	**Natalia Best** *Vice President* *Horizon Capital*
16:20 – 16.50	Panel Discussion **Mr. Randal Petersen** *IFC* **Mr. Pascal Bouillon**, *Société Générale* **Mr. Ton Huls,** *ING Bank Ukraine* **Mr. Dominique Menu,** *BNP Paribas* **Mr. Andriy Zhylinsky,** *Ukrainian Association of Lessors* **Mr. Martin Elling** *Former shareholder of First Lease Herz* **Others to be confirmed**	
17:00 – 18:30	***RECEPTION AND MATCH-MAKING ACTIVITY***	

International Conference
February 21, 2006
List of Participants

State Institutions

1.	Kateryna Otchenash	(SCRFM), Commissioner, Director of Department on Finance Companies Supervision
2.	Andriy Lytvyn	(SCRFM), Deputy Head of Commission
3.	Victor Novikov	NBU, Deputy Director of Legal Department
4.	Vitaliy Riznik	NBU, Lawyer
5.	Iryna Sachenko	NBU, Deputy Head of Administrative Department
6.	Valentyna Bilyk	NBU, Chief legal consultant
7.	Dmytro Svyatosh	Deputy of Parliament
8.	Nadia Zhyla	SCRFM
9.	Olga Fabrycheva	Assistant to Deputy of Parliament Dmytro Svyatosh
10.	Vasyl Pasichnyk	NBU, Member of the Board, Director of Legal Department
11.	Victor Kulininch	Assistant-Consultant to Deputy of Parliament Ivan Zayats
12.	Natalia Vnukova	Doctor, Professor of Kharkiv State Economics University
13.	Denys Fudashkin	Ministry of Finance of Ukraine, Department of Taxation and Customs Policy, Director
14.	Larissa Melnychenko	Ministry of Finance of Ukraine, Department of Taxation and Customs Policy, Head of Unit
15.	Serhiy Chemerys	State Tax Administration, Deputy Director of Department, Head of Division
16.	Raisa Bolila	State Tax Administration, Head of Division
17.	Iryna Melnyk	State Tax Administration, Deputy Head of Division

Non-Government Organizations

18.	David Greer	Commercial Law Center, Chief of Party
19.	Valentyna Danishevs'ka	Commercial Law Center, Director
20.	Nina Demchuk	"Ukrainian Credit-Banks Union" Association, Chief Economist
21.	Vladimir Sabischenko	Association of Ukrainian Banks, Deputy Head of Administrative department of banks connections
22.	Artem Milshyn	Logistics Platform
23.	Pavlo Kushnirenko	Ukrainian Union of Industrials and Entrepreneurs, Investment Policy Issues, Chief Specialist
24.	Andriy Zhylins'ky	President of the Association "Ukrainian Union of Lessors"
25.	Valentyna Pronina	Ukrainian Marketing Reforms Education Program

International Organizations

26.	Peter Stredder	European Bank for Reconstruction and Development, Senior Banker, Deputy to Director for Ukraine

27.	Anna Kinash	European Bank for Reconstruction and Development, Senior Banker
28.	Jorge Intriago	European Business Association, Vice-President, PricewaterhouseCoopers, Partner
29.	Lazzatt Asabayeva	BTA Orix Leasing, President
30.	Volodymyr Didenko	PricewaterhouseCoopers, Director Taxation
31.	Said Reza	International Company Orix Leasing Pakistan Limited, General Manager
32.	Andriy Kyyak	International Credit Bureau, Chairman of the Board
33.	Richard Caproni	ATCI, USAID, Pragma Corporation, Senior Advisor
34.	Liliya Snigir	ATCI, USAID, Pragma Corporation
35.	David Lucterhand	Project Director, Access To Credit Initiative/USAID, Ukraine
36.	Robert Homans	ATCI, USAID, Pragma Corporation, Senior Advisor
37.	Natalia Best	Horizon Capital, Vice-President
38.	Jean Marc Mignerey	Chairman Leaseurope and CEO Société Générale Equipment Finance (France)
39.	Pascal Bouillon	Deputy CEO Société Générale Equipment Finance (France)
40.	Olga Krasitska	American Machinery Company, Financial Manager
41.	Angela Prigozhina	The World Bank, Financial Sector Specialist
42.	Valeria Ciobanu	CNFA, Moldova, Agribusiness Credit Specialist
43.	Rick Gurley	Chief of Private Enterprise Division, Office of Economic Growth, USAID Mission for Ukraine, Belarus & Moldova
44.	Darya Lisyuchenko	Program Analyst, Private Enterprise Division, Office of Economic Growth, USAID Mission for Ukraine, Belarus & Moldova
45.	Onno Britsma	BMT Consult, Director
46.	Alan Tuayev	Embassy of Russian Federation in Ukraine, Economic Department, Attache

Leasing Companies

47.	Oleksander Zubanyov	Ukrincomlease Leasing Company, Director General
48.	Roman Ivanenko	Euro Leasing Ltd, Director General
49.	Martin J. Elling	First Lease Ltd, Ex-Chairman of the Board
50.	Mykola Dorozhenko	Kyiv Department of Leasing Company “Garant”
51.	Victoria Karpenko	Executive Director, Universalna Leasing Company LLC, Odessa
52.	Tetyana Saus	Lasca Leasing Ltd, Director
53.	Oleksandr Neschotnyi	Leasingagroinvest, Director General
54.	Olena Grudnenko	AGIO Leasing, Director
55.	Iryna Boyko	Leasingagroinvest, Deputy Director General on Development and Economy
56.	Oleg Sharf	Ukrincomlease Leasing Company, Executive Director
57.	Lyudmyla Zolotaryova	Ukrainian Leasing Company Ltd, Director
58.	Olena Kovshun	Ukrkinoinvest LLC, Accountant
59.	Oleksandr Smogoryns’ky	First West-Ukrainian Leasing Company, Director General
60.	Denis Vasilenko	Glavleasing Ukraine, Director
61.	Volodymyr Borysov	First West-Ukrainian Leasing Company, Deputy Director General
62.	Oleksandr Koshcheyev	Ilta LLC, Head of Leasing Dpartment
63.	Sergiy Komyakov	Energoleasing Leasing Company, Director
64.	German Panikar	Energy Alliance, Deputy Director
65.	Yuriy Svidzins’kiy	PL Leasing, Lviv, Director
66.	Dmytro Bogodukhov	Lease IT, Director General

67.	Dmytro Fridman	Lease IT, Marketing Director
68.	Oleksandr Budovoy	TBI Leasing, Director
69.	Anatoliy Pokhodziayev	Leasing Company "Universalna", Lviv
70.	Dmytro Prudenko	Armaleasing, Chairman of the Board
71.	Andriy Vyshnyak	First Lease Finance, Director General
72.	Elena Shkapova	Leasing Company "Renta", Commercial Director
73.	Yuriy Skoropys	Leasing Company "Ukrtransleasing", Deputy Chairman of the Board
74.	Vadym Shvitay	Leasing Company "Ukrtransleasing", Head of Aviation Administration
75.	Yuriy Vasin	Nadra-Service Director

Financial Institutions

76.	Gennadiy Sergatyy	"Transbank", Deputy Chairman of the Board
77.	Olga Onufriyenko	"Transbank", Head of Banking Technologies and Business Development Administration
78.	Dmytro Molodtsov	"Dnister" Bank, Lviv, Chief Specialist of Innovation Unit
79.	Oleh Kuriy	"Dnister" Bank, Lviv, Deputy Director of Development Department
80.	Sergiy Melnyk	"Ukrgazbank", Deputy Head of Trust Operations Administration
81.	Victor Suprunov	"Kyiv" Bank, Deputy Chairman of the Board
82.	Dmytro Lemeshov	KB "Daniel", Head of Administration
83.	Victor Bratko	"Kyivs'ka Rus" Bank, Chairman of the Board
84.	Iryna Lukiyeva	KB "Khreshchatyk", Chief Specialist, Investments Administration
85.	Yaroslav Khariy	KB "Khreshchatyk", Department of Securities and Investments
86.	Orest Stec	Societe Generale
87.	Sergiy Mayevs'kiy	"BIG Energia" Bank, Head of Credit Programs Administration
88.	Vladyslav Necheporenko	KB "Expobank", Vice-President
89.	Anna Kononenko	KB "Aktivbank", Chief Economist of Corporate Administration
90.	Lina Svintsyts'ka	"Ukrainian Credit-Trade Bank", Deputy Chairman of the Board
91.	Borys Zozulya	"Ukrainian Credit-Trade Bank", Head of Credit Department
92.	Denys Prutchykov	Hermes Capital
93.	Oleksandr Omelchuk	Hermes Capital
94.	Gennadiy Zarya	"Index-Bank"
95.	Kostyantyn Yur'yev	"Diamantbank", Leasing Program Coordinator
96.	Tetyana Geryavenko	"Nadra" Bank, Director of Corporate Bank Products Department
97.	Valentyna Prykhod'ko	"Nadra" Bank, Credit Products Administration ,Chief Economist of Long-Term Credit Products Development Department
98.	Iryna Zagrebelna	"Integral-Bank", Head of Credit Administration
99.	Volodymyr Tymchenko	"Brokbiznesbank", Director of Department of Active and Passive Operations
100.	Andriy Grabovets'kiy	"Brokbiznesbank", Head of Department
101.	Victoria Drukar	"Intercontinental" Bank, Head of Credit Administration
102.	Lyudmila Katanina	"Intercontinental" Bank, Head of Legal Entities Crediting Department
103.	Natalia Falkova	Pravex bank, Credit Department, Department of Development of New Forms and Methods of Crediting of Legal Entities, Chief Economist
104.	Oleh Gontarev	PEKAO LLC, Director of Commercial Department
105.	Lidia Kovalchuk	Eurobank, Head of Legal Entities Crediting Department
106.	Oleksiy Sysoyev	Ukrainian Financial Group, Deputy Chairman of the Board
107.	Vitaliy Golovkin	FUIB, Deputy Head of Corporate Business Department

108.	Petro Kravchenya	VABank, Director of the First Kyiv Filia
109.	Roman Kostenko	Inprombank, Kharkiv, Deputy Chairman of the Board
110.	Volodymyr Bukovyns'kiy	Ukrprombank, Deputy Chairman of the Board
111.	Maryna Godzha	Ukrprombank, Head of Administration
112.	Natalia Muzhuk	HVB Bank, Chief Specialist of Leasing Department
113.	Sergiy Kelbas	ICB, Head of internal audit
114.	Anna Kelbas	ICB, Credit Specialist
115.	Eduard Nersesov	"Arma" Bank, Chairman of the Board
116.	Eugenie Zaigrayev	Head of Business Clients ProCredit Bank Ukraine
117.	Maxim Ivasenko	Kraina, Insurance Company, Deputy Head of Corporate Clients Administration
118.	Leonid Dvoretskiy	Industrial Financial Bank, Head of Administration
119.	Yevhen Hornyuk	Polikombank, Economist
120.	Svitlana Lotots'ka	CreditPromBank, Head of Corporate Business Development Department
121.	Moshe Izchak Kanes	TBIF, Regional Representative in Ukraine
122.	Dominique Menu	Head of Représentative Office BNP Paribas in Ukraine
123.	Igor Shapovalov	Prominvestbank, Kyiv Filial, Chief Economist
124.	Andriy Kudryavchenko	"Morskoy" Bank, Credit Department, Economist
125.	Yuriy Yufa	Autokrazbank, Kremenchuk, Deputy Chairman of the Board
126.	Valentyna Plyashechnyk	First Investment Bank, Advisor to Chairman of the Board on Legal Issues
127.	Riepl Johannes	Raiffeisen Bank Ukraine, Corporate Banking Division Relationship Manager

Business

128.	Victor Korobov	Engineering Center of Water Supply, Director
129.	Andriy Korobov	PE "Alternative", Financial Consultant
130.	Andriy Skuratovs'kiy	"Dorofeev, Skuratovsky & Partners", Executive Director

International Finance Corporation

131.	Randal Petersen	IFC, Senior Operations Manager
132.	Ernst Mehrengs	Ukraine Leasing Development Project, Project Manager
133.	Nadezhda Ryazanova	Ukraine Leasing Development Project, Tax and Accounting Specialist
134.	Julia Shevchuk	Ukraine Leasing Development Project, Legal Specialist
135.	Yuriy Kolyadyuk	Ukraine Leasing Development Project, Banking Finance Specialist
136.	Alex Kononets	Ukraine Leasing Development Project, Impact Research Analyst
137.	Andrei Gulay	Ukraine Leasing Development Project, Communications Associate
138.	Tamara Veselova	Ukraine Leasing Development Project, Team Assistant

PHOTOGRAPHS

Bond Bank Workshop January 27, 2006

Bond Bank Workshop January 27, 2006

CML Certification Ceremony January 19, 2006

SSMSC Mortgage Seminar February 1, 2006