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November 28, 2000

Mr. Boris Von Hoffmann, Project Officer
USAID/Kiev Mission
19 Nizhny Val
Kiev, Ukraine

Subject: **Financial Sector Restructuring and Privatization Services in the ENI Region**
Contract No. 121-C-00-98-00628-00
National Bank of Ukraine, Kiev, Ukraine

Dear Mr. Von Hoffmann:

Enclosed please find a copy of the September 30, 2000 quarterly report for the subject contract. All attachments are on file with Barents Group and are available upon request.

If you should require additional copies, please feel free to contact me at (703) 747-3248 or via email at jhorner@kpmg.com.

Very truly yours,

Barents Group

James E. Horner

James Horner
Managing Director

Enclosure

cc: Mr. Bill Penoyar, USAID/Washington, DC
Ms. Gloria White, USAID/PPC/CDIE, Washington, DC
Ms. Catherine Mallay, Contracting Officer, USAID/Kiev
Mr. Arne Peterson, Advisor, International Monetary Fund
Mr. Alan Roe, Senior Financial Economist, World Bank
Mr. Alex Flemming, World Bank
Ms. Angela Prigohzina, Operations Officer, World Bank/Kiev
Project File

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Bank Resolution

Benchmark	Adviser	Original Date	Revised Date	Date Completed	Status
Bank Resolution					
Teach course on Mergers and Acquisitions, in conjunction with Training advisor	Boren	03/31/99		2/25/99	Eighteen individuals from the rehabilitation and liquidation units participated in the course given over a four day time frame. The pooling of interest and purchase methods were taught with a case study of two Ukrainian institutions included. The course also covered possible assistance packages utilized to finance purchase and assumptions.
Develop plan to assess involvement of other departments in problem bank designation	Boren	03/31/99		2/28/99	Interviews will be conducted to evaluate the current process utilized to determine problem bank status. These will include discussions with on-site, off-site, legal, problem bank resolution unit and the Kiev Regional Office. During February discussions were held with Kiev Regional Office, Off-site and Early Warning Analysis. Reviews will also be performed of all regulations, policies and procedures utilized to designate problem banks. Once all investigative work is complete, a formal written recommendation will be submitted to management during the second quarter of 1999.

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Submit outline of BRU operations manual to management	Boren	03/31/99	4/30/99	June 25, 1999	The outline has been drafted and presented to management. A schedule will be drafted for completion of sections as soon as approved by management.
Draft at least two chapters of proposed operations manual	Boren	06/30/99	08/31/99	8/30/99	Two chapters for the handbook have been drafted (Introductory Section and then Supervisory Remedial Actions). The materials have yet to be translated and are scheduled to be presented to management and discussed during October. Revisions will then be made in November.
Propose rules for coordination of work between rehabilitation and liquidation sections of BRU	Boren	06/30/99	8/15/00	10/4/2000	The proposal for coordination was completed and submitted to management on October 4, 2000. A copy of this memorandum is attached to the quarterly report.

Conduct review of operational enforcement procedures and report findings to management	Boren	06/30/99	10/30/00		The review of operational procedures will begin during the week of October 9th with recommendations to management within the last week of the month. Numerous recommendations have previously been made, however, this review will focus upon whether current procedures will ensure the compliance with the new Resolution #215 and the active use of enforcement tools. Attached a memorandum dated August 31, 200 addressing the issue of Quality Control as Applied to the Bank Resolution Unit. Also attached is a memorandum addressing Transfer Documents dated September 15, 2000. This document discusses a recent transfer of an institution to the BRU and the information which accompanied the transfer. The failure of the department to receive appropriate information delays considerably the ability of the department to utilize any enforcement actions or to properly supervise the institutions.

Review timeliness of referrals to BRU and present findings to management	Boren	06/30/99		May 6, 1999	Review completed which concluded institutions are not transferred to BRU in a timely manner. Report issued to management with recommendations for corrective action. Significant criticisms concerning Regional Office, On-Site and Off-site functions in addition to BRU. Management stated general concurrence with the document and has begun to take steps to eliminate the numerous criticisms. First, a working group comprised of an individual from on-site, off-site and the BRU has been established. The task is to review all institutions, by August 1st, and determine whether CAMELS are accurate and whether additional actions should be taken. The previous recommendation by Senior Policy Advisor Selby to establish Supervision Senior Management Committee has been accepted. Advisor's review recommended this committee review and approve CAMEL rankings and determine enforcement actions. The committee has assumed this responsibility and is also providing oversight of the working group assessing the accuracy of current CAMEL rankings and whether to pursue additional enforcement actions. In addition, On-site has stated that it is implementing the recommendation that reports of examination which are not adequate should be rejected and returned to the originating office for correction. Other recommendations are also made within this document and this advisor will follow-up to ensure they are addressed.

Teach course in Elements of Effective Rehabilitation Plan, in conjunction with training advisor	Boren	06/30/99	7/19/99	7/19/99	Course taught jointly with Tacis. Barents Group, LLC. Advisor taught Effective Rehabilitation Plans and Provisional Administration, although the original agreement with Tacis had been that they would cover the Provisional Administration Section of the review.
Recommend changes to process of problem bank designation	Boren	06/30/99		9/2/99 5/20/00	Changes to Resolution #425 – Problem Bank Criteria were made and submitted to management on September 2, 1999. These were then modified on May 20, 2000 according to the content of the revised #38 (Now resolution #215). However, it is unlikely these will be addressed by management until #215 is approved by the Justice Ministry and reorganizational issues currently being addressed by senior management are complete. BRU has indicated it will not lead the effort in adopting these provisions as it is felt the methodology unit should address. Once #215 is approved by Justice, the issue of Revising Resolution #425 will be addressed with Prudential Supervision.

NBU to have adopted changes to process of problem bank designation	Boren	09/30/99	9/30/00		Resolution #215, which is an enforcement document, was approved by the Ministry of Justice during July, 2000. It is attached to this quarterly report. The document requires enforcement action on all 3, 4, and 5 CAMEL rated institutions. The recommendations for revision to #425, problem bank designation, have been made and were included with the last quarterly report. Specifics within that document define problem banks as 3, 4, and 5's. No action has been taken by the NBU due to the reorganization issue and the Presidential Decree. However, management has stated they will give consideration to the recommendations made and will address this issue in October. The advisor's proposal contains rules for transfer of an institution to the BRU and it is not clear at this point whether the BRU will remain in its current form. Recommendations have previously been submitted concerning reorganization and the position BRU would occupy in a new regime.
Draft at least two further chapters of operations manual	Boren	09/3099	12/31/99	12/31/99	The chapters include the following: (1) Formal Written Agreements and Subsequent Supervisory Actions, and (2) Mergers and Acquisitions.
In cooperation with legal advisor, draft at least two sections of enforcement manual	Boren	09/30/99	12/31/99	12/31/99 8/11/00	The initial draft was presented to management on December 31, 1999 awaiting final revisions to Regulation #38. Regulation #38 was reissued as #215 in July 2000. The enforcement manual was reissued August 11, 2000 reflecting the new #215. The revised manual is attached to this quarterly report. No actions have been taken to-date by Management concerning this document.

Draft at least two further chapters of operations manual	Boren	12/31/99	10/30/00		Work in this area was dramatically slowed by the intensive effort to finalize the revisions to Regulation #38 during the second quarter. The draft has been completed and in translation. Completion slowed due to changes in translators, translation of final #215, revisions to the Enforcement Manual and translations, in addition to other drafted documents as included with this quarterly report. Manual to be submitted to management no later than October 30, 2000.
NBU to have adopted rules for coordination between rehabilitation and liquidation	Boren	12/31/99	9/30/00		Recommendations for coordination were provided to management on October 4th. However, the issue of the coordination is highly dependent upon NBU reorganization which have been held-up to address the Presidential Decree on Independence. Recommendations, included within the June Quarterly report stripped liquidation away from the Problem Bank Unit. If this were to occur, the implementation of recommendations for coordination between the rehabilitation and liquidation become crucial.
Teach course in Analytical Assessment of Banks, in conjunction with training advisor	Boren	09/30/99	10/18/99	10/20/99	The financial analysis course included 20 participants and was structured around a case study. Extensive time was expended at the beginning of the instruction fully explaining the concepts to be utilized. After analysis was performed, the students were required to make a presentation of their findings. The course was well received and participation in discussions was extensive.

Teach course in liquidation criteria, in conjunction with training advisor	Boren	12/31/99		11/10/99	A financial analysis course was taught instead of the liquidation seminar. This was taken after consultation with the NBU and agreement that liquidation issues are the prerogative of Tacis advisors. This course is a repeat of the presentation made in October, 1999 and included the same number of participants. The Deputy for the Bank Resolution Department (Domshenka) attended the entire seminar and participated fully in the case study.
Comment on the Revision of Due Dates					Significant changes occurred in the NBU with designation of a new Deputy Governor for Supervision and the replacement of the Director of the Bank Resolution Unit. In addition, the Presidential Decree concerning the independence of the NBU and the possible removal of supervision from the NBU has had a negative impact. The Director of the BRU has been busy dealing learning his new job. He has been extensively involved in the issue of Bank Ukraina and the recent appointment of a Provisional Administration to that institution and Bank Slavianski. In addition, the Advisor contended with the departure of his translator to the U.S. for a two year Master's Degree Program. This translator was replaced just prior to the advisor's vacation in the U.S. but only remained with the project a few days. Upon the advisor's return to Ukraine, the translator position was again filled. All of these events impacted the completion of projects, but it is still anticipated all issues will be addressed by November 30th except the full implementation of recommendations. Implementation is a slow methodical process in the Ukraine.

Outside Contacts (for quarter ended September 30, 2000	**Name (None)**	**Affiliation**	**Time spent**
Additional assistance requested by IMF	Given the absence of the IMF advisor to Ukraine, Edward Herron, the IMF brought in an interim advisor to assist the NBU's task force addressing Bank Ukraine. A request was made to USAID that this advisor work with the interim IMF advisor Michael Newton in guiding the task force on all the issues which would need to be addressed if a Provisional Administration were to occur. The involvement was limited to several days just prior to my holiday in the U.S. In addition to guidance for the task force, this advisor also provided a verbal overview to Newton concerning operations within the NBU and the banking system as a whole.		
Other comments	The IMF and the NBU requested the advisor to conduct a series of presentations on Provisional Administration and Investigations. The seminar was initially structured for attendance by individuals which were to be designated as members of the provisional administration team for Bank Ukraina. However, it appears that not all members of the team could attend and others were sent in their stead. The seminar was organized by the large bank unit with the guidance and cooperation of the IMF interim advisor Michael Newton. Presentations were made by this advisor, Newton and individuals selected because of their position within the NBU, such as individuals to address legal and personnel issues. It was anticipated that a more thorough seminar with all team members present would be conducted before any action taken in establishment of a Provisional Administration. However, in September, Provisional Administration action was taken without the additional seminar.		
Other comments	A proposal for the final seminar to be conducted by the advisor will be submitted to the BRU for their consideration during the first week of October. It will be recommended the seminar be focused upon 8 institutions which are problem banks. The NBU will be requested to instruct Regional Directors of Supervision to make presentations addressing their supervision of these institutions. In addition, it is hoped the NBU will honor the request for a presentation by Krutiyk, Andrushenko, and Zabska. The entire focus will be upon the sharing of ideas, approaches, and information. It will also serve the useful purpose of getting the NBU personnel directly involved in the education of their staff rather than full reliance upon advisors.		