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The roots of corruption in Ukraine's energy sector

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Center for Human Capital

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EXECUTIVE SUMMARY

Ukraine's energy sector, exhausted by systematic Russian attacks, has seen a rapid expansion of state control through nationalization and martial law. This shift has not reduced corruption; in many cases, corrupt practices have persisted or worsened. The reason is that officials increasingly rely on and deepen schemes that serve as key instruments of corruption: political control and distorted regulation of energy markets.

Core corruption mechanisms in the energy sector from the pre-war period endure, including procurement abuses, market manipulation, and collusion among market participants – have also persisted. However, the war has given rise to new distortions in state energy policy, such as politically driven reconstruction, misallocation of funds (including donor aid), and informal barriers that enable rent-seeking and hinder new projects. These are reinforced by structural weaknesses: persistent political interference in state-owned enterprises (SOE), legislative loopholes, weak and dependent national regulators (National Energy and Utilities Regulatory Commission (NEURC), the Antimonopoly Committee), and the absence of transparent, rule-based market operations.

Addressing these systemic risks depends on the effective implementation of reforms launched before the war: fully implementing Organisation for Economic Co-operation and Development (OECD) standards, enforcing Regulation on wholesale energy market integrity and transparency (REMIT), and the fulfilment of commitments on energy market integration.

Without eliminating political influence over state-owned enterprises and regulators and ensuring transparent, enforceable market rules, anti-corruption efforts will remain ineffective.

Transparency is not only the foundation of good governance, it is also a political necessity to break the "vicious circle", in which corrupt proceeds are reinvested to distort the political system itself.

This study by the Ukraine Facility Platform analyses corruption risks and vulnerabilities in Ukraine's energy sector and offers practical recommendations for their mitigation. The methodology includes preliminary research, media analysis, surveys, and interviews with sector stakeholders, energy experts, and anti-corruption practitioners. The findings are summarized in conclusions and recommendations aimed at improving the regulatory and institutional framework, strengthening governance, and ensuring compliance with Ukraine's EU integration commitments and international anti-corruption standards.

This is a shortened version of the full report, which has been made public.

CORRUPTION LANDSCAPE AND ENABLERS OF UKRAINE'S ENERGY SECTOR

Core mechanisms of corruption include:

- **The manipulation of procurement processes,** particularly in construction, repair, and restoration of energy facilities, as well as in the fuel supply for energy infrastructure. These tenders are frequently designed to favour predetermined winners, often under the guise of protective measures or emergency needs.
- **Market distortions,** where dominant players abuse market power and distort competition, notably through the misuse of Public Service Obligation (PSO) mechanisms in both electricity and gas.
- **Politicised reconstruction processes,** with generation capacities selectively rebuilt not based on technical merit but political interference.
- **Financial mismanagement,** including the opaque use of state and donor funds.
- **Informal bureaucratic hurdles** are systematically imposed on new projects, creating opportunities for rent-seeking and corruption.
- **Non-transparent appointments** to supervisory boards and top management of state-owned enterprises, often based on nepotism – where preference is given not to managerial professionalism but to belonging to a political "inner circle".
- **Concentration of actual power** in the hands of a few individuals whose authority effectively outweighs formal institutions, creating broad opportunities for systemic abuses.

At the same time, **anti-corruption efforts within Ukraine's energy sector are notably fragmented.** The state lacks a clear national-level strategy specifically targeting sector-specific corrupt practices. Despite the adoption of two Anti-Corruption Strategies and their implementation programs since 2014, no dedicated anti-corruption document has focused on analyzing energy sector corruption's causes, conditions, or mitigation measures. This gap is partly due to the National Agency on Corruption Prevention (NACP) lacking sufficient expert resources, relying on energy regulators and the Ministry of Energy to lead risk analysis—a role they haven't effectively fulfilled. Their anti-corruption programs primarily address internal compliance rather than external functions or root causes of corruption. Crucially, none of Ukraine's energy strategies, including the latest one extending to 2050, mentions corruption as a hindering factor.

The consequences of this state of affairs are severe and extend far beyond financial loss. The key ones include inefficiency and delays in critically important projects for restoring energy facilities, the inability of state-owned enterprises to systematically pay dividends to the state budget, and chronic losses at both local and national levels.

The investment climate remains weak, with a minimal number of bankable projects. The development and scaling of hybrid renewable energy systems (HRES) have effectively stalled, while the resilience of regions, especially vulnerable frontline and border communities, continues to decline.

A clear trend has emerged – the appearance during the war of a "new class of oligarchs." Market power and administrative control are no longer concentrated in private business groups but have shifted to officials and management elites of state-owned companies, who, in essence, reproduce oligarchic practices – using state assets for personal control and enrichment.

Several enabling factors underpin this systemic corruption.

1. **Political interference in state-owned** companies through direct control and weakened corporate governancein state-owned energy companies. Respondents interviewed by the Ukraine Facility Platform identified "abuse of power and influence" and "ineffective management of the sector" as the main prerequisites for corruption. The core reason for this inefficiency is the lack of separation between policy formation (the responsibility of the Ministry of Energy) and the management of state-owned companies. This leads to violations of key legislative norms that enshrine the European principle of separating the management of energy assets from political or business influence. This principle is often ignored when appointments of top managers and supervisory board members of state-owned energy companies take place under political pressure.

2. **Political influence over the national regulator NEURC.** The independence of the energy regulator (NEURC) is compromised by its legal design and historical susceptibility to political maneuvering during commissioner appointments. The primary root cause is the regulatory body's vulnerability to external political pressure and direct intervention by political figures. This enables politically motivated "manual steering" of markets, distorting competition and hindering business development.

3. **Regulatory capture and a lack of enforcement capacity.** Due to the lack of political will and resources, oversight bodies effectively create advantages for large business groups. Powerful economic elites can influence regulatory decisions or operate with low risk of accountability. Surveys confirm a low level of prosecution and punishment for corrupt practices.

4. **Use of law enforcement structures for business pressure or selective targeting.** Political elites involve law enforcement bodies, security services, and courts to exert pressure on legitimate energy businesses. Common methods include fabricated investigations, corporate raiding, or inspections carried out for private gain or political purposes. The root cause is the lack of independence and institutional capacity of law enforcement and the judiciary.

5. **The absence of clear penalties for violations.** When the risk of punishment is minimal, energy market participants prioritize profit over compliance. This is rooted in weak legislative drafting, a lack of political will to impose penalties on powerful violators, and is exacerbated by regulatory capture and an inefficient or corrupt enforcement system.

6. **Non-transparent market functioning.** Inconsistent rule enforcement, closed procedures, and selective decision-making allow preferential treatment for certain players. The absence of clear rules, predictable procedures, and open information is a systemic flaw in the market model, creating benefits for a narrow circle of stakeholders and distorting market incentives.

Addressing these enablers requires institutional reform, stronger state-owned companies governance, independent and capable regulator and law enforcement, and a transparent, rule-based market environment.

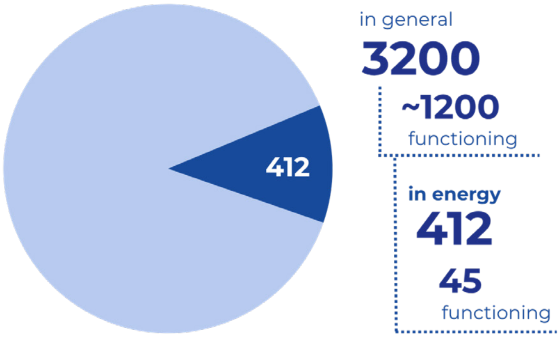
1.

Ukraine still maintains has an excessive number of state-owned enterprises: as of 2022, there were around **3,200,** of which only **about 1,200** were actually functioning. In the energy sector, there are **412** enterprises subordinated to the Ministry of Energy, most of which are either located in temporarily occupied territories or in a state of bankruptcy. **Only 45 operate fully.** Managing such a system is extremely resource-intensive and inefficient.

Among the key recommendations is the transparent privatization of non-strategic energy assets. The OECD recommendations also include the possibility of establishing a state institution for managing state property or a commercial structure with similar functions. However, these measures will be effective only if the energy sector undergoes comprehensive reform, **since corruption persists where recommendations are implemented selectively.**

The number of state-owned enterprises

in Ukraine



in OECD countries

Hungary	**370**
Czech Republic	**133**
Lithuania	**128**
Poland	**126**
Slovak Republic	**113**

Data source: Analysis of Corruption Risks and Practices in theUkrainian Energy Sector by the Ukraine Facility Platform, citing data from the Organisation for Economic Co-operation and Development.

2.

Failures in state-owned enterprises of corporate governance and abuses of power are prevalent in Ukraine's energy sector. Cases at Energoatom, Ukrenergo, Guaranteed Buyer, and Ukrainian Distribution Grids (UDG) show delayed or incomplete corporatization, non-compliant or politically controlled boards, and conflicts of interest. The Ministry of Energy has used opaque appointment processes, restricted board powers, and bypassed oversight to maintain manual control over strategic enterprises. Improvements require centralized recruitment or donor-funded independent oversight, plus pre-set contracts to prevent post-appointment manipulation.

These practices pose challenges for companies. For instance, the Ministry of Energy's management across UDG and Ukrenergo creates a vertically integrated business entity involved in electricity distribution, transmission, and supply, which risks Ukrenergo's certification as a transmission system operator (TSO).

Another example: state-owned coal mines receive subsidies, accumulate debts, and produce unneeded commodities. Restructuring is necessary, involving the closure of some mines and increased production at others based on actual needs. This could save USD 100 million annually in coal industry subsidies within two years.

Issues with the corporate governance of state-owned enterprises

JSC NNEGC Energoatom	Supervisory Board delayed first meeting for seven months after appointment; loss of independent majority not rectified by the Government
NEC Ukrenergo	Ministry of Energy failed to appoint a fourth independent member from 2022 to late 2024, resulting in a non-compliant board composition
Guaranteed Buyer	The corporatization remains incomplete since mid-2023, raising concerns about the government's ability to complete such transformations
JSC Ukrainian Distribution Grids	The Ministry of Energy, as 100% shareholder, appointed its Supervisory Board in 2023 without competition, including members with potential conflicts of interest
Market Operator	Ministry of Energy retroactively reduced Supervisory Board remuneration without consultation, violating Ukrainian law and non-interference principles

3.

The energy regulator lacks political independence. The Ministry of Energy has consistently expanded its influence over the National Energy and Utilities Regulatory Commission (NEURC). The Ministry controlled the commission selecting NEURC members by appointing former deput ministers, loyal allies, and individuals under criminal suspicion. Intimidation of candidates to limit competition and secure preferred candidates raises concerns about legality and transparency.

One example of the regulator's political dependence is the tariff policy regarding Ukrenergo. The state-owned transmission system operator, through its Public Service Obligations (PSO), pays renewable energy producers compensation for the difference between the "green" tariff and the market price of electricity. The source of these payments is the revenue from market participants for electricity transmission services, at a tariff set for Ukrenergo by NEURC. The regulator's systematic underestimation of the transmission tariff, whose increase would be disadvantageous for big business and state players on the market, has led to the tariff not covering Ukrenergo's actual costs of fulfilling its PSO. The result is a chain of debts between Ukrenergo and market participants and a liquidity crisis.

4.

Mutual debts are accumulating between market participants. The debt of the state-owned Guaranteed Buyer to renewable energy producers exceeds UAH 20 billion, hindering investment and causing financial instability. Another critical issue is balancing market debts: as of the beginning of August 2025, Ukrenergo owed market participants UAH 15.7 billion, while they owed Ukrenergo UAH 38.7 billion. Eliminating this imbalance is crucial for the proper functioning of the market and for forming correct price signals.

A particular problem is posed by enterprises that effectively do not pay for consumed electricity, such as state-owned coal mines and water utilities.

The main reasons for the debt crisis are:

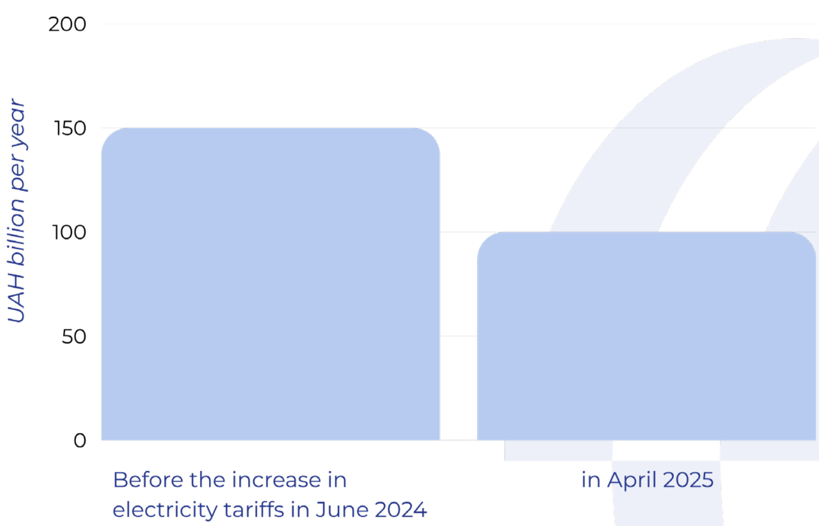
- the Ukrenergo tariff does not cover the company's costs of fulfilling PSO obligations;
- the absence of effective rules for disconnecting non-payers.

5.

Public service obligations (PSO) as a corruption factor. The PSO mechanism not only distorts the market and reduces efficiency but also creates corruption risks. It provides electricity subsidies for households without considering their consumption level or income. As a result, discounted price receive both households that genuinely need support and those, who able to pay the market price. The Government uses PSO as a tool of political advantage, which can be seen as a form of political corruption.

PSO obligations are imposed on the state-owned Energoatom and Ukrhydroenergo. These companies compensate electricity suppliers for the difference between the market price and the fixed tariff for households. At the same time, they do not receive reimbursement for these costs, which weakens their financial stability and creates additional opportunities for corruption.

The cost of Ukraine's public service obligation (PSO) scheme



Data source: Analysis of corruption risks and practices in Ukrainian energy sector by Ukraine Facility Platform.

6.

The construction of new generation capacity is complicated by inefficient resource use and weak coordination. The only coordination center – the Ministry of Energy – lacks sufficient competence. Distorted data on the amount of new capacity already operating in the power system create false market signals.

Another distortion is the absence of a mechanism for forming long-term price indicators. Today, the Day-Ahead Market segment determines the price for about 70% of non-household consumers, even though less than 20% of the annual electricity volume is traded there.

RECOMMENDED MITIGATION MEASURES

To address the risks outlined above, Ukraine must pursue a set of reforms, aligned with the EU and agreed and outlined prior to the invasion, that include full implementation of OECD recommendations, REMIT legislation, and market reforms, outlined in the Ukraine Plan and Reform Matrix. Measures to mitigate these risks should build on existing post-war recommendations, which have already proven their relevance.

The recommendations stated below must be implemented both promptly and in parallel and without delay, otherwise their effectiveness will be diminished.

RECOMMENDATION 1: REDUCE THE DOMINANCE OF STATE OWNERSHIP IN THE ENERGY SECTOR BY:

a) Strictly separating the commercial management functions of State-Owned Enterprises (SOEs) from the state's policy development and implementation roles;

b) Transparent privatization of non-strategic energy assets;

c) Establishing a centralized and professional management entity (such as a commercial structure or a dedicated state asset management institution) for strategic energy assets remaining in state ownership. This will only work if implemented as part of a comprehensive sector reform;

d) Ensuring transparency in the management of state-owned energy assets and protecting them from political interference.

RECOMMENDATION 2: STRENGTHEN CORPORATE GOVERNANCE IN LINE WITH OECD STANDARDS AND ENSURE PROFESSIONAL, INDEPENDENT MANAGEMENT IN STATE-OWNED ENERGY ENTERPRISES BY:

a) Implementing a fully transparent, merit- and reputation-based selection process for SOE's supervisory board members, ensuring international supervision;

b) Engaging independent recruitment agencies within a clearly defined financial framework: initial funding and integrity monitoring – covered by donors, followed by a transition to centralized selection financed from the state budget;

c) Defining, standardizing, and publicly disclosing competitive contractual terms for SOE's supervisory board members before the start of the selection process – to ensure transparency and mitigating risks of political influence or manipulation;

d) Mandating that all key state-owned energy enterprises (including Energoatom, Guaranteed Buyer, Ukrainian Distribution Grids, Market Operator, and Centrenergo) establish and maintain internal audit services that are directly accountable to their respective supervisory boards. This will enhance transparency, public control, access to information, and institutional capacity while significantly reducing opportunities for political corruption.

RECOMMENDATION 3: ESTABLISH A TRANSPARENT, FINANCIALLY VIABLE, AND EFFICIENTLY REGULATED ENERGY MARKET. HOW TO ACHIEVE THIS:

a) Reform the subsidy system. This means dismantling the current ineffective PSO mechanisms and replacing them with a system of targeted **direct monetary subsidies** for vulnerable consumers. This model can be financed through:

- Dividend payments to the state budget by Energoatom and Ukrhydroenergo. For this, legislative amendments should allow advance payments and calculation not from net profit, but from fixed income per share.
- Carefully structured donor contributions, where financing for subsidies is proportional to the dividends these enterprises pay to the state budget for other essential needs (including military expenditures), ensuring state-owned enterprises financial discipline;

b) Reform electricity disconnection procedures to enforce payment discipline. Any decision by the state or a territorial community to prohibit the disconnection of a specific consumer from the electricity supply must be accompanied by a **legally binding financial guarantee** from that authority to cover the consumer's energy payment obligations (e.g., a direct guarantee or bank guarantee).

RECOMMENDATION 4: CREATE STRONG INCENTIVES FOR REGIONAL ENERGY DEVELOPMENT. TO ACHIEVE THIS:

a) Withdrawing of the current **PSO** model and reforming of the associated support mechanisms will remove regulatory and market barriers to investment in new regional generation;

b) Establishing a clear and stable **regulatory framework** that enables viable business models for local energy producers, ensuring they can operate with transparent rules (e.g., grid access conditions, licensing and permitting processes), and opportunities to achieve profitability by investing in efficient and modern generation capacities;

c) Implementing **targeted financial instruments and incentives** to encourage investment in diverse local energy projects.

FINAL RECOMMENDATIONS

Based on this study, it is important to specify that the government should either **formalize all informal approaches** applied during the period of martial law or cease using them. As for anti-corruption institutions, especially in law enforcement bodies handling energy-related cases, there is a critical need to **enhance specialized expertise on the energy sector** – both through internal capacity-building and by engaging qualified sectoral experts.