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EU–UKRAINIAN RELATIONS IN THE LIGHT OF
THE NEW AGREEMENT. UKRAINE'S EXPECTATIONS
AND REALITIES



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FOREWORD

This paper is one of several studies done at the Hungarian Academy of Sciences' Institute for World Economics (IWE) under the CIS Strategic Research Project. A contract between the Hungarian Prime Minister's Office and the Hungarian Academy of Sciences in the summer of 2007, allowed some new, wide-ranging thematic research into the post-Soviet space to be launched. The project entitled "Hungary's CIS strategy with special regard to Russia, Ukraine and Kazakhstan" gave new impetus to post-Soviet research in the IWE and its partner the Hungarian Academy of Sciences' Research Institute of Sociology. The new opportunity was important especially because the CIS or post-Soviet space had become a neglected area in Hungary over the previous 15 years and there was a research gap to fill.

Meanwhile the post-Soviet space has been returning to the political agenda in the last year or two, due to rising ambitions in a strengthened Russia, sharp conflicts within the post-Soviet space, and worldwide problems of energy supply and prices. The research seeks to provide up-to-date answers to such emerging questions.

The project sets out to cover a wide range of essential issues about the CIS space, notably the three most important countries for Hungary: Russia, Ukraine and Kazakhstan. It deals with the issues such as the regional energy prospects, the integration and disintegration processes among the CIS states, the formulation of relations with the European Union and with other important actors worldwide, and the effects of the world economy in the region. In conjunction with the key economic questions, it examines the current social and political changes and the various political systems.

The intention is to create not just a network of Hungarian specialists on the post-Soviet space, but an international network of researchers from these newly independent states. Inviting outside researchers and think-tanks to join us in this project was a first step. The IWE is currently working with Russian and Ukrainian partners.

This paper by Volodymyr Sidenko, principal researcher at the Institute for Economics and Forecasting of the National Academy of Sciences of Ukraine and corresponding member of the National Academy of Sciences of Ukraine, analyses a very important and challenging issue of the prospects for the forthcoming agreement between the European Union and Ukraine. What are its possible contents, with special regard to its economic dimension, and most importantly to the general European answer of Ukraine's European ambitions?

Zsuzsa Ludvig
project leader

1) THE GENERAL FRAME- WORK OF THE PROBLEM

The Partnership and Cooperation Agreement (PCA) between Ukraine and the European Communities—concluded in June 1994 and in force since March 1998—has reached the end of its ten-year term of validity. In its final three-year stage, it has been substantially augmented by a bilateral three-year EU/Ukraine Action Plan, signed on February 21, 2005, which served as a tool for reaching the main PCA objectives and extending cooperation into new fields, in view of the EU enlargement process.

Now, the “PCA + Action Plan” format is to give way in the near future to a New Enhanced Agreement (NEA) that will bring EU–Ukrainian relations to a new level and define the prospects for Ukraine’s future integration into the European structures. The negotiating parties agreed that the NEA would go beyond the PCA and Joint Action Plan wherever possible. But in view of ongoing NEA negotiations which have not been completed before the expiry date of the PCA and the 2005 bilateral Action Plan, both documents are still valid until the new agreement has been reached. So the Action Plan will remain in force for a maximum of one more year, and for this purpose it has been supplemented with additional specific measures of cooperation for 2008 (outlined later in this paper).

It is stated, “By the end of 2008/beginning of 2009 both sides will develop a *new joint tool* (‘guideline’, ‘action plan’, ‘road map’ or other name yet to be decided). This will take account of the issues to be agreed by then in the NEA negotiations and prepare for the NEA’s entry into force.” It was also agreed that the current NEA negotiations are to be concluded in 2009.¹

The formal negotiations on a new agreement have been underway since March 2007, and several rounds have taken place. The first covered such items as the structure of the negotiation process and the future agreement, its basic elements and principles. Subsequent rounds and special working-group meetings concentrated on the content of relevant articles of the future Enhanced Agreement.

Of special socioeconomic interest here are the talks in Working Group No. 3 on economic and sectoral cooperation and the development of human resources, and in No. 4 on trade cooperation (creation of a free trade area). WG No.3 considers 27 separate fields of cooperation, from energy and transport to culture and tourism. According to the Ukrainian Ministry of the Economy, there has been substantial progress in discussion on such items as macroeconomic cooperation, social policy, research and technological development, nuclear energy, cooperation in mining and metallurgical industries. There are full-fledged ongoing discussions on the content of future relations

¹ Joint Evaluation Report. EU/Ukraine Action Plan. Brussels/Kyiv, March 2008, 1 and 9. http://www.delukr.ec.europa.eu/files/eu_ukraine/ukraine_eu_joint_evaluation_2008_en.pdf.

in education and training, the energy sector, industrial policy and entrepreneurship, company law and establishment, audiovisual policy, transport, the information society, environmental protection, cross-border and regional level cooperation, taxation, and public finance and financial control. Lagging somewhat are discussions on tourism and public health-sector policy, housing, and communal services development.

Alongside these discussions on the NEA there have been formal negotiations on the core element of a deep and comprehensive Free Trade Area. These were launched on 18 February 2008, just after the positive decision of the WTO General Council on Ukraine's accession.

Currently, it is not easy to estimate accurately the prospects of a negotiated NEA, especially in view of the customary non-disclosure of the contents of trade talks before completion. But certain predictions can be made, based on the general environment of EU/Ukraine relations, the achievements in improving the institutional framework in Ukraine, and the structural features of mutual flows of trade and investment.

Ukraine has come a long way with its reforms, notably in convergence of the country's economy (and society) on European standards, so that it looks quite different from what it was in the early 1990s. Ukraine today is basically a market economy. It has been a member of the WTO since May 16, 2008, and it is objectively ready for further comprehensive cooperation and integration with the EU. But there remains much uncertainty about the specific model for cooperation and integration—its substance, structure, and terms. This

uncertainty derives from differences of vision between Ukraine and the EU as to what has been achieved and what is especially desired.

The EU approach to this matter² (although there may be some differences between member-states) inclines towards a step-by-step approach proceeding from the previous EU *model of neighbourhood*.

The general EU approach is quite definite and understandable: to move ahead only in line with achieved institutional improvements in its neighbour countries, to bring them closer to EU norms in different areas. Perhaps the most radical economic element in this approach is the idea of a deep Free Trade Agreement (FTA) to provide conditions for further liberalization of mutual economic relations in the context of progressively adapting the Ukrainian business framework to the European norms of the *acquis communautaire*. EU seems reluctant to make at present any political commitments that could later

² Several basic documents were recently adopted in the EU with regard to Ukraine (or directly relating to it in a multilateral framework), including: the European Neighbourhood and Partnership Instrument. Ukraine. Country Strategy Paper 2007–2013; European Neighbourhood and Partnership Instrument. Ukraine. National Indicative Programme 2007–2010; Commission of the European Communities. Communication from the Commission to the Council and the European Parliament. Black Sea Synergy—A New Regional Cooperation Initiative. Brussels, 11 April 2007, Com (2007) 160 Final; Commission of the European Communities. Commission Staff Working Document Accompanying the Communication from the Commission to the Council and the European Parliament 'Implementation of the European Neighbourhood Policy in 2007'. Progress Report Ukraine, Brussels, 3 April 2008, Sec (2008) 402; Commission Staff Working Document Accompanying the Communication from the Commission to the Council and the European Parliament 'Implementation of the European Neighbourhood Policy in 2007' Sectoral Progress Report, Brussels, 3 April 2008, Sec (2008) 403.

be seen as explicit or implicit content for Ukraine's full accession to the EU. So it is reluctant to commit itself to the official Ukrainian idea of "associated membership",³ especially if this is treated as European Agreement of the kind granted to CEE countries, giving them status in the 1990s as EU candidate-states.

Of course, this EU stand characterizes mainly the approach of the Council and the European Commission—the European Parliament is more sympathetic to Ukraine's official aspirations. The European Parliament resolution of 15 November 2007 on strengthening European Neighbourhood Policy⁴ admits that "democratic neighbours which are clearly identifiable as European countries and which respect the rule of law may in principle apply, pursuant to Article 49 of the Treaty on European Union, for membership of the EU, and that the pace and depth of a common European process should correspond as closely as possible to the abilities to implement the appropriate reforms and meet conditions (Copenhagen criteria) in the partner countries and in the EU" (Article 25). In Article 26 it reiterates the view stated in Parliament's recommendation of 12 July 2007 to the Council on a negotiation mandate for a

new enhanced agreement between the European Community and its member-states of the one part and Ukraine of the other part that the current negotiations with Ukraine "should result in the conclusion of an association agreement which contributes efficiently and credibly to Ukraine's prospects in Europe and initiates the corresponding process, including the possibility of EU membership."⁵ Unfortunately, the European Parliament's position is only a recommendation; it does not commit the European Commission or the Council to take such action.

The Ukrainian official stand on this looks rather different. Ukraine, of course, is not devoid of economic motivation and supports the idea of an FTA. But these questions are subordinate to a much more significant matter: the leadership's obsession with the idea of receiving from the EU formal approval for its "European aspirations"—not in terms of verbal support (heard regularly from Brussels and the capitals of EU member-states), but in the form of a judicial commitment. In the Ukrainian version of the NEA it would mean not just an FTA arrangement but an explicit grant of association status, with defined prospects of future membership. Ukrainian officials claim that Ukraine has already surpassed the narrow boundaries of neighbourhood policy and needs a more extensive field for development of mutual relations, like what was granted in the 1990s to the candidate CEE

³ Interestingly, the legal provisions of the European Union (European Community) do not formally envisage an associated *membership* status; there is a status of association which does not refer to *membership*. See: Part Four (Articles 181–8) of the Treaty establishing the European Community and the Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community, which will make Articles 198–204 in the Treaty on the Functioning of the European Union

⁴ European Parliament resolution of 15 November 2007 on strengthening the European Neighbourhood Policy (2007/2088(INI)). Text Adopted – P6_TA(2007)0538.

⁵ European Parliament recommendation of 12 July 2007 to the Council on a negotiation mandate for a new enhanced agreement between the European Community and its Member States of the one part and Ukraine of the other part (2007/2015(INI)). Text Adopted – P6_TA (2007) 0355.

countries under the so-called European Agreements.

This difference suggests a watershed between the two approaches. The European approach concentrates on a real, though gradual integration process, where the target of formal membership is a function of this process and real outcomes. The Ukrainian approach is basically politically motivated. The EU's approach seems to lie mainly within the usual domain of a neo-functional approach (extensively used at earlier stages in the development of the European Community), with its emphasis on gradualism and so-called spillover effects (where economic instruments matter more than political targets), the Ukrainian proposals originate from a different intellectual sphere of "social construction", where social values and associated political objectives prevail over purely economic motivations.⁶

Which of these approaches is to take the upper hand, or whether there will be a sort of compromise between them, depends not only on the parties concerned but on certain geopolitical considerations. Europe is concerned about its further relations with Russia and will not be eager to intrude on territory that is of explicit geopolitical interest to Russia. (There is ample evidence of this concern in discussion of the problems of possible Ukrainian membership of NATO. It would not be viable to incorporate Ukraine at the expense of further deterioration in EU-Russian relations, at least for its leading members—Germany, France, Italy and others. So

any new agreement would probably be, first and foremost, a diplomatically balanced document with open options for its further interpretation.

While the political contents of the future enhanced agreement still appears rather indefinite and determinable within an "association vs. enhanced (neighbourhood) cooperation" formula, the issue of an accord on a FTA looks formally unchallenged. But it leaves many open concrete questions as to the real contents, structure and timing of a future FTA.

Unfortunately, the analyses of this issue performed so far do not provide compelling evidence of a significant positive impact of this arrangement on Ukraine's economy, while its effects for the EU appear to be minor. Among various options for setting up a free-trade area, the EU evidently prefers a deep free trade (FTA+) option that would incorporate a set of existing (maybe expanded) commitments under the ENP Action Plans.

However, the FTA+ formula ignores the substantial differences of the parties in terms of level of economic development, maturity of market institutions, cultural foundation, political tradition, and geopolitical stand, and the capacity of Ukraine to perform rapid institutional changes in the direction of Europe, due to the huge implementation costs of internal restructuring. And there are excessive risks implied in compounding the difficulties of adapting to WTO norms with adjustment problems to do with an FTA with a far more competitive partner.

⁶ It should be emphasized that similar social-value arguments were widely used by CEE countries during the last wave of accessions, despite their problems in terms of economic readiness for European integration.

A more viable agenda for an FTA might be priority for the institutional capacity factor and a differentiated approach to rapid/gradual, deep/shallow FTA, depending on specific balances of interests in different sectors of the economy: asymmetrical FTA formation in favour of Ukraine, with the EU taking the lead in liberalization.⁷

2) DEVELOPMENTS IN UKRAINE'S IMPLEMENTATION OF ECONOMIC AND SOCIAL OBJECTIVES IN THE BILATERAL ACTION PLAN WITH THE EU

Ukraine made some progress towards meeting EU standards during 2007. It had success in implementing many targets outlined in the EU/Ukraine Action Plan (*Table 1*), which was aimed at implementing the PCA and creating the necessary conditions for further agreement between the parties.

Of course, the outlined record of implementation of the EU/Ukraine bilateral Action Plan is only part of the work performed in this context. But it gives us a full idea of the gradual approach of Ukraine towards targets mutually set for its European integration activities. It is important to emphasize that according to the Joint Evaluation Report on the EU/Ukraine Action Plan

⁷ For more detail, see Sidenko, Volodymyr: EU/Ukraine relations in the context of a possible free trade agreement, *EU Working Papers* (Budapest), 3/2007, 3–18.

as of March 2008,⁸ the EU and Ukraine have agreed that good progress has been achieved in implementing the plan. This finding is a major prerequisite for enhancing the cooperation format in future.

Nevertheless, it should be borne in mind that there are failures as well as to address on certain important issues. The report mentioned identifies a number of problematic issues to be solved (*Table 2*).

These problems are quite numerous and profound. They contradict the frequent claims by Ukrainian officials that Ukraine has outgrown the bounds of the ENP Action Plan. This is untrue, which is why the EU is in no hurry to finalize negotiations with Ukraine on the NEA, so leaving open the chance of better conformity with its objectives and measures to be taken.

3) DEVELOPMENT OF EU/UKRAINE TRADE AND INVESTMENT AS A FACTOR IN THE PROSPECTS OF COOPERATION

Factors to bear in mind in analysing EU/Ukraine relations include the dependence between the institutional forms of relations of the EU and Ukraine, and the intensity of the trade and investment flows between them. This relationship can be examined from several points of view.

⁸ Joint Evaluation Report. EU-Ukraine Action Plan. Brussels/Kyiv, March 2008.

Table 1
Key measures taken towards the main objectives of the bilateral three-year EU/Ukraine Action Plan signed on February 21, 2005

Articles ⁹	Implementation
2.3. Trade, market and regulatory reform	
Trade relations	
(25) <i>Full implementation of PCA commitments in trade in goods, including:</i> Gradual liberalization of trade in steel products and gradual removal of export duties on ferrous scrap in line with the EU-Ukraine bilateral steel agreement, ahead of full liberalization on Ukraine's accession to the WTO.	Agreement on Trade in Certain Steel Products, signed in Luxembourg on June 18, 2007. With that, Agreement on the extension (to 31 December 2007, with a possibility of tacit renewal for 2008), and amendment of the Agreement between the European Community and Ukraine on trade in textile products, concluded on March 28, 2007. But both are now to be suspended due to Ukraine's accession to the WTO.
(26) <i>Accession to the WTO, including:</i> Implementation of Ukraine's bilateral commitments and of requirements of WTO rules; Address specific non-tariff issues raised by the EC, including through the appropriate commitments in the WTO Working Party report.	The Ukraine Parliament (Verkhovna Rada) adopted in 2007 11 pieces of legislation adapting the Ukrainian trade regime to WTO rules, including: the state system of biological security in creating, testing, and practical utilization of genetically modified organisms; safety and quality of foodstuffs; export duty on waste and scrap ferrous metals; scrap doped metals, non-ferrous metals and semi-finished products made thereof; export duty rates for certain sorts of oilseeds; standards, technical regulations and conformity assessment; the order of settlements in foreign exchange; customs tariff of Ukraine; insurance; protection of intellectual property; value-added tax (withdrawing preferences for agricultural producers). The process culminated on February 5, 2008, when the WTO General Council adopted its decision on Ukraine's accession to the WTO. The accession package was ratified by Verkhovna Rada on April 10, 2008 and submitted to the WTO Secretariat, giving Ukraine membership status since May 16, 2008.
(27) <i>Under Article 4 of the PCA and in the light of advances in economic reform and implementation of PCA commitments, joint consideration of the feasibility of establishing a Free Trade Area after Ukraine's accession to the WTO.</i>	Three rounds of talks took place in February, April, and September 2007 within the frame of informal technical consultations on FTA creation. They were devoted to such problems as regulatory reforms; investment and establishment in certain fields (financial services, telecommunications, transport and postal services); cooperation in the field of technical regulation, harmonization of standards and conformity assessment procedures; government procurement; intellectual property protection, etc. In June 2007, the parties considered a preliminary draft structure for the future FTA. During a sixth round of consultations in September 2007, the parties discussed questions of cooperation over non-tariff barriers in trade, tariff liberalization within an FTA, rules of origin, trade facilitation, i.e. streamlining customs procedures. The January 2008 round of consultations was devoted to sanitary and phytosanitary measures.
<i>Customs</i>	
(28) <i>Elaborating and implementing customs legislation aligned with international and EU standards, including:</i> * Finalized implementation of legislation for the Customs Code, in line with internationally recognized standards, especially WTO agreements in par-	According to the act amending the Customs Code of Ukraine adopted on May 31, 2007, the latter was brought in conformity with the 2002 version of the Harmonized System (HS-2002) and the EC Combined Nomenclature (in force since January 1, 2008). Preparation is underway (according to a Cabinet of Ministers' Regulation of March 19, 2008) to adopt further amendments bringing the Customs Code into conformity

⁹ EU/Ukraine Action Plan. – DG E VI. UE-A 1051/05. ANNEX. Available at <http://www.delukr.ec.europa.eu/>.

Articles ⁹	Implementation
<p>particular in the area of customs value, and with the EU Customs legislation.</p> <ul style="list-style-type: none"> * Further revision of the Customs Code, taking into account EU legislation and previous * recommendations. * Ukraine to adopt and keep up to date the Harmonized System in use, with a view to adopting the Combined Nomenclature in the longer term, as agreed in the PCA. 	<p>with the 2007 version of the Harmonized System. Progress has been made on legislative approximation with the EU, upgrading the capacity of the customs service, and improving relations with economic operators. There have also been positive developments in facilitation and speeding up of customs procedures, including measures to implement the concept of a “single window” at borders. Start of negotiations on 18 February 2008 on the deep and comprehensive Free Trade Area, to form a core element of the New Enhanced Agreement.</p>
<i>Elimination of restrictions and streamlined administration</i>	
<p>(31) <i>Facilitating the movement of goods through (i) prevention of quantitative restrictions, (ii) gradual elimination of import licences and (iii) progressive removal, and prevention of new discriminatory measures. Improving institutional and administrative cooperation.</i></p>	<p>Following introduction of grain export curbs in 2006 and similar export restrictions in other areas, Ukraine has agreed that for the future such curbs will be temporary; should be introduced only when really needed, in a fully justified and transparent manner, taking into account Ukraine’s legal obligations; and should be implemented in a non-discriminatory manner.</p>
Standards, technical regulations and conformity assessment	
<p>(30) <i>Continuing alignment of Ukraine with EU and international regulatory and administrative practices and preparing for Ukraine’s participation in the EU internal market in selected priority industrial sectors, including:</i></p> <p>Jointly identifying priority sectors for alignment with EU and international regulatory practices and possible inclusion in an Agreement on Conformity Assessment and Acceptance of Industrial products, (ACAA), including consultations with producers and exporters.</p> <ul style="list-style-type: none"> • Harmonizing the necessary framework and sectoral legislation with EU technical regulations in priority sectors. 	<p>Ukraine negotiated and started to implement the Agreement of Conformity Assessment and Acceptance of Industrial Products (ACAA), with many legislative and normative changes introduced.</p>
<i>Intellectual and industrial property rights</i>	
<p>(41) <i>Ensuring a level of protection similar to that in the EU, including effective means of enforcement, in line with provisions in Article 50 of the PCA, including:</i></p> <ul style="list-style-type: none"> * Ensuring implementation and effective enforcement of TRIPS –compliant legislation on Ukraine’s accession to the WTO. * Enforcing legislation on trade marks and geographical indications. * Continuing to harmonize legislation to EU legislation in intellectual and industrial property rights protection. 	<p>Consultations were initiated on the subject of an agreement dealing with protection of geographical indications. To deepen cooperation in this priority area, the European Commission and Ukrainian authorities set up a specialized bilateral Dialogue on Intellectual Property Issues, which has met twice a year since 2006.</p>
2.5. Transport, energy, information society and environment	
<i>Transport</i>	
<p>(46) <i>Elaborating and starting to implement a national transport strategy, including transport infrastructure devel-</i></p>	<p>Two important projects are being currently implemented: introduction of high-speed passenger trains on Ukrainian railways (USD 200 million, including a USD 120 million loan from the</p>

Articles ⁹	Implementation
<p><i>opment, i.e.:</i></p> <ul style="list-style-type: none"> * Developing an infrastructure policy to identify and evaluate priority infrastructure projects in various sectors and continuing to participate in joint development of Pan-European Corridors and Areas, and in the TRACECA programme. * Identifying and committing resources to financing and adopting financing strategies, also in the light of the decision to extend EIB lending. Addressing issues of infrastructure financing (<i>e.g.</i> PPP, shadow-tolling, <i>etc.</i>) 	<p>EBRD); maintenance of the automobile road M-06 Kyiv–Chop, its Kyiv–Brody section (€668 million, with a €200 million loan from the EBRD, and €200 million from the EIB). Preparatory work is underway for a joint project with the EBRD and EIB on construction of a 750 kW electric power line from the Rivne Nuclear Power Plant to Kyiv (€364 million). The project was approved by the EBRD Board of Directors (November 6 2007). The Ukraine Ministry of the Economy prepared in December 2007 a list of promising projects to be financed by the EIB in the fields of the energy sector, energy saving, and transport infrastructure.</p> <p>A Concept for development PPPs in Ukraine in 2007–12 has been prepared.</p>
Energy	
<p>(51) <i>Adoption of an overall energy policy converging towards EU energy policy objectives, including:</i></p> <ul style="list-style-type: none"> * Preparing and adopting, by the appropriate instance, sub-sectoral energy policy documents with an indication of possible financing sources for implementation. * Reinforcing EU–Ukraine energy policy cooperation. 	<p>Ukraine obtained observer status in the Energy Community Treaty (ECT) in 2006, and in 2007 its application for full membership was formally welcomed by a meeting of energy ministers from ECT member-countries. The Ukraine Ministry of the Economy prepared in December 2007 a list of promising projects to be financed by the EIB in the fields of the energy sector, energy saving and transport infrastructure.</p>
<p>(53) <i>Progress regarding energy networks, including:</i></p> <ul style="list-style-type: none"> * Feasibility analysis of electricity interconnection of Ukraine with the UCTE synchronous network. 	<p>Progress was also made towards analysing Ukraine’s possible interconnection with the Union for the Coordination of Transmission of Electricity (UCTE).</p>
<p>(57) <i>Continuing cooperation on nuclear energy and nuclear safety, including:</i></p> <ul style="list-style-type: none"> * Complying with internationally accepted nuclear safety standards in completing and starting-up of K2R4 nuclear reactors; fully implementing the Memorandum of * Understanding on the closure of the Chernobyl nuclear power plant. * Taking necessary measures to ensure the entry into force and implementation of the agreement with EURATOM on peaceful uses of nuclear energy. * Continuing work on the Shelter Implementation Plan to transform Unit 4 of Chernobyl NPP into an environmentally safe site. 	<p>The Commission and Ukraine agreed to launch a joint project, with involvement of the International Atomic Energy Agency, on evaluation of the nuclear safety of Ukraine’s nuclear power plants. The contracts for Interim Spent Fuel Storage Facility (ISF–2) and for New Safe Confinement for the Chernobyl unit 4 (NSC) were signed in September 2007.</p>
Science and technology, research and development	
<p>(63) <i>Prepare Ukraine’s integration into the European Research Area, including:</i></p> <ul style="list-style-type: none"> * Finalizing the specific “Action plan to enhance cooperation between EU and Ukraine in the field of science and 	<p>The EU 7 Framework Programme in the field of research is now open to Ukrainian scientific institutions. Ukrainian science policy has been oriented towards attaining associate membership status in the Research Framework Programme.¹⁰ The Ukraine Ministry of the Economy has developed a draft</p>

¹⁰ Joint Evaluation Report. EU-Ukraine Action Plan. Brussels/Kyiv, March 2008, p. 7.
http://www.delukr.ec.europa.eu/files/eu_ukraine/ukraine_eu_joint_evaluation_2008_en.pdf.

Articles ⁹	Implementation
technology ⁷ .	Framework Agreement between Ukraine and the European Community on Basic Principles of Ukraine's Participation in Community Programmes, ¹¹ which would be implemented through specific working arrangements. On January 25, 2008 the Agreement between Ukraine and the European Space Agency (ESA) on space cooperation in peaceful purposes was signed.
<i>Education, training and youth</i>	
<p>(66) <i>Reform and upgrade the education and training systems and work towards convergence with EU standards and practices.</i></p> <p>(67) <i>Enhance cooperation in the field of education, training and youth.</i></p>	Ukraine continues with reforms to enable the country to contribute to the creation of the European Higher Education Area. Both sides have agreed on the importance of Tempus as a support instrument in this reform, and of promoting also the possibilities offered for cooperation activities and mobility of teachers, students and young people under the Erasmus Mundus, Erasmus Mundus External Cooperation Window, the Youth in Action programmes, and the Jean Monnet Action for teaching projects in European integration studies.
<i>Cross-border and regional level co-operation</i>	
<p>(70) <i>Enhance contacts and cooperation at the cross-border and regional level with neighbouring new EU member-states by taking up the opportunities and challenges arising from EU enlargement, i.e.:</i></p> <p>* Providing support to the regions and participating in preparing and implementing the Neighbourhood Programmes involving Ukraine.</p>	Several important projects are being implemented, <i>i.e.</i> : the Neighbourhood Programme Ukraine–Hungary– Slovak Republic envisages for 2008 16 cross-border cooperation projects with total budget financing of UAH 6.62 million. With the aim of granting the necessary technical and financial assistance in implementing the Action Plan (including the objectives of cross-border and inter-regional cooperation) the European Commission has developed a new European Neighbourhood and Partnership Instrument (ENPI). Currently, extensive work is being performed to develop and approve joint programmes for the cross-border cooperation Ukraine–Hungary–Slovak Republic–Romania, Ukraine–Poland–Belarus, Ukraine–Romania–Moldova, and Black Sea.

Source: Ministry of Economy of Ukraine. Information on the State of Implementation of the Measures Envisaged by the Ukraine–EU Action Plan: 2007 Report; Joint Evaluation Report. EU/Ukraine Action Plan. Brussels/Kyiv, March 2008.

¹¹ This will provide conditions for the use of opportunities already created by the EU. See Commission of the European Communities. Communication from the Commission to the Council and to the European Parliament on the general approach to enable ENP partner countries to participate in Community agencies and Community programmes. Brussels, 4 December 2006, COM (2006) 724 final.

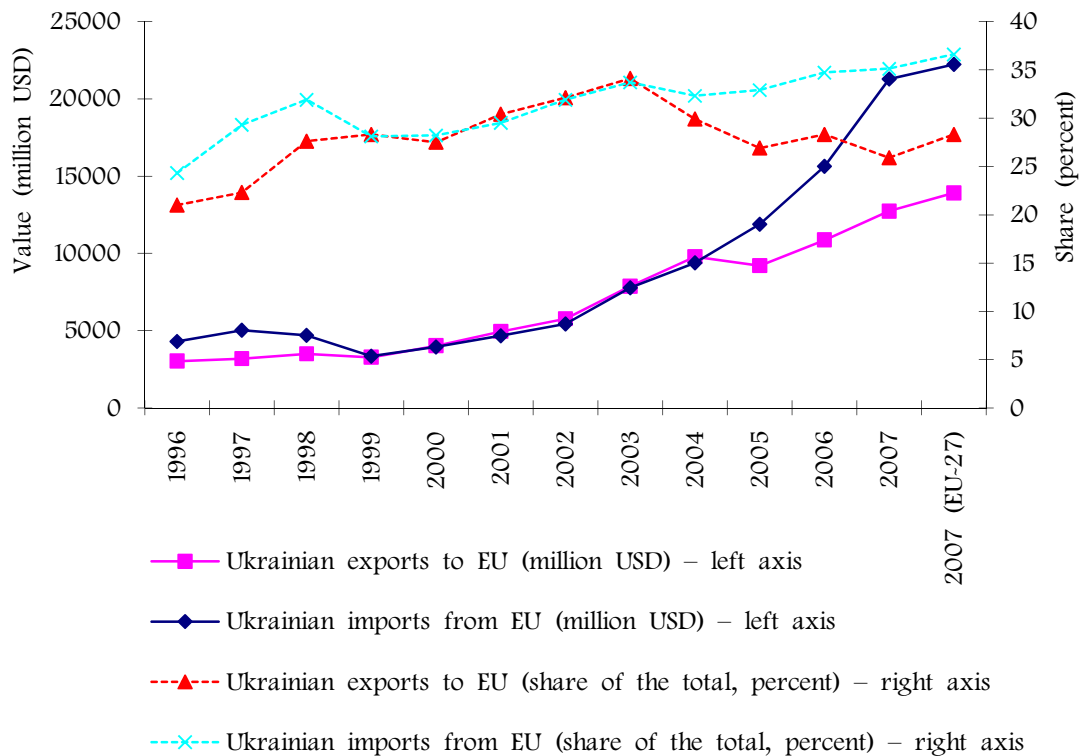
Table 2
Unresolved economic issues of the EU/Ukraine Action Plan

Section	Subsection	Substance of the problem
<i>Economic and social reform and development</i>	<i>Macro-economic developments</i>	Inflation has accelerated since 2007 (16.6% in 2007). State intervention in the economy through direct subsidies and tax breaks: should be disciplined and progressively reduced. Insufficiently open, transparent privatization procedures should be based on a formal mid-term privatization strategy. The ease of doing business has not shown tangible improvements: it remains a priority for the country, <i>i.e.</i> through wide-ranging tax reform, risk-based and less burdensome administrative controls, and simplification of the licensing system.
	<i>Social developments</i>	A shortage of qualified workers, a lack of quality jobs and the large share of the informal economy. The adoption of a new modern labour code is a priority for the government. Social dialogue needs to become more effective.
<i>Trade, market and regulatory reform</i>	<i>Trade</i>	The introduction of curbs on grain exports to Ukraine in 2006 and similar restrictions in other areas: for the future such curbs are to be temporary; should be introduced only when they are really needed, in a fully justified and transparent manner, taking into account Ukraine's legal obligations; and should be implemented in a non-discriminatory manner.
	<i>Business and investment climate</i>	Business and investment climate in Ukraine needs further steps of improvement, including a transparent, predictable legal and administrative framework as well as an independent judiciary.
	<i>Financial services</i>	Further steps are needed, including the adoption of rules on the introduction of disclosure rules regarding the ownership of banks; a unified approach to drafting of new legislation on insurance, to ensure closer conformity with relevant European and international rules and commitments.
	<i>Customs</i>	Further measures are needed to modernize customs procedures and fight corruption.
	<i>Technical standards</i>	The priority now is to focus on structural reforms of Ukraine's quality control system.
	<i>Sanitary and phytosanitary issues</i>	Ukraine has proposed to start discussions on a veterinary agreement, which is to be envisaged in the framework of the NEA.
	<i>Company law</i>	Further measures are needed, <i>i.e.</i> a new law on joint-stock companies; a new tax code to replace and consolidate more than 200 regulations in force; timely reimbursement of VAT refunds for exporters and economic operators generally; possible measures to implement new EU legislation on registration, evaluation, authorization and restrictions of chemicals (REACH).
	<i>Intellectual property rights</i>	Further measures are required regarding implementation and enforcement of the rules in this field.
	<i>Public procurement</i>	Changes in the legislative and administrative set-up in Ukraine have overall reduced transparency and hampered the efficiency of the public procurement system in Ukraine.
	<i>Statistics</i>	Discrepancies in trade statistics between the EU and Ukraine.
<i>Energy, transport, the information society and the environment</i>	<i>Energy</i>	More needs to be done to improve the safety of coal mines.
	<i>Transport</i>	Developing transport infrastructure as a key element of preparations to host the 2012 Euro football championships. Adherence to the Interbus Agreement. Negotiations on a comprehensive EU-Ukraine aviation agreement (started in December 2007).
	<i>Environment</i>	Key issues relate to air quality, water quality, waste management and nature protection.
	<i>Information society</i>	Functioning of the National Commission for Communications Regulation (NCCR) needs to be restored to ensure fair competition in electronic communications markets.

Section	Subsection	Substance of the problem
<i>People-to-people contacts</i>	<i>Research</i>	Further inclusion of particular topics of mutual interest in the 7th FP work programmes.
	<i>Education and youth</i>	Full utilization of opportunities offered by the Tempus programme and of promoting the possibilities offered for cooperation activities and mobility of teachers, students and young people under the Erasmus Mundus, Erasmus Mundus External Cooperation Window, the Youth in Action programmes, and the Jean Monnet Action for teaching projects in European integration studies.
	<i>Audio-visual policy</i>	Ratification of the Council of Europe Convention on Transfrontier Television.

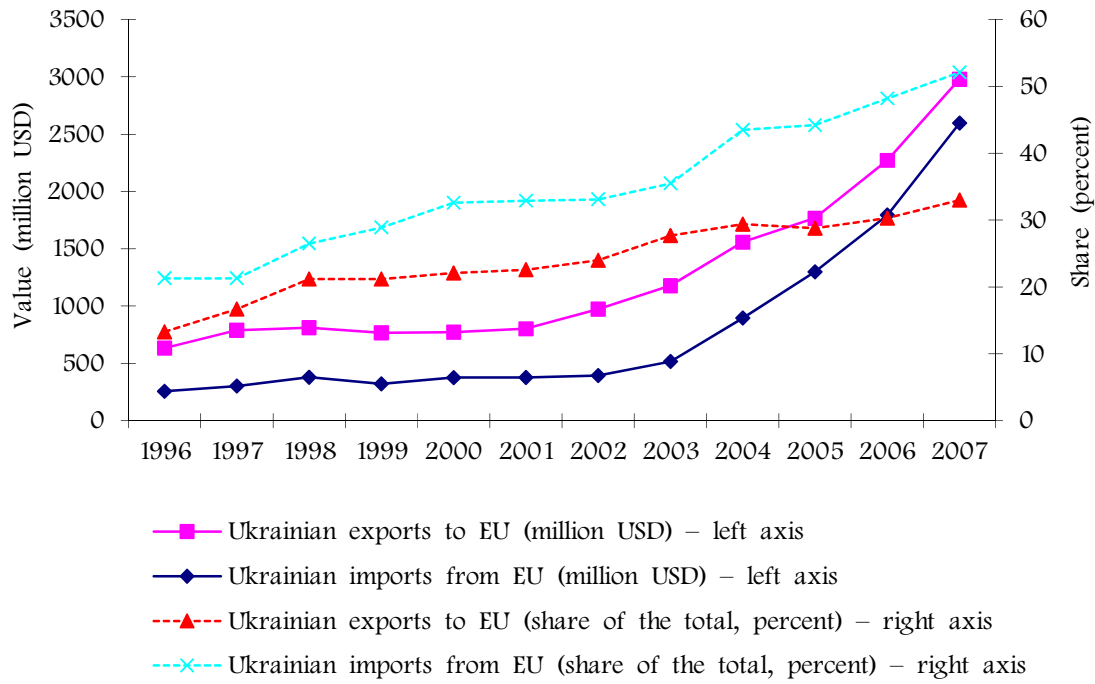
Source: Joint Evaluation Report. EU-Ukraine Action Plan. Brussels/Kyiv, March 2008.

Figure 1
Dynamics of Ukraine's goods trade with the EU, 1996–2007
(on an EU-25 basis over the entire period)



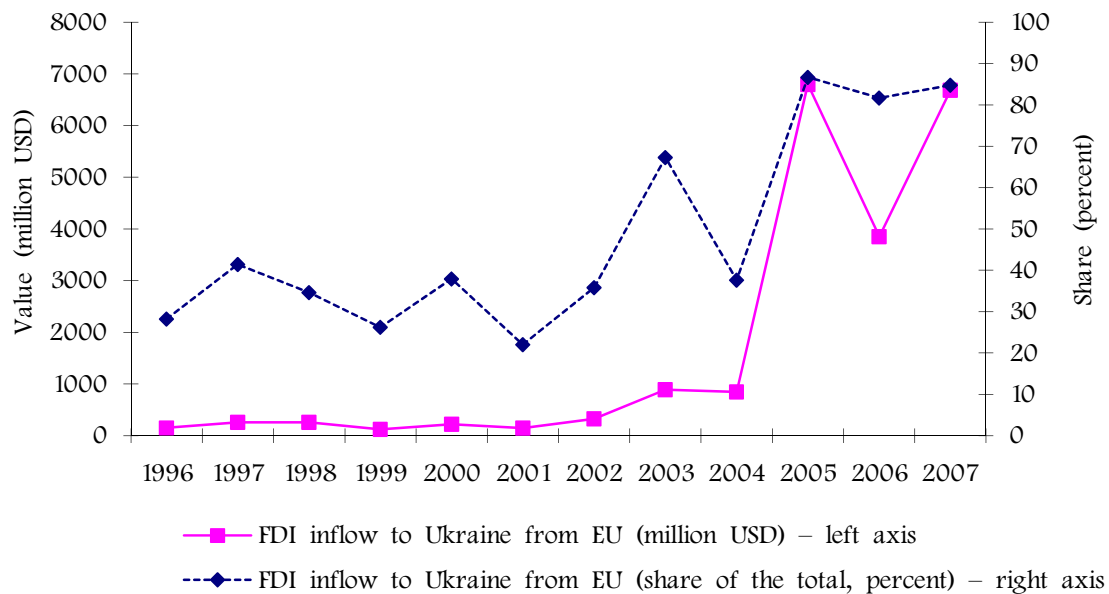
Source: State Statistics Committee of Ukraine, author's calculations.

Figure 2
Dynamics of Ukraine's trade in services with the EU, 1996–2007



Source: State Statistics Committee of Ukraine, author's calculations.

Figure 3
Dynamics of EU FDI inflows to Ukraine, 1996–2007



Source: State Statistics Committee of Ukraine: data for various years, author's calculations.

First, mutual trade flows have been showing explicit upward trends (*Figures 1 and 2*). Important here are not only the ever growing values of mutual exports and imports, but a distinct growth trend in the EU share in total Ukrainian imports (reaching in 2007 36.6 per cent for goods and 52.1 per cent for services, as compared to 24.3 and 21.3 respectively in 1996.) This is a convincing proof of a profound structural reorientation of Ukrainian imports in favour of the EU.

With Ukrainian exports to the EU, the picture is less clear. There is fairly rapid expansion of services exports, but the growth of goods supplies to the EU market has been rather moderate since the 2004 EU enlargement. In terms of total trade share, there is growing importance of the EU for services (33 per cent in 2007 as compared to only 13.3 per cent in 1996), but a decreasing trend in the indicator for goods exports: 28.3 per cent in 2007 (25.9 per cent for the EU 25), while in 2003 it was 34.1 per cent.

So the existing model of cooperation has asymmetry in favour of the EU. This has resulted in the period since the EU enlargement in ever lower growth rates of Ukrainian goods exports in comparison with the country's goods imports from the EU. It testifies to certain impediments to Ukraine's presence in the enlarged EU market, which will be of some concern to the parties negotiating the ENP, specifically during the talks on an FTA. These impediments refer primarily to the system of EU agrarian protectionism within the Common Agricultural Policy, the failure of some Ukrainian goods and services to meet European standards and technical

regulations (regarding consumer safety and sanitary and phytosanitary norms), and recurrent politically motivated high tech protectionism, some traces of which were seen, for instance, in aerospace and air cargo transportation.

The second dimension of this question relates to investment flows. As *Figure 3* shows, there has been a real breakthrough since 2006 in terms of the EU FDI inflows to Ukraine.

The total FDI stock of the EU in Ukraine reached on January 1, 2008 the equivalent of USD 22,944.5 million, making up a striking 77.8 per cent share in the total FDI stock of the country. For the three last years the EU share in total annual FDI inflows exceeded the 80 per cent mark.

Though this picture is an undoubted sign of growing integration with the EU, it bears strong marks of asymmetry. There has been only minor, negligible investment by Ukrainian companies in the EU, but this hides a far stronger process of hidden investment by Ukrainian business in some regions of the EU (e.g. Cyprus, with its offshore regime). But by 2007, there were noticeable signs of change in this situation. In 2007, the total amount of Ukraine's FDI in the EU rose from USD 74.8 million to USD 5926.4 million, of which USD 5825.5 million was invested in Cyprus.¹²

¹² This sizeable upsurge in outward FDI arises not only from improved statistical observations undertaken, *inter alia*, within the framework of measures against capital flight and money laundering, but largely reflect the growth of interest of Ukrainian financially robust companies in penetrating into the EU investment market. Cyprus here gains the evident priority as a *gate to this market*, taking into account the earlier created network of commercial relations, financial assets of Ukrainian banks, and offshore accounts of Ukrainian big companies.

Finally, in the third dimension of the problem, there has to be taken into account the relative significance of Ukraine as a trade and investment partner for the EU. This appears to be the most problematic aspect for Ukraine, as it is still not an influential player in the EU market, with, for instance, only about 1.1 per cent of total EU trade turnover (data for 2006).¹³ This limited presence is a major factor behind the restrained attitude of the EU to Ukrainian aspirations to be rapidly included in the EU structures.

4) THE NEAR FUTURE: ADDITIONAL OBJECTIVES FOR 2008

Both sides have agreed to take some additional specific measures in 2008, including the following issues:¹⁴

- * To continue negotiations on the NEA, including its deep and comprehensive free-trade area, with the aim of concluding these in 2009.¹⁵
- * To prepare a second joint progress report for the summit in the autumn of 2008 and seek by then overall understanding on the scope, main objective, principles and broad lines of the institutional framework.

¹³ Ukraine-EU: Bilateral Trade Relations. <http://www.delukr.ec.europa.eu/page36088.html>

¹⁴ Joint Evaluation Report. EU-Ukraine Action Plan. Brussels/Kyiv, March 2008, p. 9–10.

¹⁵ For a detailed analysis for the problems with the EU/Ukraine FTA see: Sidenko, Volodymyr. EU-Ukraine Relations in the Context of a Possible Free Trade Agreement, *EU Working Papers* (Budapest), No.3/2007, p. 3–18.

- * To cooperate closely on fully implementing the visa facilitation and re-admission agreements.
- * Based on successful implementation of the visa facilitation and readmission agreements, and taking into account the possibility of a visa-free travel regime referred to in its preamble as a long-term prospect, for both sides to envisage dialogue on this matter.
- * To continue consultations on possible EU use of Ukraine's long-haul aviation capacities.
- * To continue working on the Joint Stock Company and Procurement acts and the Tax Code.
- * To elaborate possible ways of cooperation on REACH.
- * To finalize negotiations on the Common Aviation Area Agreement.
- * To elaborate further and start to implement a national transport strategy, including priorities for transport infrastructure development, covering all transport modes, coherent with the EU's White Paper on transport and the High Level Group's report on the extension of Trans-European Transport Networks.
- * To reach a framework agreement that allows Ukraine's participation in European Community programmes and cooperate closely to implement it through specific working arrangements.
- * Building on the recent EU-Ukraine study on reform of the operation of the system of gas transit in Ukraine, to intensify cooperation to encourage investment in rehabilitation and upgrading of the infrastructure network for hydrocarbon transit, including in-

- creased transparency, and organize a pledging conference to help mobilize the necessary financing.
- * To continue and intensify cooperation with the aim of using the Odessa–Brody oil pipeline in the South–North direction and of extending it to Plock (Poland).
 - * To intensify cooperation aimed at Ukraine’s accession to the Energy Community Treaty.
 - * To launch exploratory talks on the Regional Environmental Centre (REC) in Ukraine.
 - * To speed up ratification of the Ukraine–EU Cooperation Agreement on Civil Global Navigation Satellite System (GNSS) by the EU side.
 - * To promote the conclusion of the Ukraine–Europol and Ukraine–Eurojust agreements.
 - * To continue consultations on reintroduction of joint customs and border controls at the borders of Ukraine with neighbouring EU member-states within the limits of the Schengen *acquis*.
 - * To promote the conclusion of bilateral agreements between Ukraine and neighbouring EU member-states on small border traffic.
 - * To consider measures in the sphere of employment and the treatment of migrant workers to ensure, in accordance with the PCA, that such treatment does not discriminate on grounds of nationality.
 - * To work closely in reforming the public administration system in Ukraine on the basis of an assessment by SIGMA.
- * To use, where appropriate, existing forms of cooperation to facilitate the Ukrainian side’s preparations for co-hosting the 2012 European football championships.
 - * To take appropriate steps to make an independent National Tempus Office in Ukraine fully operational in time for the new phase of the Tempus programme.
 - * To ratify the UNESCO Convention on the Protection and Promotion of Diversity of Cultural Expressions and the Council of Europe Convention on Trans-frontier Television.
 - * To discuss in the context of the Steering Committee on the EU–Ukraine Science and Technology Agreement, in the first half of 2008, *i.e.* the steps that would need to be taken for Ukraine to attain associate membership status in the Research Framework Programme.

5) CONCLUDING REMARKS

The mutual relations of Ukraine and the EU have been developing rather rapidly and have been bringing fruitful results in recent years, since the adoption of a bilateral Action Plan. Nevertheless, the list and scope of unresolved problems, the level of institutional readiness of Ukraine for intensifying its integration into EU structures, and the actual presence of the Ukrainian economy in the EU internal market are not yet sufficient to expect a radical breakthrough in terms of a new enhanced agreement

concluded in 2009. Most likely is a partially expanded and amended Action Plan aimed at continuation of the current step-by-step approach of the EU towards Ukraine's inclusion in the European integration process.

This kind of policy may also rest on such uncertain factors as Russian policy towards Europe, and not least, internal political conflicts in Ukraine accompanied by a deteriorating economic situation (rising rates of inflation and a threatening slowdown of economic growth, especially under the influence of prices for imported energy supplies).

Taking into account the internal problems of the EU, which faces substantial tasks in adapting new members and implementing internal institutional reforms, it seems doubtful that a rapid inclusion of Ukraine in the EU domain is a viable priority.

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