Chaillot Paper

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Ukraine: Quo Vadis?

Sabine Fischer, Rosaria Puglisi, Kataryna Wolczuk and Pawel Wolowski

Edited by Sabine Fischer

Institute for Security Studies
Institut d'études de Sécurité
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Preface

Álvaro de Vasconcelos

Ukraine is the litmus test for the European Neighbourhood Policy. Is it possible to extend democracy to countries that aspire to join the EU – which is universally recognised as a laudable aim – if the prospect of future EU membership is then denied to them? Ukraine is no ordinary neighbour, as this Chaillot Paper *potently illustrates, but is in the unique position of being a close neighbour of both the EU and Russia which has embarked on a course of far-reaching economic and political reforms. Under Sabine Fischer's guidance, the contributors to this paper, all of them renowned specialists in this field, take a hard look at the monumental task of making these reforms work. To make the challenge to the EU even more compelling, expectations regarding Europe's ability to fully integrate Ukraine are still as high as they were in 2004, when the European option was an unmistakable driver of the Orange Revolution, and such high hopes are equally shared by all those who see a future for Ukraine outside Russia's orbit.*

The ENP is being put to a decisive test in Ukraine for this is a case where it is rather exceptionally required to channel the EU's support to unequivocal democratic transition. A modern, democratic Ukraine is equated by large and influential parts of the political and economic elite with a European destiny – falling short of full membership – which they see as the natural outcome of the Orange Revolution. They look to belonging in Europe *therefore as a reassurance that there will be no turning back from a democratic constitution firmly grounded in the rule of law and, no less importantly, that the country will be a full partner in the world economy. This reassurance is interestingly sought by the post-Soviet capitalist oligarchy as well, as is highlighted by Rosaria Puglisi. There is no unanimity in the European Union for or against future membership of the Ukraine, which is currently favoured only by a handful of Member States. Many will object that the ENP was never intended as a 'waiting room' where hopefuls are coached to get ready to join. Echoing the official discourse, most will argue that it is rather a border-setting mechanism where near-membership begins but the hope of full membership definitely ends. The truth is that the finalité of the ENP remains undecided. In its more developed stages, it translates into full*

integration within the European economic area plus advanced political cooperation. In this sense, the ENP is largely EU-driven and broadly amounts to a gradual 'internalisation' of the acquis communautaire*, rather unglamorous and highly technical in content. In short, an exact replica of the accession methodology that has proven highly successful to consolidate democracy and promote reform in central and southern Europe. But for Poland or for Portugal, the certainty of eventually joining the club made painful reforms seem like a small sacrifice needed to earn a much sought-after prize. Without such a reward, will the sacrifice, however beneficial in itself, seem quite as manageable and worthwhile? Can Europe, in Kataryna Wolczuk's words, 'imbue the neighbours with the determination needed for a renewed and sustained reform effort?'*

The present volume does not provide a definitive answer to this question. There is no doubt that the European Union's 'democratic effect' was crucial for the democratic revolution in Ukraine and continued to be felt in its aftermath. There can be no doubt, also, of the Union's genuine desire to lend its unflinching support to the far-reaching reforms undertaken by the Ukrainians. It is doubtful, however, that 'constructive ambiguity' regarding the ultimate goal will work forever.

Awareness of the many difficulties ahead also exists, and this study shows, inter alia*, that the party system is still fragile and the rule of law which must provide the basis for a strong Ukrainian state, as Pawel Wolowski points out, has yet to take firm root. But it illustrates perhaps a broader point: the need for a EU policy more clearly designed to support democratic transition. Like elsewhere in eastern Europe (and somewhat differently from what happens in southern Europe), this is a case where a cautious approach dictated by considerations of stability does not take precedence over a genuine desire on the part of the EU to see reforms succeed and a strong democracy soundly based on the rule of law take hold.*

All contributors seem to agree that concern not to antagonise Russia does not diminish the ambition for a strong democracy in Ukraine that the EU shares with the victors of the Orange Revolution. The 'Russia factor' could however, as is argued in the concluding chapter, hamper its ability to act owing to the many difficulties standing in the way of a common EU strategy to deal with such issues as energy and frozen conflicts, which are of paramount importance to Ukraine and its neighbours.

Europe must devise a strategy of active involvement in the resolution of conflicts which continue to poison relations with its neighbours, and crucially so with Russia. It is vitally important in this regard to come up with a well-thought out common stance towards NATO's eastern expansion. If in the case of central Europe a Euro-Atlantic framework made a lot of sense, NATO being regarded as a step ahead of EU membership, there is no denying that Russia perceives the NATO membership of non-EU members or even hopefuls in the common neighbourhood as a naked threat. There is little point in arguing the glaringly obvious, i.e. that this is a non-existent threat for the Atlantic Alliance has long ceased to be antagonistic to Russia. The fact that it is still perceived as threatening by Russia must be acknowledged. In contrast, the Union's involvement in settling disputes and conflict in the common neighbourhood can more easily be integrated into a general framework of cooperation between the EU and Russia.

Sabine Fisher is right to the point in concluding that Ukraine's future largely depends on its ability to develop a balanced, sound cooperation with all its neighbours. This was actually one of the main concerns and political priorities in the aftermath of the 2004 democratic revolution. The Union is faced with the no lesser challenge of proving it is able to coherently combine support to economic integration and the rule of law with active involvement in resolving conflict. The days of the Orange Revolution are not so far behind, when the EU displayed a remarkable capacity for timely and effective action, based on the combined strength of the Member States and those capitals with special ties to the Ukraine. Such a scenario is likely to happen every time the EU is consistently and fully united behind its values and its best interests.

Paris, February 2008

Executive Summary

Sabine Fischer

Where is Ukraine going? The renewal of a coalition between the Orange forces in December after the early parliamentary elections on 30 September 2007 seems to be a good occasion to take a step back and reflect on this question again. After a long period characterised by ambivalent multi-vector policies vacillating between Russia and the Western community of states under President Kuchma, a democratic upheaval swept away his corrupt regime, and Ukraine embarked on a course towards Euro-Atlantic integration after the Orange Revolution in 2004. However, the post-revolutionary transformation did not go smoothly. The new political leadership quickly became bogged down in domestic infighting, with the Orange camp split between different ambitious personalities and figures from the ruling elites of the Kuchma era insinuating their way back into power. Domestic blockades and power struggles left the country practically without leadership between March and August 2006 and again between April and September 2007.

Ukraine is a European state 'sandwiched' between Russia and the EU. It is one of the largest and most populous states in Europe, rich in natural resources and fertile agricultural regions. Itself a country divided along ethno-political lines, Ukraine is located in the centre of a European sub-region which has been characterised by great instability and ambiguous domestic developments since the breakdown of the Soviet Union. As will become clear throughout this *Chaillot Paper*, Ukraine itself has great potential to both stabilise and destabilise the region. Therefore, the question about where Ukraine is going is of crucial importance for European security in general.

This *Chaillot Paper* deals with Ukraine's domestic developments and foreign policy since the Orange Revolution. In Chapters One and Two, Pawel Wolowski's and Rosaria Puglisi's investigations into the causes of recent domestic crises and the role of single groups of actors (specifically, the Ukrainian oligarchs) provide the background for understanding the domestic intricacies of a coun-

try as complex and unpredictable as Ukraine. Both Ukraine and the EU declared swift *rapprochement* and far-reaching Europeanisation of Ukraine to be their common goal when the European Neighbourhood Action Plan was signed and amended after the Orange Revolution. Three years on, Kataryna Wolczuk in Chapter Three takes stock of the problems and opportunities on both sides. Relations with Russia and its CIS neighbours remain a crucial dimension of Ukraine's often ambivalent foreign policy. In the final chapter Sabine Fischer discusses the extent to which Ukraine has become, or has the potential to become, a regional stabiliser.

The chapters

Pawel Wolowski: Ukraine after the Orange Revolution – how far from democratic consolidation?

Pawel Wolowski's chapter provides an in-depth analysis of the domestic crises and upheavals which transformed the political landscape in Ukraine twice after the Orange Revolution and led to the early parliamentary elections in September 2007. In his view there are three main causes for the domestic instability. All three causes can be described as symptoms of state weakness, a diagnosis which Pawel Wolowski ascribes to the 'pre-revolutionary' as well as 'post-revolutionary' political system in Ukraine.

Dysfunctionalities in the constitutional and legal system of the country provide a self-seeking and divided political elite with loopholes and windows of opportunity to pursue their own interests at the expense of functioning statehood. The constitutional reform, which was drawn up after the Orange Revolution and entered into force in January 2006, changed Ukraine's polity from a presidential-parliamentarian into a parliamentarian-presidential system. The President's powers were reduced to the advantage of the Government/Prime Minister and Parliament. However, the altered constitution did not provide a clear distribution of powers and competencies. In his analysis, Pawel Wolowski demonstrates how political actors in all camps exploited these loopholes in their struggle for power. The lack of clear constitutional regulations was further aggravated by the feebleness and lack of independence of the judicial system, particularly the Constitutional Court, which also became a pawn in domestic infighting.

The second factor preventing the Ukrainian state from func-

tioning properly is the weakness and instability of the party system. Pawel Wolowski sees the party system as being shaped essentially by legacies of the Soviet era as well as path-dependencies stemming from post-Soviet transformation in the 1990s. He particularly emphasises the fact that the same people continued to occupy key positions in the political establishment, since the founders of the Ukrainian parties in the 1990s had belonged to the middle and lower ranks of the Ukrainian party *nomenklatura*. Although Wolowski ascribes to the Orange Revolution the role of a window of opportunity for the emergence of a more effective and more pluralistic party system in Ukraine, his overall assessment remains bleak. Ukrainian parties are still characterised by a lack of transparency as well as by a lack of internal democratic procedures and external accountability; their leaders display a lack of loyalty both internally (within parties/factions) and externally (towards voters), and parties still have close connections with Ukrainian business elites, making them tools for the implementation of individual interests rather than representations of their voters.

The third main factor adding to the weakness of the Ukrainian state is the precarious interrelationship between politics and business elites. After the insider privatisation in the 1990s, Ukraine, like many other post-Soviet countries, was turned into an oligarchic system, in which politics, business and crime merged in an opaque rent-seeking network. Pawel Wolowski provides convincing proof that despite some token measures during the early stages of its term, the Orange leadership did not manage to efficiently smash this network, thus allowing for the continued exploitation of state structures by business actors.

Despite his overall critical view of the situation, Pawel Wolowski points out developments which allow for cautious optimism regarding the future of Ukraine's political system. The political elite as well as society in general have time and again displayed their preference for non-violent solutions to political tensions. Furthermore, the elite, although deeply divided, managed to compromise on early elections. While the weakness of the party system is all too obvious, Ukraine remains the only post-Soviet republic (apart from the Baltics) in which political pluralism could take firm root. Last but not least, Wolowski observes some changes in the mindsets of parts of the Ukrainian oligarchy, which might in a not too distant future lead to a broader and more powerful platform for political reform.

Rosaria Puglisi: Ukrainian oligarchs – a source of change?

Rosaria Puglisi's chapter on the Ukrainian oligarchs takes this observation as a starting point and investigates changes in the Ukrainian oligarchs' attitudes towards the political system and foreign policy after the Orange Revolution. These economic and business elites, who made immense fortunes during the phase of intensive capital accumulation in the 1990s, later transformed economic power into political influence over the Kuchma regime. By the end of the 1990s, business and political elites had merged into a mutually dependent rent-seeker/rent-giver relationship, which prevented state income from being reinvested and redistributed and posed a major impediment to economic development in Ukraine. Not surprisingly, business elites sided with the Kuchma regime during the Orange Revolution. The core purpose of the chapter is to explore the significance of these actors and their political involvement for Ukraine's choice between different models of development and, closely linked to this, its foreign policy orientation.

Why would Ukrainian oligarchs, who benefited so extensively from the rent-seeking possibilities of the political regime under Kuchma, change their attitude towards the domestic transformation and foreign policy orientation of the country? Puglisi presents three main reasons.

First, after the Orange Revolution, Ukrainian oligarchs were – at least temporarily – confronted with changed political conditions. The broad public support for the new President led to the old, corrupt and clientelistic political structures, in which the oligarchs were the main profiteers, being totally discredited. During the period when Yulia Tymoshenko was Prime Minister, the new government's rhetoric against the economic elites remained harsh. Thus, at least for the 18 months after the Orange Revolution, Ukrainian oligarchs found themselves under considerable political pressure. In reaction to this they decided to create a new image for themselves. Trying to do away with the negative connotations connected to the term 'oligarch', they started to portray themselves as public welfare-oriented, independent entrepreneurs, interested in economic productivity and sustainability. Some of them, like Viktor Pinchuk, openly advertised EU membership as *the* option for Ukraine's future.

Secondly, Ukraine's economy had already left behind the phase of 'wild capital accumulation' some years before the Orange Revo-

lution. After having accumulated their immense wealth, oligarchs started to change their political allegiances accordingly, and became more interested in the strengthening of ownership rights – especially in a context as fluid and unstable as Ukraine. Consequently, at least parts of the EU's norms and standards became more appealing to Ukraine's business elites because they saw in them a possibility to protect the wealth they had acquired throughout the 1990s.

Thirdly, and also already before the Orange Revolution, parts of the economic elites developed an interest in intensified exchange and integration with the global economy. After the process of capital distribution had been completed, increased productivity and access to foreign markets were perceived as the main leverage to increase welfare – Ukraine's integration into the global economy thus becoming a central goal. The EU is attractive from this perspective both as a market and as a source of know-how and technology for the modernisation of the backward Ukrainian economy.

For the first time after Ukraine's independence, therefore, the interests of at least parts of the country's business elites seem to coincide with the sustainable development of the state and society. Business actors have suddenly displayed the potential to become driving forces in Ukraine's economic development and modernisation, and in the long run in the process of political change.

As Pawel Wolowski shows in more detail, the Orange Revolution changed the institutional environment in which economic actors operated. Puglisi and Wolowski both point out that the harsh rhetoric of the early Orange leadership did not translate into drastic political measures. President Yushchenko tried to co-opt the economic elite, but did not threaten their position and property. However, the constitutional reform in early 2005 meant that economic actors now had much more scope for access to political institutions. The President became just one among several competing centres of power, thus losing his/her position at the top of the political hierarchy. The strengthened Rada gained in attractiveness for economic actors who were looking for points of entry into the political process. The result of this was the 'monetisation' of the Rada in the wake of the March 2006 parliamentary elections, when a large number of parliamentary seats were taken – and often indeed bought – by business actors.

In the current situation the further development of the oligarchs' role in Ukraine's transformation has reached a critical juncture. As before, economic actors are acquiring political positions in undemocratic ways, which works against democratic rules and transparency. Their 'European commitment' and 'democratic vocation' remain questionable. Furthermore, Ukraine's business elites lack cohesiveness. Actors showing an interest in the adoption of international rules and standards and in Ukraine's integration into the world economy form only one – albeit a growing – part of the elite. It remains to be seen whether the business elite will become a driver of reform in Ukraine. In the context of a weak and divided executive lacking strong political will for reforms, and only lukewarm commitments on the side of the EU, however, it would be a mistake to ignore this possibility.

Kataryna Wolczuk: Ukraine and the EU – is the glass half-full or half-empty?

Kataryna Wolczuk highlights both positive and negative tendencies in Ukraine-EU relations since the Orange Revolution. First of all, she discovers significant qualitative changes in Ukrainian attitudes towards the EU and in the bilateral relationship between the two sides.

The coming to power of a pro-EU and reform-oriented elite after the Orange Revolution has had a profound impact on Ukrainian discourses about the EU. The new leadership and its supporters displayed a much clearer comprehension of the substance of Europeanisation and the policy pursued by the EU in the framework of the Partnership and Cooperation Agreement (PCA) as well as the European Neighbourhood Policy (ENP). The Ukrainian discourse on the EU thus shifted from history, geopolitics and security to European norms, standards and values, and from the foreign policy to the domestic politics sphere.

The Action Plan (AP) adopted by the EU and Ukraine in the framework of the ENP for the first time provided the Ukrainian leadership with a more or less clear reform agenda. Wolczuk sees this as an important supportive factor giving impetus to the discoursive shift she observes within the political elite. According to her reading, the AP also had an empowering effect on reform-oriented parts of the state bureaucracies. These 'bureaucratic enclaves' became the driving forces in the implementation process of the ENP AP.

However, the fact that it is mainly lower-ranking bureaucrats who pursue the reforms induced by the ENP AP also highlights the many weaknesses of this policy. Two preconditions crucial for a consistent implementation of the EU-defined reform agenda are lacking in Ukraine. The political class does not display clear political determination to conduct coherent domestic reforms according to the Action Plan. A direct consequence of the political leadership's weakness is an almost total lack of institutional reform, which would pave the way for the creation of an effective coordination mechanism for AP implementation. Lacking clear support from the political class, which would have to enact political reforms and sell them to the public, the reform measures pursued by isolated sections of the state bureaucracy cannot but remain fragmented and limited in their results.

This downward spiral is further accelerated by weaknesses in the EU's approach towards Ukraine. Among various aspects discussed in Wolczuk's chapter, three seem to be of special importance:

There is no clear and unambiguous recognition of Ukraine's 'Europeanness' on the side of the EU. For the Ukrainian political elite, the domestic and foreign policy orientation towards the EU is essentially a matter of the nation's identity, making the issue and its treatment by the EU extremely sensitive in political terms. The EU, for its part, tries to answer Ukraine's political demands with bureaucratic and technical responses. However, Wolczuk emphasises that if the EU wants to be instrumental in mobilising support for reform-oriented forces in Ukraine, the process of *rapprochement* has to become 'political' on both sides.

Secondly, the rewards Ukraine may expect for adopting large parts of the *acquis communautaire* remain unclear, while what is on offer from the EU side falls short of Ukrainian expectations. Wolczuk criticises the EU for applying an inflexible 'blanket approach', presuming a broad adoption of the *acquis* without taking into consideration the needs, costs and benefits of the partner countries. Together with Brussels' lukewarm attitude towards Ukraine's European aspirations, this has inflicted serious damage on the EU's credibility in Ukraine and on the domestic position of the elites supporting *rapprochement* with the EU.

Last but not least, Wolczuk points to the 'Russia factor', which cannot be neglected when analysing Ukraine-EU relations even after the Orange Revolution. The fact that relations with Ukraine

are still seen through the 'Russia prism' in many EU capitals causes considerable frustration in Kyiv.

Analysing the prospects for Ukraine-EU relations and the Europeanisation of Ukraine proper, Wolczuk puts much emphasis on the elaboration of the Enhanced Agreement, which is due to replace the Partnership and Cooperation Agreement (PCA) after it expires in 2008. In the negotiations on this agreement, actors on both sides face the challenge of finding an appropriate balance between their expectations and their limited capacities. For the moment, however, they seem to be trapped in a vicious circle without having an exit strategy.

Sabine Fischer: Ukraine as a regional actor – too weak to escape Russia?

The chapter on Ukraine as a regional actor focuses on the regional foreign policy initiatives pioneered by the Orange leadership under President Yushchenko to underscore Ukraine's position as a regional leader with a strong European commitment. The chapter addresses the reasons why these initiatives did not bring about tangible results and were eventually marginalised after the coming to power of the Anti-Crisis Coalition in August 2006.

Ukraine's attempt to resurrect GUAM (including Georgia, Ukraine, Azerbaijan and Moldova) led to intensified activities in the framework of the organisation in 2005 and 2006. The loose grouping of states interested in economic cooperation was upgraded to a fully-fledged international organisation, renamed the Organisation for Democracy and Development, although retaining the acronym 'GUAM'. A General Secretariat was established in Kyiv, and member states started to debate more concrete measures in the security realm. President Yushchenko also made GUAM the platform for the launch of his initiative to resolve the Transnistrian conflict in 2005.

The Yushchenko Plan for Transnistria infused the negotiations about the settlement of the Transnistrian conflict, which had been stalled since the failure of the Kozak memorandum in 2003, with a new dynamic. The Ukrainian government, with the support of Georgia and Moldova, succeeded in drawing the EU deeper into the negotiation process. Brussels was granted observer status in the five-sided negotiation format and deployed an observer mission (EUBAM) to monitor the Transnistrian strip of the Ukrain-

ian-Moldovan border. The conclusion of a new border agreement with Moldova diminished the possibilities for contraband trade across the Ukrainian-Moldovan border and thus altered the economic and political situation of the regime in Tiraspol.

However, these and other regional initiatives inaugurated after the Orange Revolution only had a limited impact on overall regional developments. Ultimately, Ukraine failed to consolidate its self-proclaimed position as a regional leader and remained stuck in a precarious position in between Russia and the EU. Relations with Russia hit rock bottom after the Orange Revolution. Although the new political authorities repeatedly confirmed their desire for good relations with their eastern neighbour, Kyiv did not have a clear strategy for its policy towards Russia. Moscow, for its part, retreated to a more assertive policy after the 'trauma' of the Orange Revolution, using economic and political leverage to put the Ukrainian government under pressure. The Russian-Ukrainian gas crisis in 2005/2006 and the disputes over the future of the Black Sea Fleet demonstrated the way in which Russian-Ukrainian relations function in the aftermath of the Orange Revolution. Transnational elite networks benefiting from (in this case) energy rents, and the lack of cohesiveness of the Ukrainian political elite, still present opportunities for Russian actors to strongly influence domestic developments in Ukraine to their advantage.

The analysis presented in this chapter shows that the causes of the failure of the Orange Coalition's regional policy are to be found at different levels. Although economic *rapprochement* with the EU is seen as an important goal by all political camps, a clear consensus on the foreign policy orientation of the country still has to emerge. This is partly due to the fact that political actors tend to exploit foreign policy issues as an asset in domestic power struggles, thus downplaying rather than emphasising commonalities. When it comes to regional policy, there is in fact disagreement between the Orange forces and the Party of Regions, since the latter is not prepared to confront Russia on what it perceives as its zone of influence. With the advent to power of the Anti-Crisis Coalition it was clear, therefore, that Yushchenko's regional approach would lose momentum. Furthermore, the Orange leadership itself failed to connect its plea for good relations with Russia with its regional initiatives, thus undermining both dimensions of its foreign policy.

The (self-generated) paralysis of Ukraine's regional initiatives was fostered by the general weakness of inter-state cooperation in the post-Soviet space. In a region where political thinking is inspired by statist and neo-realist perceptions of international relations, the readiness to enter deeper cooperation arrangements with neighbouring states remains very limited. Russia's obstructive attitude towards Ukraine's and its partners' attempts to create new cooperation structures added to this weakness, as did the almost complete lack of political support from Western international organisations, namely the EU and NATO.

Lessons learned and recommendations

Throughout 2007 a certain fatigue came to characterise statements on EU-Ukrainian relations both in Brussels and Kyiv. EU officials voice frustration over political instability and the absence of a clear strategy in Ukraine. Ukrainian actors complain about the EU's reluctance to provide a clear political perspective. Both sides should be aware that they are trapped in a vicious circle: the combination of domestic chaos, caused by the self-interested behaviour of leading political figures, on the one hand, and constant criticism of the EU and its ENP, on the other, do not encourage the EU to 'reward' Ukraine with a stronger commitment and to transform relations with Kyiv from a technical into a political project – however justified Ukrainian criticism may be. At the same time, the low level of political commitment from the EU has weakened reform-oriented politicians in Ukraine. The lack of outside support and the absence of a tangible political goal, which could also be 'sold' to the population, deprived the ruling elites after the Orange Revolution of a strong incentive to unite and pursue a cohesive reform strategy. Unlike political elites in the Central Eastern European candidate countries, Ukrainian leaders cannot base their reform policies on the firm prospect of membership. Consequently it is much more difficult either to convince or sideline veto-players in the state bureaucracy and to efficiently and quickly involve political and business elites and other sectors of society in the reform processes. It remains to be seen whether after the emergence of a new government in Kyiv the EU and Ukraine will be able to break out of this vicious circle.

The reasons for the mutual estrangement between the EU and Ukraine are to be found on both sides. The EU has experienced internal crisis over policies towards the Eastern neighbourhood since its enlargement. Decision-making processes among the 27 members are much more complicated now than before 2004. Positions on almost every issue have grown very diverse, as could be seen during the debate on the constitutional treaty. Regarding policies towards the Eastern neighbourhood – and by extension towards Ukraine – this process of diversification has probably gone farther than in any other policy area. Some of the new Member States display views on Eastern Europe which differ radically from the perspectives prevailing in the European debate before 2004. For them, the whole region is shaped by an immediate security threat emanating from the Russian Federation, which in turn has a strong impact on their approach towards the region. Therefore, especially Poland and the Baltic states advocate strong support for the Euro-Atlantic integration of the Western Newly Independent States (NIS), and a much tougher stance towards Russia. Their position differs significantly from that of some of the old Member States, who put more emphasis on Russia's economic importance and prefer a pragmatic relationship, without stronger engagement of the EU in the region. As long as these Member States shaped the EU's policy towards the CIS region, it was dominated by a 'Russia first' approach, accepting Moscow's preponderance over its direct neighbours. With the advent of enlargement and the development of the ENP, this attitude seemed to be replaced by a more diversified policy, taking into consideration the needs and interests of all Eastern neighbours, and to a certain extent challenging Moscow's position in the region. However, this approach has not taken root firmly. Today, given an increasingly more assertive Russia facing elections, Ukraine drowning in internal crisis and the EU still paralysed by internal disputes over most of the issues concerning its Eastern neighbourhood, there is not much hope for a radical change in the EU's policy towards the region.

Despite some positive developments with regard to political pluralism and the acceptance of democratic rules of the game, political elites in Ukraine do not seem to have the capacity to seriously tackle the problem of state weakness, which brings with it the prospect of recurrent and self-replicating domestic crisis. Some foreign policy issues, like NATO accession, are highly con-

troversial, and are being exploited in domestic infighting. Others, like the project of regional leadership, have slipped down the political agenda. The only issue which does not face strong opposition is the desirability of closer relations with the EU – which is reflected *inter alia* in the well-coordinated continuation of negotiations on the Enhanced Agreement (due to replace the Partnership and Cooperation Agreement after it expires in 2008) despite political turmoil between April and September 2007. However, in the absence of an elite consensus on strengthening the state and its capacity to act, it remains to be seen whether Ukraine's record on the implementation of the reform agenda can improve under the new government.

In this situation, EU policy has limited room for manoeuvre to change the overall climate of both domestic politics in Ukraine and EU-Ukraine relations. However, there are a number of toeholds for a more proactive EU policy, which should be taken into account.

Pawel Wolowski emphasises the central importance of a change in the Ukrainian elite's mindset, so that clear rules of the game can be introduced that could become the guiding line of Ukrainian domestic politics. Such a shift presupposes learning processes, which inevitably do not evolve within a short period of time. They certainly cannot be imposed from the outside. However, as Kataryna Wolzcuk demonstrates, Ukrainian elites have already covered an impressive distance on their way towards a better understanding of the substance of *Evrointegracija* – as well as its weaknesses. Regarding domestic politics in Ukraine and bilateral EU-Ukraine relations, the EU should follow an approach characterised by three aspects. The EU should therefore:

1. **Be concerned about implementation and take Ukrainian concerns seriously**. The new agreement, which is being negotiated now, plays a key role for the future of EU-Ukrainian relations. Considering the low level of commitment to reform among the political elite, it has to envisage efficient instruments to monitor and – if necessary – to put pressure on Ukraine in the event that Ukraine does not comply with the standards agreed with the EU. At the same time, valid concerns on the Ukrainian side – and, as Kataryna Wolczuk shows, there are quite a lot of them – have to be taken seriously. This is currently the only way to break out of the vicious circle described above, since the EU will not be able to provide Ukraine

with a clear membership perspective any time soon. On the other hand, Ukrainian elites should moderate their extremely negative attitude towards the 'Enhanced Agreement' and capitalise on the fact that the EU has committed itself to a comprehensive treaty which encompasses – and thus makes negotiable – all aspects of Ukrainian-EU relations.

2. **Increase knowledge/encourage learning/foster dialogue**. Knowledge about the EU has already increased significantly in Ukraine over the last couple of years. However, in order to expand the 'bureaucratic islands' supporting reform policies, the EU should be still more active in promoting knowledge not only about itself, but also about the advantages of democratic rule, good governance, political and societal pluralism and the like. While there has been a 'European College' established in Moscow as a training centre for political, societal and economic actors dealing (albeit not exclusively) with the EU, no such initiative has been taken so far in relations with Ukraine. A 'European College' in Kyiv could help to increase knowledge, and make emergent elites familiar with the characteristics and functioning of the EU, as well as with the benefits close cooperation with it can bring. Ukrainian think tanks and other civil society actors have done very valuable work in engaging elite groups and actors from different political camps and regions in a political dialogue about a wide variety of facets of domestic and foreign policy. The EU should provide financial and substantive support to such activities in order to help bridge the gaps that divide the country and its elites, and raise awareness of the necessity of constructive political behaviour oriented towards common welfare.

3. **Stimulate interest in closer cooperation**. Rosaria Puglisi gives a cautious assessment of the 'democracy potential' of the changes she observes among Ukraine's business elites. Political changes resulting from these shifts could at best be labelled 'democratisation by default.' However, all authors represented in this *Chaillot Paper* confirm that there is potential for change. The EU should therefore try to strengthen these trends by encouraging economic cooperation between EU and Ukrainian companies, as well as foreign investment. Growing awareness that cooperation with the EU brings benefits would most likely increase Ukrainian economic actors' preparedness to adapt to European/international rules and

norms. In the longer run, this could have a stabilising effect on Ukrainian society as a whole, while the strengthening of transparency and good governance might lead to a more equitable redistribution of wealth and resources and an improvement in general living standards. However, this is not possible without a contribution from the Ukrainian side. The new government should make a concerted effort to create the optimum legal and economic conditions for attracting foreign capital and actors interested in mutually beneficial cooperation. This argument obviously links back to the negotiations on the Enhanced Agreement, and the Ukrainian leadership's commitment to reform. Ukraine's admission to the WTO, approved in late January 2008, which paves the way for a free trade agreement between the EU and Ukraine, is an important and positive step in the same direction.

Things seem to be more complicated regarding the regional triangle between the EU, Ukraine, and Russia. Here, the most important precondition for the development of a coherent EU approach would be to overcome the internal divide separating EU Member States on the issue of the Eastern neighbourhood and relations with Russia. The conflicting desires to support reforms and *rapprochement* with Ukraine, and at the same time to avoid a complete deterioration of relations with Russia, have resulted in a situation where the EU has to perform a difficult balancing act, which so far it has had difficulty managing. Instead of following a clear political line, Brussels shies away from (re)acting on many controversial, but important, issues. There is little prospect that EU Member States will quickly overcome their disagreements on an appropriate policy towards the Eastern neighbourhood. However, if the right degree of political will and determination was assumed on all sides, the EU could act more decisively regarding a number of issues, and by doing so assist Ukraine in broadening its scope as a regional actor.

4. **Regional cooperation**. Although EU strategy papers usually proclaim regional cooperation as a tool for political stabilisation and economic growth, there has been little concrete action in this direction so far. Brussels has been reluctant to support initiatives emerging from the region itself. Russian-led integration efforts are seen as neo-imperialistic attempts to restore Moscow's control over the former empire; while non-Russian initiatives like GUAM were not supported because of fears that relations with Russia could be

damaged. This ostrich-like policy does not lead very far in a fragmented and polarised region, where actors see the EU either as a competitor or a saviour. The Black Sea Synergy, launched during the German presidency in June 2007, is a useful step to support regional cooperation in parts of the CIS. However, it should be complemented by an open and critical dialogue about other regional initiatives, and the search for possible synergies. This would be a signal that such initiatives are taken seriously in Brussels, and thus provide regional actors with an argument in favour of their continuation. It could also strengthen the advocates of a stronger regional engagement in the domestic context and make it easier for them to 'sell' regional cooperation to their electorate.

5. **Protracted conflicts/peacekeeping**. The protracted conflicts pose a permanent security risk and add to the fragmentation of the region. They hamper the political and economic development of the countries directly affected by separatism, but also that of neighbouring states. The EU should become more proactive in this area. In the case of Ukraine this would have meant a more visible – albeit critical – support for the Yushchenko Plan on Transnistria, and a more decisive engagement, possibly even an open debate, about the scope for the deployment of a truly international peacekeeping force in Transnistria with EU participation. The successful performance of EUBAM has demonstrated that such engagement is possible despite Moscow's initially dismissive attitude. While Russian consent to NATO peacekeepers remains very unlikely, Moscow has repeatedly displayed interest in closer cooperation with ESDP. Therefore, a more decisive EU policy could have positive effects both for the conflict-resolution processes and EU-Russia relations.

6. **Energy dialogue/multilateral transit consortia**. The EU follows a 'Russia first' approach also in its energy policy. While it conducts an institutionalised 'energy dialogue' with Russia, there is no such arrangement with Ukraine. As could be seen during the gas crisis at the beginning of 2006, this puts Ukraine in a precarious situation, in which informal rent-seeking networks can undermine transparent regulations for energy relations between Russia, Ukraine and ultimately also the EU. Therefore, the EU should open up an energy dialogue with Ukraine as well. This would certainly not alter the country's energy dependence on Russia in the short run, but it could infuse Ukrainian discourses with new ideas about

the restructuring of the energy sector, energy efficiency and the like. Furthermore, EU Member States should consider the creation of trilateral or even multilateral transit consortia, involving Western European, Ukrainian, and possibly also Russian companies. Joint ventures of this kind could strengthen international rules and norms in Ukraine's energy sector, make it more efficient through Foreign Direct Investment (FDI) and the transfer of knowledge and technologies, and protect the country from the deleterious consequences of energy dependence.

Ukrainian politics after the Orange Revolution – How far from democratic consolidation?

1

Pawel Wolowski

Introduction

The Orange Revolution in autumn 2004 brought Ukraine to the forefront of international attention. In early 2005, the new 'Orange' government promised radical reforms to make Ukraine an entirely democratic state with a market economy, invoking democratic values including the rule of law and development of a civil society. The promises included establishing the rule of law in the country, eliminating corruption, reform of the judicial system and creating transparent business rules. Although the cabinets headed by Tymoshenko and Yekhanurov took some measures related to those issues, the promise of a general reconstruction of the state was not fulfilled before the parliamentary elections in March 2006.

As a result of the elections a coalition led by the Party of Regions was eventually put together and the new government was formed in August 2006; Viktor Yanukovych, who had been Viktor Yushchenko's main rival in the presidential election, became the head of government. This caused anxiety both in Ukraine and among the international community that the pro-democratic policy might be discontinued and authoritarian methods of governing the state might be restored. These fears appear to have been exaggerated. Democratic achievements such as a multi-party system, freedom of association, freedom of expression and freedom of the press had already become well-established in Ukraine and were not reversed.

However, during a year of difficult cohabitation (summer 2006-summer 2007) between the 'Orange' president and the 'white-and-blue' government, a whole series of disputes over the scope of powers under the new constitution revealed fundamental weaknesses in the functioning of the state. The bitter conflict in spring 2007, during which both sides broke the law many times and on fundamental issues, deepened the legislative chaos in the

country, undermined society's trust in the state authorities and significantly tarnished Ukraine's image in the West.

Clearly, developing an orderly legal system to enable the effective functioning of the state is currently the greatest challenge Ukraine faces.

This chapter explores the reasons why transformation processes kicked off by the Orange Revolution did not lead to democratic consolidation in Ukraine. It focuses on the fundamental factors impeding the evolution of the Ukrainian state towards a functioning democracy.

The main reason for the partial failure of the project of democratic consolidation is the weakness of the Ukrainian state, which is caused by the legacy of the Soviet past as well as path dependencies which emerged during the transformation processes in the 1990s. The three main factors which determine the way in which the political system develops – under the circumstances of state weakness – are: a faulty constitutional/legal system, a dysfunctional party system, and corrupt collusion between politics and business.

This chapter consists of three main parts. The first section provides an analytical description of the political crisis, a symptom of state weakness, which existed between the March 2006 parliamentary elections and the early parliamentary elections in September 2007 and which was continued in the fight for creating a government coalition in autumn 2007.

The second section attempts to show the underlying causes of state weakness in the three key areas, namely the legal-constitutional system, the party system and the relations between politics and business. As already mentioned, state weakness originates from both the legacy of the Soviet past and dysfunctionalities inherent to the transformation processes of the 1990s.

The last section provides a summary of the conclusions of the analysis and highlights those elements of the political processes which may contribute to overcoming the multifaceted weakness of the state in the future. The chapter ends with a forecast outlining possible scenarios for Ukraine's future development.

Domestic crisis in Ukraine

The period between the parliamentary elections in March 2006 and the early elections in September 2007 can be described as a series of

political conflicts resulting in periodic political crises. These crises in turn caused chaos in the functioning of the main institutions of the state and sometimes even posed a risk of destabilisation of the entire country.

Coalition games: March-August 2006

The elections held on 26 March 2006 posed a dual challenge to Ukraine. From the perspective of building the political system of the state, this was the first election since the amendment of the constitution which had introduced the parliamentary-presidential system, limited the president's powers and transferred some of the previous presidential prerogatives onto the parliament and government. From the point of view of shaping the political landscape after the Orange Revolution, the essential question was whether the so-called 'Orange forces', among whom deep divisions had already been revealed at the beginning of Viktor Yushchenko's presidency, would be able to continue governing the country.

There was no indisputable winner in the March election. Although the Bloc of Yulia Tymoshenko (BYuT), and Our Ukraine achieved a better result overall than the Party of Regions, to create a government coalition they would have had to enter into an alliance with the Socialist Party of Ukraine. The victorious Party of Regions could choose between creating a 'blue' coalition with communists and socialists or a 'rainbow' coalition with Our Ukraine.

The tactics adopted by Our Ukraine, the third biggest force in the parliament, were a key element of the complex game aimed at forging the coalition. Ultimately, the shape of the coalition depended on that party. The business circles led by Petro Poroshenko, which had a strong position in Our Ukraine at the time, wanted a coalition with the Party of Regions because they believed that this would guarantee the government's pro-big business policy. The rest, who mainly originated from right-wing parties representing the nationalist approach, saw such a possible alliance as a 'betrayal of the Maidan'[1] and supported the project of the 'Orange' coalition. The president did not want his influence to become marginalised as a consequence of an alliance with the popular leader of BYuT, who did not conceal her presidential ambitions, but at the same time he was aware of the risk of losing popu-

1. Maidan Nezalezhnosti [Independence Square] – a place in the centre of Kyiv where the Orange Revolution started. The term 'Maidan' is often used symbolically in Ukraine to denote the Orange Revolution.

larity in the event that his party entered into a coalition with the Party of Regions. Therefore, he persuaded the leaders of Our Ukraine to embark upon parallel negotiations with BYuT and the Socialist Party of Ukraine on the one hand and with the Party of Regions on the other.

Two coalition agreements were developed as a consequence of the negotiations in late June. Both draft agreements were presented to the president almost at the same time. Yushchenko's choice of the Orange Coalition was perceived by Yanukovych as a breach of their previous arrangements. The leader of the Party of Regions then embarked on radical actions to prevent the creation of that coalition. The most serious consequence of his actions was that Oleksandr Moroz, the leader of the Socialist Party of Ukraine, came over to the side of the Party of Regions and thus enabled the creation of the 'blue' coalition. Desperate attempts by BYuT to prevent the formation of the coalition with street demonstrations, and pressing the president not to present Yanukovych as a candidate for prime minister, appeared ineffective.

Our Ukraine was still engaged in talks on the possibility of joining the coalition with the Party of Regions between July and September 2006. Our Ukraine's weak bargaining position was the main reason for the failure of the talks.

The coalition games revealed some negative phenomena. Firstly, the violation of agreements by the key players had become standard practice in Ukrainian political life, which resulted in common mutual mistrust. Secondly, legal loopholes and defects in the constitution, which could cause disruption in the political process, were discovered.

The conflict between the president and the prime minister

It appeared quite soon that the cohabitation of the 'Orange' president and the 'blue' prime minister had set the stage for an open conflict.

The dispute between President Viktor Yushchenko and Prime Minister Viktor Yanukovych over the scope of their respective powers began in autumn 2006 and reached its peak in a bitter conflict in April and May 2007. It posed the threat of destabilising the political situation in the country and ended in an agreement to hold early elections in September 2007. The dispute can be regarded as a sort of a case study, which exposed the weaknesses of the state.

The dispute extended over many issues and in fact concerned the entire scope of executive power in the country. Between September and December 2006, the so-called Anti-Crisis Coalition, which consisted of the Party of Regions, the Socialist Party and the Communist Party, prepared bills that determined the scope of powers in more detail to the advantage of the prime minister in those areas which the constitution did not regulate in a precise way. Although two competing pieces of legislation concerning the Cabinet of Ministers, one aimed at widening the prerogatives of the prime minister and his government and the other at extending the powers of the president, had been drafted, respectively, by the government and the president, the parliament only accepted for consideration the one proposed by the government. The bill was passed by the parliament, vetoed by the president, and finally it was adopted on 12 January 2007, after the presidential veto was overridden by the coalition's opportunistic alliance with Yulia Tymoshenko's Bloc.

The law filled in the legislative gaps in the constitution (e.g. it provides that if the president fails to present to the parliament a prime ministerial candidate proposed by the parliamentary coalition, the parliament shall nominate the prime minister without the president's approval). The act also removed numerous legal loopholes which had enabled the president to extend his powers beyond the limits prescribed by the constitution (e.g. the requirement to consult the president on the candidates for many executive positions in the Interior Ministry, Foreign Ministry and Defence Ministry). Since the powers of the government and individual ministers were determined under the constitution of Ukraine in much more general terms than were the powers of the president, the new legislation extending the prerogatives of the Cabinet of Ministers redressed the balance to a certain extent; however, not all of the changes increased the powers of the government.[2]

Although the president refused to sign the law, it formally came into force on 2 February 2007 and was signed by the Speaker of the Parliament. The government and coalition camp were emboldened by this victory in the battle for competences against the president. After having extended the interpretation of the legal regulations to make them more favourable for the government and parliament, they took further actions, the constitutionality of which raised serious doubts.

2. The law, among other provisions, reduced the dependence of local administration on the president and introduced the possibility of refusing to countersign presidential decrees. It also granted the prime minister the right to propose candidates for ministers in the so-called presidential ministries in case of delays in the president presenting his own candidates, which could be regarded as usurpation, according to the constitutional provisions. Cf. Tadeusz Olszanski, 'Yanukovych and Tymoshenko override president's veto', *East Week* no. 467, Centre for Eastern Studies, Warsaw, 18 January 2007.

Although the constitution provides that a parliamentary coalition shall be formed by parliamentary factions and that those MPs who leave their faction for another shall automatically lose their seats, the Anti-Crisis Coalition accepted some MPs from the opposition factions into their ranks and offered them senior governmental positions.[3] This gave rise to a weird legal situation in which a group of MPs found themselves in the governing coalition and at the same time were officially members of factions which were in opposition to the government. Leaders of the coalition did not conceal the fact that the intention behind such actions was to ensure a parliamentary majority of more than 300 MPs that would enable them to amend the constitution, including reducing the powers of the president and limiting the scope of his responsibilities to representative functions, as well as changing the presidential election procedures by replacing the general election with appointment of the president by the parliament.

The dissolution of the parliament

President Yushchenko realised that the actions taken by the coalition posed a real threat to his power and on 2 April he announced a decree dissolving the parliament and scheduled early parliamentary elections for 25 May 2007. This opened a subsequent phase in the struggle for power, the most dramatic one so far, which ended in the agreement reached on 27 May to hold the early elections in September 2007.

When the president dissolved the parliament, he claimed he was enforcing his general powers as the defender of the country's sovereignty and guardian of the constitution. He argued that the entry into the coalition of MPs who were members of opposition factions was contrary to the constitution, distorted the will of the electorate, constituted an usurpation of power and posed a threat to national security. This reasoning did not have a strong legal basis; none of the three sets of circumstances determined under the constitution[4] as valid reasons for dissolving the parliament had actually occurred.

The practice of headhunting opposition MPs by the parliamentary majority is in fact unconstitutional (although it is not directly forbidden); still, the claim that it was a threat to national security was definitely an overstatement. Moreover, the president is not authorised to exclusively determine by himself when another one

3. The group of Anatoly Kinakh, being a part of the Our Ukraine faction, entered the coalition without leaving the faction in late March, and Kinakh himself was nominated Minister of Economy on 21 March 2007.

4. Pursuant to Article 90 of the constitution, these are: a failure to form a coalition within one month, a failure to form the government within 60 days of the dismissal of the previous one, and a failure by the parliament to hold plenary sessions over one month.

of the central state institutions (parliament, government or the Council for National Security and Defence) violates the constitution. This role is reserved for the Constitutional Court.

Pursuant to the constitution, a dissolved parliament is not authorised to pass any decisions. Nevertheless, the parliament deemed the decree unconstitutional (which it was not authorised to do, either) and at the same time sought the intervention of the Constitutional Court, requesting a clear assessment as to whether the decree complied with the constitution.

The 'legal' phase of the conflict

Following that first instance of confrontation between the president and the government coalition (2 April), since both sides had broken the law, they seemed to agree that the political conflict had to be resolved by legal means, i.e. through the Constitutional Court. However, it soon transpired that they preferred reaching a political agreement rather than asking the Court for an opinion. That solution was beneficial first of all to the president, especially when he realised that he had practically no chance of obtaining a favourable judgement from the Constitutional Court.

Simultaneously, an intense propaganda game began. Both sides were doing their best to present themselves to the public and to the international community as the sole defenders of constitutional order and democracy.[5] At the same time, a campaign of criticism against individual members of the Constitutional Court was launched in the media, especially the media favourably disposed to the president.[6] The Court, which already enjoyed little prestige due to both the widespread belief that it was subservient to politicians and suspicion of corruption among its members, was additionally discredited by actions taken by politicians, especially those from the president's camp.

As early as April, both sides in the conflict misused law enforcement agencies to meet their own needs. The Security Service of Ukraine, linked to the president, presented material to discredit the Constitutional Court judge Siuzana Stanik, while the general prosecutor's office, which was loyal to the government, refused to bring charges against Judge Stanik, contrary to the president's demands.

The president acted in excess of his constitutional powers again when he passed the decrees to dismiss Constitutional Court

5. For example, President Yushchenko and Prime Minister Yanukovych did so during their respective visits to Brussels and Strasbourg. Other examples included repeated appeals by the prime minister and the Speaker of the Parliament defending democracy addressed to the international community, and hour-long TV speeches by the president addressed to the people of Ukraine.

6. Cf. *Orbity Konstytutsiynoho Sudu. Zolota aktsyia Medvedchuka u viyni Yushchenka i Yanukovycha*, [The orbits of the Constitutional Court. The golden share of Medvedchuk in the war between Yushchenko and Yanukovych], *Ukrayinska Pravda*. See: http://www.pravda.com.ua/news/2007/4/6/57073.htm.

judges.[7] However, he came closer to achieving a tactical political goal, namely the elimination of the threat that the Court would pass a verdict to his disadvantage, which had been very likely, and instead created a situation where only a political agreement offered the opportunity of breaking the deadlock.

The negotiations took almost a month. The first version of the deal, which was agreed on 4 May, was not fulfilled mainly due to obstruction by the parliamentary speaker Oleksandr Moroz and the hesitant behaviour of the prime minister, who had to take into account the view of most elites and a majority of the Party of Regions' electorate, who opposed the agreement.

As both sides did not comply with the provisions of the agreement, which was being hammered out in an atmosphere of mutual accusations of law breaking, the conflict worsened again. Characteristic of this stage of the conflict was direct interference by executive authorities in the functioning of the judicial system. Between 16 and 25 May, various common courts, acting under pressure from both sides in the conflict, passed in total 12 judgements, 6 of which approved the suspension and the other 6 of which ordered the cancellation of the suspension of the Constitutional Court judges, who had been suspended under the presidential decrees. This 'ping pong game' violated many court procedures.

Demonstrations of force

As it was impossible to resolve the situation by legal means and the negotiations to achieve an agreement were completely deadlocked, the two sides resorted to the last possible instrument, direct engagement of law enforcement agencies, in order to obtain a favourable solution.

The political crisis, which had existed since 2 April, suddenly got more serious between 25 and 26 May. The president's decision to dismiss Sviatoslav Piskun from the post of Prosecutor General and make him acting prosecutor instead was not accepted by the interior minister, who used special police troops to enable the former Prosecutor General to enter his office. In response, the president decreed that the internal troops report directly to him (they normally report to the Interior Minister) and ordered the commander-in-chief of those forces to guard the government buildings and enforce law and order in the city during the Days of Kyiv festival on 26 and 27 May. In the atmosphere of intensifying dis-

7. Presidential decrees dismissing three judges of the Constitutional Court were passed on 30 April, 1 May and 10 May 2007.

pute and with both sides accusing each other of seeking to foment a violent confrontation, unarmed Internal Troops from almost every part of Ukraine headed to Kiev. On their way they were stopped in many places by traffic police troops, which reported to the Interior Minister.

The confrontation on 25 and 26 May demonstrated to both political camps the risk of a violent escalation of the crisis. It seems that this awareness encouraged all players to compromise on early parliamentary elections on 30 September – a solution they perceived as the only possible way out.

After 30 September 2007 – stabilisation or new crisis ahead?

The four months of preparations for the election (including 60 days of the official election campaign) were used by the major players to reinforce their position and to work on coalition options in the future parliament.

The main opponent of the Party of Regions, the increasingly popular Yulia Tymoshenko, managed to make the president, who is the honorary chairman of the People's Union 'Our Ukraine' party, and Yuri Lutsenko, the leader of People's Self-Defence, the strongest faction within the Our Ukraine bloc, give a solemn promise that they would create an 'Orange' coalition after the election. On the other hand, although the Party of Regions was presented as a monolith during the election campaign, the conflict of interest between Viktor Yanukovych, the main political and public 'face' of the party, and the multibillionaire Rinat Akhmetov, the party's main sponsor and the richest man in Ukraine, had been increasing. Akhmetov and his informal faction inside the Party of Regions unofficially supported the idea of creating a broad coalition with Our Ukraine to ensure stabilisation of the situation in the country and to create a good institutional and legal basis for conducting business and business development. To achieve this goal Akhmetov was ready to sacrifice the candidacy of Yanukovych for the post of prime minister. There are strong indications that President Yushchenko supported such a solution.[8] For Yanukovych, a scenario which marginalises his position is unacceptable. The possibility of his party sweeping to victory in the elections and good results achieved respectively by his minor potential coalition members offered him a chance to have a 'blue coalition II' and to retain his position as the head of the government.

8. In the opinion of some analysts in Kyiv, a secret deal to that effect, which was struck by Yushchenko and Akhmetov in May 2007, enabled the reaching of an agreement to hold early elections.

The results of the 30 September elections[9] made possible the creation of two coalitions, i.e. the 'Orange' coalition of BYuT and Our Ukraine with a majority of 228 seats, possibly reinforced by the Lytvyn Bloc, with Yulia Tymoshenko as the prime minister, or a coalition of the Party of Regions and Our Ukraine with a majority of 246 seats, probably with a 'compromise' prime minister (i.e. not Yanukovych). The creation of a 'rainbow' coalition (PR + BYuT + OU), was unlikely from the beginning due to personal enmity between the leaders and conflicting business interests between PR and BYuT. On 15 October BYuT and Our Ukraine announced that they would form a coalition and build a government under the leadership of Yulia Tymoshenko. The coalition government was eventually formed on 18 December 2007, after several weeks of very difficult negotiations between the coalition leaders and the president.

However, there are reasonable grounds for concern that this renewed Orange Coalition will not be able to have a long-term stabilising effect on the country.

The main destabilising factors will be the presidential ambitions of Yulia Tymoshenko on the one hand and the likely anti-governmental activity of the Party of Regions. Tymoshenko very clearly suggests that she sees no one else but herself as the candidate of the 'democratic' forces in the presidential election in 2009. Therefore, a conflict can only be avoided if Yushchenko gives up seeking re-election. Otherwise, conflict will be inevitable and will lead to the break-up of the coalition.

At the same time, the opposition Party of Regions will have a sufficiently strong potential to veto any legislative projects proposed by the coalition, organise an anti-governmental campaign in the eastern regions of Ukraine and, if necessary, to paralyse activities of the parliament by making the deputies who belong to the faction resign their seats.

Furthermore, the coalition government will not have the majority of 301 votes necessary to amend the constitution. Therefore, it is quite likely that the legal defects and loopholes in the constitution, which exacerbated the political crisis in spring 2007, will generate further crises of this type. Only a rainbow coalition would at least in theory be able to tidy up the constitutional system and guarantee stability in the country.

9. Results of the elections held on 30 September 2007: The Party of Regions won 34.27% of the votes and 175 seats, BYuT won 30.78% of the votes and 156 seats, Our Ukraine-People's Self-Defence won 14.20% of the votes and 72 seats; the Communist Party of Ukraine won 5.38% of the votes and 27 seats, and Lytvyn Bloc won 3.96% of the votes and 20 seats.

State weakness in Ukraine

This analysis starts from the assumption that the main cause of recurrent domestic crises in Ukraine is state weakness. In order to fully understand the phenomenon of state weakness in transition countries like Ukraine, it is helpful to distinguish between the state as a provider of solutions (e.g. the provision of public goods, solving collective social problems) and the state as a source of problems (state failure, the costs and risks associated with state action). A functional state provides its citizens with internal and external solutions, health and social security, an effective law and order system, as well as redistribution of economic resources and minimum living standards. Post-Soviet transition countries usually suffer from a very low level of functionality; the state does not provide solutions to security and other problems affecting society. State dysfunctionality occurs when state agencies are being undermined by corruption and become involved in shadow economic structures and organised crime.[10] As the following section will demonstrate, the Ukrainian state suffers from both a low degree of functionality and high dysfunctionality – even after the Orange Revolution.

The low level of functionality is evident *inter alia* in the state's inability to satisfy the basic material needs of the population, as well as in the inability of the state authorities to determine a comprehensive reform strategy. However, the latter is mainly a symptom of the poor quality of the law-making process, the Constitution being the first example.

However, the following paragraphs will focus mainly on state dysfunctionalities, which in the case of Ukraine, similarly to other Eastern European countries, become manifest in the arbitrary application of rules and various forms of corruption.[11] This concerns first of all three interrelated areas: the constitutional/legal system, the party system and the relationship between business and politics.

Ukraine's Constitution and Constitutional Court: A dysfunctional legal system

In Ukraine the low quality of the law is exploited by various actors as a means of furthering their political struggle. The weakness and defectiveness of the legal system on the one hand results from the

10. Verena Fritz, 'State weakness In Eastern Europe: concept and causes', European University Institute, Robert Shuman Centre for Advanced Studies, no. 2004/35.

11. Ibid., p. 3.

inadequate qualifications and expertise of law-makers (e.g. in the field of constitutional law), and on the other is a consequence of interference by executive authorities and lobbyists representing various groups of interests.

The question of the law being respected by bodies of executive authority is a separate issue. The lack of an imperative to obey the law and notorious violations or evasions of legal regulations by the authorities seem to originate from the experiences related to observance of the law and the practice of its application in the former USSR. In the Soviet Union, the constitution and the entire legal system were subordinate to the 'will of the working people of cities and villages' which was defined and expressed by senior officials of the Communist Party. The cavalier approach to the law manifested by the president and the government (both at central and local levels) and the belief in the superiority of political over legal solutions in contemporary Ukraine seem to be continuations of the Soviet practice.

The events which have taken place over the past 18 months in Ukraine paint a picture of a state which has found itself in a serious institutional and legislative crisis. The incoherence of the principal legal regulations, namely, the imprecision and inconsistency in the provisions of the constitution itself and discrepancies between the constitution and lower-ranking executive laws, have created legislative chaos. Representatives of the executive, who originate from different political camps, try to exploit this situation to broaden their prerogatives.

The current crisis doubtlessly originated in the so-called constitutional reform project, which was adopted in December 2004. It provided for the change from the presidential-parliamentary political system to a parliamentary-presidential one. Consequently, it significantly reduced the president's powers and broadened the powers of the government and parliament instead. The project was an element of the unofficial pact between the old team of Leonid Kuchma and the 'Orange' camp, which guaranteed a peaceful transfer of power by reholding the presidential election runoff on 26 December 2004.

The amended constitution came into force on 1 January 2006, and some of its provisions became effective after the parliamentary elections. The overly general, incoherent and sometimes contradictory provisions of the constitution, especially those concerning the division of powers between the president and the

government, fanned the flames of the dispute over the scopes of powers vested in the president and the prime minister respectively. To cite a few examples:

- the imprecise provision on the countersigning of presidential decrees by the prime minister and a relevant minister[12] which does not provide for any consequences in the case of a countersignature being refused;
- the insufficiently precise division of responsibilities between the president and prime minister respectively in setting the guidelines for and directing the implementation of foreign policy;[13]
- lack of regulations on dismissing ministers appointed by the president, including the foreign minister.

Subsequent legal defects came to light gradually, as the relations between the head of the state and the head of the government worsened. The two latter issues were at the core of the dispute in autumn 2006 and at the beginning of 2007. As early as September 2006, Oleksandr Sushko, an analyst from Kyiv, claimed that the incomplete and internally inconsistent newly-amended constitution greatly complicated the decision-making process in the domain of foreign and defence policies and that the 'competition between the camps of the president and the prime minister who aspire to have real influence on the foreign policy decision-making of Ukraine is likely to turn into a permanent conflict of interpretations of legislation, struggling to cover numerous legislation gaps and creating advantageous precedents.'[14]

The errors, loopholes, imprecisions and contradictions in the provisions of the constitution come to light virtually every time a serious political conflict occurs. The fact that deputies belonging to factions of Our Ukraine and BYuT gave up their parliamentary seats in June 2007 was used by the president as grounds for deeming the parliament unable to operate and announcing the early election on that basis. In the president's opinion, the parliament's mandate expired due to the loss of a quorum and its further legislative activity was illicit. However, the laws regulating this issue are also incoherent. Article 60 of the constitution provides that the 'powers' of the old Rada expire when the new Rada convenes. However, this provision is then followed by a qualification to the effect that the president shall have the right to 'extinguish the powers of the parliament earlier.' This lack of precision was

12. The Constitution of Ukraine, Article 106, part four.

13. Pursuant to item 3 of Article 106 of the Constitution, the president shall represent the state in international relations, manage the foreign activity of the state, conduct negotiations and enter into international treaties for and on behalf of Ukraine. Pursuant to item 1 of Article 116, the Cabinet of Ministers, including the prime minister, shall be in charge of the internal and foreign policy of the state.

14. Oleksandr Sushko, 'Ukrainian foreign policy decision-making in new political conditions', *Policy Paper* no. 4, September 2006, Centre for Peace, Conversion and Foreign Policy of Ukraine. Available at: http://www.foreignpolicy.org.ua.

exploited for some time by Oleksandr Moroz, the former Parliamentary Speaker and the head of the Socialist Party of Ukraine, who until as late as September 2007 used to convene meetings of Verkhovna Rada which were then deemed illicit by the president.

Another constitutional loophole which has already been used as a threat by the leaders of BYuT and PR after the 30 September 2007 election is the lack of a clear procedure to be followed in the event that the parliament is not convened or is unable to function. The constitution only decrees that a subsequent election cannot be held within one year of holding early elections. This may mean that if a faction which has more than 150 seats fails to take the oath of office or gives up its seats Ukraine will have no legal legislative authority.

The weak judicial system is a separate problem. Ukraine is a country whose constitution provides for the separation of powers. However, the fact that the constitution does not include a separate regulation stating independence of the judiciary and only provides for independence of individual judges seems symptomatic. In practice, the major weaknesses of the Ukrainian judicial system are yielding to pressure from political and business groups and the related corruption problem.

Obvious political pressure could be noticed this April and May during the 'ping-pong' games described above, when the presidential decrees dismissing judges of the Constitutional Court were six times repealed and then approved under verdicts passed by different common courts. It was only possible to use the mechanism because some individual judges appeared to be 'loyal' to the president and others to the government.

In turn, the Constitutional Court itself can be cited as an example of an institution which is part of the judicial system and whose activity has been paralysed by politicians. The parliament did not appoint the number of Constitutional Court judges which it had the power to appoint for more than a year. This was due to the fear shared by most deputies in the parliament, which had been elected in 2002, that President Yushchenko might complain to the Constitutional Court about the way in which the constitutional reform which had been launched in late 2004 was implemented and thus bring back the *status quo ante*. This meant that Ukraine did not have a Constitutional Court at all for one and a half years. In turn, during the crisis in spring 2007, the Constitutional Court was delaying its decision to consider the motion deeming the pres-

ident's decision to dissolve the parliament unconstitutional. Most probably, the main reason was due to the fact that the judges, most of whom were clearly associated with certain political camps, were afraid of taking the risk of passing an independent judgement. Then, as the president became increasingly afraid that the Court's verdict could be disadvantageous to him, he took actions which in effect discredited the Constitutional Court[15] and deprived it of its legal function of deciding on the constitutionality of lower-ranking legislative acts.

A perfect example of judges yielding to pressure exerted by business groups is the so-called 'reiderstvo' (raiding). This term is used in Ukraine to describe the enforced takeover of an enterprise on the basis of forged ownership titles. The key roles in such criminal dealings, which have been described on many occasions in the Ukrainian press,[16] have been played by corrupt judges, who awarded the titles of ownership to the new owners. On such 'formal legal' grounds, enterprises were then taken over, often with the use of brutal force, by security agencies.

The Ukrainian party system – no stronghold against state weakness

In contrast to other former Soviet republics, political pluralism and competition between political parties really do exist in Ukraine. However, the standards of the party system differ significantly from those generally applied in well-developed Western democracies. These differences concern such essential issues as accountability to the electorate for implementation of party programme provisions, using democratic procedures inside political parties and relations between political parties and business circles. The Ukrainian party system has its roots in the Soviet period as well as in the trajectories of Ukraine's post-Soviet transition.

The leaders and the personnel of Ukraine's newly founded parties had belonged to the upper and middle ranks of the *nomenklatura* before the breakdown of the Soviet system.[17] The political landscape which emerged under their guidance was characterised by a lack of open political discourse and mechanisms. Many of the new parties were creations of business groups from the very beginning, aiming at pursuing individual or group interests rather than providing political representation for larger parts of society. This

15. This concerns the actions taken by President Yushchenko, which have been described in the section 'The 'legal' phase of the conflict', pp. 31-2.

16. See e.g. O. Bondarenko, 'Kirovohrad trial', *Ukrainska Pravda*, 18 October 2006 (retrieved from: http://pravda.com.ua/news/2006/10/18/49224.htm.).

17. Tadeusz Olszanski, *The Ukrainian party system*, CES Analyses, 17 November 1999.

party system, which was consolidated around 1995, failed to provide the necessary foundations for developing a democratic state.[18]

At the same time, the distribution of powers in Ukraine's political system did not provide fertile ground for the development of a pluralistic and dynamic party system. The Ukrainian constitution laid the foundations for a presidential system, in which the parliament played a secondary role compared to the strong executive. The executive authority exploited its advantages and treated the law in the way that it found most suitable for itself, which additionally undermined the prestige of the parliament. During most of the Kuchma era, parliamentary elections did not determine who would govern Ukraine, and consequently there was no need to form a stable parliamentary majority. The government, which reported to the president, did not need any stable support from the parliament. Therefore, there was no stimulus to create a clear 'coalition versus opposition' set-up. The government could assemble *ad hoc* coalitions to vote for specific bills, including through 'working with individual MPs.'[19]

On the other hand, tendencies towards 'presidential centralism' were undermined by strong oligarch groups competing with the state and among themselves and thus guaranteeing a certain form of pluralism. After 2000, the growing politicisation of Ukrainian society resulted in the first protests against the increasingly corrupt political elite. Both factors contributed to the pluralisation of political life.

Political liberalisation and constitutional reform following the Orange Revolution opened a window of opportunity for change in Ukraine's party system. New groups, which had emerged on the Maidan in autumn/winter 2004, entered Ukrainian politics.[20] However, their small membership figures, low level of activity and internal disputes prevented them from fulfilling the task which they had been expected to carry out, namely to bring about a qualitative change on the party political scene.

Major roles are still played by parties of either oligarchic (the Party of Regions, BYuT) or communist origin (the Communist Party of Ukraine, the Socialist Party of Ukraine), which have not undergone a total generational change. Therefore, the party elites set the trend for a certain style of policy-making, which James Sherr has defined as characteristic of 'Ukraine's culture of power: collusive, self-referential, unaccountable (and opaque) to out-

18. Ibid., p. 1.

19. A euphemistic phrase which in fact means 'buying' MPs.

20. For example, the youth movement *Pora!*, which was transformed into a political party in spring 2005.

siders, motivated by subjective interests and restrained only by equal or greater power'.[21]

The basic problem of the Ukrainian party system can be described as follows: political parties are not perceived as representatives of societal interests, but merely as tools of political and business elites, who use the parties to maximise their political influence and financial profits.

The election in March 2006 was the first one to be held according to completely proportional electoral regulations, which greatly reinforced the local significance of parties and stimulated the development of local party structures. However, electoral regulations permitted drawing up partly undisclosed lists of candidates[22] and treating the whole of Ukraine as a single constituency. This resulted in parliamentary seats for a number of candidates who would most likely not have been elected had the country been divided into many constituencies, or had the election procedure allowed for certain candidates on an open party list. The procedure was not changed for the elections in September 2007, mainly because selling party list places to business representatives is a major source of income for political parties in Ukraine.

In Ukrainian politics, business representatives account for a significant majority of MPs.[23] This enables them to lobby for particular bills and guarantees immunity. The situation in which a seat in the parliament is owed not to the voter but to the party leader, who may or may not place the candidate in an 'electable' ('seat-winning') position on the list, changes the loyalty relationship because the MP feels accountable to party leaders rather than to voters.[24] At the same time, considering the circumstances, party membership is treated as an investment, which is successful if returns come quickly and unsuccessful when it takes more time to receive the dividend. The translation of party membership/parliamentary mandates into economic benefit presupposes closeness to the executive. Therefore, changes of government in Ukraine have always been accompanied by the migration of parliamentarians between parties and factions.

To prevent this practice, the amended constitution provides for a so-called imperative mandate mechanism.[25] It imposes a legal ban on changing factions during a given parliamentary term. It appears to have been ineffective,[26] and it has been criticised as undemocratic both in Ukraine and in the West. The Parliamentary

21. James Sherr, 'Ukraine's security. The interplay of internal and external factors', in: *Quid Ukraine's strategic security?*, European Security Forum, Working Paper no. 24, January 2007.

22. The ballots which the voters received at polling stations in March 2006 specified only the names of the first five candidates. Although full lists of candidates were published in the official journal of the Ukrainian parliament *Holos Ukrainy* and on the Central Election Committee's website, the access to such information was significantly restricted.

23. According to estimates published in various press articles, business representatives accounted for approximately two thirds of the MPs (i.e. 300 deputies) elected in March 2006.

24. Volodymyr Horbach, 'Kryza demokratii' [The crisis of democracy], *Narodna Pravda*, 21 May 2007. Available at: http://www.narodnapravda.com.ua/politics/465186c14522e/.

25. The Constitution of Ukraine, Article 81, item 6.

26. Evading the imperative mandate regulation by the coalition was one of the reasons for the dissolution of the parliament by the president on 2 April 2007; see page 30.

Assembly of the Council of Europe (PACE) in their resolution of 19 April 2007 appealed for the cancellation of the regulation.[27]

Another problem is the weakness of party structures at the local level. In many cases, before local elections,[28] a rich local businessman involved in politics is put in charge of the local election campaign budget and the right to draw up lists of candidates, developing a local programme and organising the work of campaign staff. In such cases, situations whereby certain items of the local programmes were inconsistent with or even contradictory to the national programme of a given party occurred quite often before the local elections in March 2006.[29]

A serious problem in the context of democratic accountability is the entirely superficial aspect of party programmes. Ukrainian parties do not compete on real programmes; instead they compete on pre-election slogans and the image of their leaders. The role of their programmes is limited to that of cosmetic window dressing. Usually they include a set of general principles or political goals, without specifying any means necessary to achieve them.

None of the parties which have had a real influence on the functioning of the state has made an attempt to implement their programmes over recent years. It is not surprising therefore that their programmes are not taken seriously by voters. Consequently, party representatives do not feel constrained in making even the most unrealistic electoral promises.

Business and politics – collusive linkages

Relations between business and politics are essential for shaping the principles of a democratic state governed by the rule of law. In this context, similar to the case of political parties, the reality in Ukraine is significantly different from Western European standards.

As mentioned before, business and politics are two interdependent, overlapping and mutually complementary areas of activity. To understand the phenomenon of the 'symbiosis' of political and economic powers, one has to keep in mind the way in which the communist *nomenklatura* gained property in the newly independent state in the early 1990s. 'The process of *nomenklatura* privatisation,' claims James Sherr, 'consummated and partially legalised a process whereby bureaucratic power was transformed into financial power. The principal custodians of this power remained, as

27. Cf. Resolution 1549 (2007), 'Functioning of democratic institutions in Ukraine', Parliamentary Assembly of the Council of Europe, par.9. http://en.wikisource.org/wiki/Parliamentary_Assembly_of_the_Council_of_Europe_-_Resolution_1549_(2007)_Functioning_of_democratic_institutions_in_Ukraine.

28. The local elections coincided with the parliamentary elections in March 2006.

29. 'Analysis of the 2006 local election campaigns', in *National Security and Defence*, no. 8, 2006, p.2. Ukrainian Centre for economic and political studies named after Olexander Razumkov. See: http://www.uceps.org.magazine.

before, an inbred, collusive elite, unrepresentative of the wider society and, in ethos and practice, largely unaccountable to it.'[30]

The *nomenklatura* privatisation, which was carried out amidst legal chaos, coexisting with the formation of the state, contributed to the emergence of a peculiar 'relationship between politics, business and crime that has become characteristic of Ukraine since that time'.[31] The Ukrainian variant of post-Soviet oligarchy was born.

The oligarchs simultaneously control the economic, information (media) and political authority, although it is true that usually this is informal control. The ownership structure of enterprises controlled by individual oligarchs is usually dissembled and presents a false picture of ownership stakes by various companies which are often registered in tax havens (including Cyprus), and in Switzerland, the United Kingdom and the USA. Legal ownership is often less important than an informal influence exerted on the managers and/or owners of the enterprises. The influence can be personal (family relations and/or relations within certain circles), may originate from a previous professional career (which especially concerns former Soviet communist party activists), criminal relations established in the early 1990s or *zemlachestvo* (attachment felt by people to a certain city or region in which they have worked, which is very strong in post-Soviet countries).[32]

The influence on the state administration (both central and regional) very often involves corruption; however, personal relations are very important in this context, as well. Many posts in local state administration structures are filled at least subject to the permission of the oligarchic groups which dominate in the given area. Choosing heads of local government in common elections facilitates the oligarchs appointing 'their men' to the posts. It is not unusual for oligarchs to take the posts themselves.

This description of the pre-2004 realities is still true of today's Ukraine. The actions taken by the 'Orange' governments between 2005 and 2006, including the flagship renationalisation campaign (called reprivatisation) of Kryvorizhstal, or Yushchenko's anti-corruption policy, have failed to bring about a real change in the 'system'.

In this system, political power is first of all a means of supporting, generating and maximising economic profits. The following examples from the post-revolutionary period demonstrate that the shadow structures linking political and economic actors have not significantly changed.

30. James Sherr, op. cit. in note 21.

31. Ibid., p.17.

32. Tadeusz Olszanski, 'Uklad władzy na Ukrainie w przededniu wielkiej zmiany - wyborów prezydenckich 2004', [Who is who in politics and business in Ukraine on the eve of a great change, the presidential election in October 2004], *CES Report*, Warsaw 2004.

One of the typical examples of such behaviour has been the use of influence in the government, especially in the Ukrainian State Property Fund (SPFU) to guarantee victory in bidding procedures during the privatisation process.

On 6 February 2007, SPFU announced that Transport and Investments Technologies (Transportno-Investytsiyni Technologii – TIT), a company representing the interests of the Interpipe group, owned by the leading Ukrainian businessman Viktor Pinchuk, had won the bidding competition for the sale of state-owned 96.67% shares in the Nikipol pipe factory (Nikopolsky Pivdennotrubny Zavod, NPZ). The victorious investor offered a price of approximately US $70 million for NPZ shares, which made it the biggest privatisation transaction to take place in Ukraine for many months. However, the bidding competition result came as no surprise; the factory had for a long time been under the influence of Pinchuk's metallurgical empire. The sham bidding competition in this privatisation process was ensured by the company Logoimpeks, which offered only approximately US $1,200 less than TIT. Both firms which were allegedly rivals for the privatisation of NPZ were in fact controlled by the Interpipe group.[33]

In turn, on 23 March 2007, SPFU offered 76% of the shares in Luhanskteplovoz, one of the largest Ukrainian locomotive manufacturers, for sale to bidders. The bidding was won by a company controlled by the Russian corporation Transmashholding. Only two companies took part in the bidding. They represented the same Russian investor, Transmashholding. The winner, 'Upravlayushchaya kompania Briansky Mashinostroitelny zavod', offered only less than US $60 million for the controlling stake in the Luhansk factory. Their offer was much lower than the estimated market price of the factory (some shares in the Luhansk factory are listed on the local stock exchange) and lower than the prices offered by Ukrainian investors who were interested in buying the company (between US $80 and $100 million). The latter claimed that SPFU had deliberately prevented them from participating in the tender.[34]

Another example of discrimination in favour of businessmen linked to the government is the practice of allocating selective VAT rebates to entrepreneurs. VAT rebating has been the Achilles' heel of the Ukrainian fiscal system for years, and delayed rebates have caused financial liquidity problems for very many firms. In the worst years, the VAT rebate arrears were counted in hundreds of

33. 'The privatisation of the Nikipol pipe factory: a journey back to the past?', *East Week* no. 470, Centre for Eastern Studies (CES), Warsaw, 8 February 2007.

34. 'Another controversial privatisation', *The Bulletin of the CES*, no. 4, Warsaw, 28 March 2007. (On 1 March 2007 CES issued the last issue, no. 473, of *East Week* (Polish version). Since 7 March 2007 the CES has issued *The Bulletin of the CES*).

millions of US dollars. In 2007, the tax was rebated according to selective criteria; firms from Donetsk oblast, which is a major source of political support for the Party of Regions, got VAT rebates of 100%, while firms from Ivanofrankivsk oblast, where 96% of votes were cast for Viktor Yushchenko in 2004, got a rebate of 4%.

Political posts are also (ab)used as a means of protection against political opponents or courts. Parliamentary mandates or government positions fulfil two major goals: They guarantee security to the MPs/officials and their companies, and help develop their businesses. Ukrainian MPs enjoy a very extensive immunity, which practically guarantees them personal inviolability and protects them against prosecution authorities and court actions, including criminal matters. Businessmen appreciated the value of the immunity since widely publicised lawsuits had been brought against some members of the Party of Regions by the 'Orange' government in 2005.[35] This seemed to be one of the main reasons for the great interest in parliamentary seats among businessmen before the March 2006 elections.

The parliament, especially since the implementation of the constitutional reform, has been used as a forum for lobbying for private interests. Passing legislative bills favourable to a given industry or to particular enterprises in a branch of industry have been the most vivid examples of this approach.[36]

The 'Russia factor' in Ukraine's economy

Russia as the largest neighbour and partner, a country with which Ukraine is bound by strong and deep-rooted political, cultural, social and economic ties, plays an important role not only as an 'external partner' but also has a strong impact on domestic politics in Ukraine. Russian and Ukrainian business elites are still closely intertwined, and use their formal and informal networks in order to promote their interests on both sides of the Russian-Ukrainian border. This section therefore investigates the impact these networks have on the functioning of the state and the economy in Ukraine.

The State Statistics Committee of Ukraine (SSCU), ranks Russia only seventh among other investing countries, with US $1.07 billion in direct investments, which is equivalent to 4.8% of total FDI (see box overleaf).

35. Among other cases, the arrest of Kolesnikov, one of the main advisors to Rinat Akhmetov.

36. The Ukrainian specialist press has quoted many examples of such actions taken by representatives of all parliamentary factions. An interesting example is the case of Volodymyr Boiko, who controls the Mariupolsky Metalurgichny Kombinat im. Ilicha ['the Mariupol Metallurgical Plant named after Lenin'], which is worth US$ 2 billion. He had been linked to the Party of Regions since 2002. He left the party to join the Socialist Party before the election in March 2006. Because the leader of the SPFU was a socialist, the Kombinat im. Ilicha had a guarantee of protection against any possible attempts to revise its privatisation process. Boiko, acting either by himself or through his business partner Matvienkov, between 2002 and 2005 proposed 8 detailed bills, 2 of which were passed by the parliament. Cf. O. Muzychenko, N. Verner, O. Shkarpova, 'Chervony Oligarch', *Kontrakty* no. 24, 12 June 2006. See: http://www.kontrakty.com.ua/show/ukr/print_article/7434/2420067434.html.

Russian FDI in Ukraine in comparison to total FDI in the country as of 1 April 2007

	Value (in US$ million)	Share in total FDI (in %)
Total FDI	22,433.7	100
1. Germany	5,690.1	25.4
2. Cyprus	3,226.6	14.4
3. Austria	1,782.3	7.9
4. United Kingdom	1,699.9	7.6
5. Holland	1,692.2	7.5
6. USA	1,360.0	6.1
7. Russia	**1,077.9**	**4.8**
8. Virgin Islands	883.7	3.9
9. France	873.2	3.9
10. Switzerland	566.5	2.5
11. Poland	380.0	1.7

Source: State Statistics Committee of Ukraine.[37]

However, part of Russian foreign investments in Ukraine have been hidden in capital flows originating from other countries, including tax havens in Cyprus and the Virgin Islands. Some investments, which are in fact Russian, may also be officially registered as investments made by Ukrainian companies controlled by Russian entities.

In the era of globalisation, it has become increasingly difficult to identify the exact sources of capital investments from abroad. On the one hand, Ukrainian companies, i.e. those formally incorporated in Ukraine, may invest in accordance with the interests of their Russian owners. On the other, Russian companies operating in Ukraine often belong to supranational corporations. Therefore, it seems that the extent of Russian engagement and, consequently, Russian influence on the Ukrainian economy is much greater than is reflected in official statistics.

Ukraine's dependence on Russia can also be measured by the share the Russian Federation possesses in the total value of Ukrainian foreign trade. According to official data, Russia's share in Ukraine's foreign trade in commodities reached as much as 27.3% in the first four months of 2007 (US $8.9 billion, while the total value of Ukraine's commodities turnover in foreign trade was US $32.56 billion during the period). Russia is the biggest outlet for Ukrainian products (accounting for a 25.2% share in the total value of Ukrainian exports) and the largest import market (29.1%).[38]

Russia has gained importance as a trade partner of Ukraine over recent years owing to increasing prices of natural gas and

37. http://ukrstat.gov.ua/control/en/localfiles/display/operativ/operativ2007/zd/ivu/ivu_e/ivu0407_e.htm

38. This concerns turnovers with individual countries. However, the value of turnovers with the EU-27 is higher than the value of turnovers with Russia.

crude oil imported from the Russian Federation on the one hand, and the expansion of Ukrainian manufacturers in the Russian market, on the other. Over recent months, the growth index has been two times higher in the case of Ukrainian sales to Russia than the average growth index measured for Ukrainian exports in general.

Russia's share in Ukrainian foreign trade in services was 31.15% (US $857.9 versus the total value of US $2,754 million), and its share in service exports reached as much as 40.1% (including incomes generated by transit of Russian oil and gas through Ukrainian territory, among other services).

Russia has a dominant share in the Ukrainian gas, oil and oil product trade sector. Gas (Russian or Central Asian) supplied to Ukraine from Russian territory accounts for over 70% of the country's total gas balance. 74.6% of oil processed in Ukrainian refineries comes from Russia. Moreover, the Ukrainian nuclear power industry is totally dependent on Russian nuclear fuel supplies.

Since the late 1990s, the Ukrainian petrochemical industry has found itself under Russian control. Russians own the four biggest refineries out of six operating in Ukraine.

The enormous energy consumption level, which is characteristic of the Ukrainian economy, makes the country's dependence on Russian energy raw materials (mainly gas) even stronger.

Russian policy on Ukraine can be considered to be a 'game of interests' on various levels. The aim of this game seems to be the maintenance of the political and economic dependence of Ukraine on Russia. This would at the same time undermine Ukraine's integration with Western structures, which Russia sees as a threat to its interests.

At the level of political relations, Russia strives for Ukraine's integration in various organisations which have emerged in the former Soviet Union, in particular the Single Economic Space covering Russia, Ukraine, Kazakhstan and Belarus. As outlined in the chapter by Sabine Fischer, Kyiv has been reluctant to respond positively to such requests, because deeper integration with Russia precludes quick *rapprochement* and the establishment of a free trade zone with the European Union.

Ukrainian-Russian energy relations are formally dealt with at the level of state-owned firms, namely Gazprom and Naftohaz. However, negotiations between these companies are conducted in the presence of government representatives, and are regularly

accompanied by political statements by state officials from both sides. The correlation of economic and political relations was evident during the negotiations over setting the gas prices for 2007 in autumn 2006. According to many commentators, Russia set a relatively low price[39] in exchange for the promise that Viktor Yanukovych's government would give up the idea of promoting the integration of Ukraine and NATO. The Russian leadership has also been lobbying for the creation of a multilateral transit consortium, in which Russia would have a dominant position and Gazprom would assume decisive control of the Ukrainian transit pipeline system.

The politico-economic mechanisms at work in Ukrainian-Russian relations also become visible in the activities performed by Russian and Ukrainian companies. Where possible, they are used to enforce both the interests of their shareholders and the strategic interests of Russia, including strengthening its position in the CIS area. For example ITERA, a company in favour of which the previous management of Gazprom (linked to Rem Viakhirev) discriminated, operated as a gas trader between 1999 and 2002. Then Aleksey Miller, President Putin's *protégé*, was nominated CEO of the monopoly and, in 2003, ITERA was replaced by Eural-TransGaz (ETG), a company which the new management of Gazprom seemed to prefer. In January 2005, the duties of ETG were taken over by RosUkr-Energo. The firms and companies which co-operated with them were registered in tax havens abroad.

ITERA and ETG were suspected of being linked to the respective managements of the Russian monopoly, although there were no documents to prove this. The real shareholders of both companies were unknown. The same is the case with RosUkrEnergo (RUE). The company has been playing the same role under the stewardship of the present management team of Gazprom as ITERA did when Viakhirev directed the monopoly. It has also been acting according to the same pattern. The only major difference between the two companies is that Gazprom has officially confirmed that it holds stakes in RUE. It is commonly believed in Ukraine that RUE operates in the private interest of individuals linked to the management of Gazprom and Russian government structures.

In building agency networks, preference is given to relations based on personal contacts. Although the configurations of such

39. In 2007, Ukraine paid US $130 per 1,000 m^3, which was one of the lowest prices paid by CIS countries.

relations change, the mechanism remains the same: companies whose turnovers are counted in hundreds of millions of dollars are controlled by a small group of people. Most behind-the-scenes shareholders in transactions of this sort remain anonymous, and the names which are revealed from time to time are just the tip of the iceberg.

The impact of informal politico-economic networks can be observed in the actions of individual Ukrainian policymakers as well. They translate into politico-economic decisions which serve Russian interests.

For example former Deputy Prime Minister Mykola Azarov in 2003-2004 staunchly supported the Single Economic Space (SES) project and ensured the parliamentary vote in favour of a law supporting the SES project on 20 April 2004. Some representatives of the energy sector can also be mentioned, including former management staff of NAK Naftohaz. Yuri Boiko is responsible for the decision to operate the Odessa-Brody pipe in 'reverse' mode, i.e. to transport Russian oil in the direction of the Odessa port instead of transporting Caspian oil in the direction of Brody, which was the original intention. It seems that that politically-motivated decision was taken mainly to prevent possible usage of the pipeline as an oil transport route beyond Russian control. Moreover, Yuri Boiko and Ihor Voronin were acting as negotiators for Ukraine in the talks with Gazprom during the gas crisis in late 2005/early 2006. Therefore they, among others, are also responsible for the final shape of the agreement reached on 4 January 2006. As analysed in Chapter Four of this volume, the agreement has introduced conditions in the Ukrainian-Russian gas trade which are unfavourable for Ukraine.

Recently, however, Ukrainian business circles seem to be changing slightly in their attitudes and preferences. As discussed in Rosaria Puglisi's chapter, single oligarchs, like Rinat Akhmetov, have started to go public with reform concepts for Ukraine's state and economy. Another example is Viktor Pinchuk, an oligarch and son-in-law of the former president Kuchma. Pinchuk tries to maintain an equal distance from all the major political parties, focuses on public activity in the modern sense of the term (including patronage and charity work) and does much to improve the image of Ukraine abroad. The fact that international management and auditing practices are becoming increasingly common in Ukraine – primarily in connection with the process of

adjusting to EU standards in order to develop co-operation with EU Member States – is also an indicator of change in the economic sector.

Conclusion

Ukraine is a weak state. The causes of its weakness can be found first of all in the dysfunctionalities of the legal and constitutional system, in the flawed party system and in the non-transparent and corrupt relations between politics and business. The arbitrary application of rules, which has been determined as one of the two major criteria of state weakness, can be found in all those areas. The second criterion, the different forms of corruption, is especially evident in linkages between politics and business and concerns to a great extent the operation of the judicial system and the functioning of political parties.

The **state weakness in the institutional and legal field**, which became especially evident during the crisis in spring 2007, seems to have the greatest impact on the stability of the political system.

The **weakness of the party system** means that growing societal pluralism in Ukraine is not matched by an increase in efficiency within political parties. Parties remain isolated from the Ukrainian electorate, and they do not function according to the democratic rules of the game.

The deep-rooted **'symbiosis' of political authority and business activity** is another immanent feature of the Ukrainian political system and one of the main causes of its weakness. This relationship inevitably impedes the development of a market economy. A lack of transparency in decision-making processes and a lack of politicians' and state officials' accountability for decisions which contradict the national interest are standard features of the system, which contributes to the development of corruption.

It should not be expected that the present model of relations between politics and business will undergo a major change in the near future. Currently, a vast majority of business representatives and large parts of the political elite have a vested interest in preserving the existing rules of the game.

The main challenge which Ukraine has to face after the early parliamentary election held on 30 September 2007 is the stabilisa-

tion of the political system. A way to achieve this is the elimination of the profound causes of the crisis, by developing comprehensive and unambiguous solutions for regulating the political system and also by guaranteeing a clear distribution of powers recognised by all relevant actors. This can only be achieved through a compromise between the key political players in the country.

This would require changing the mindset and the practices of the Ukrainian political elites. A definitive resolution of the tensions dividing the country will become possible only when a clearly defined set of (democratic) rules becomes 'the only game in town'.

Having said that, two short-/mid-term (with a timeframe of up to 2009) and two long-term scenarios for the developing political situation in Ukraine seem possible.

Scenario 1: Continuing/deepening crisis

Despite the formation of the new Orange Coalition, no strategic deal will be reached with the major opposition faction, the Party of Regions. The inevitable conflict resulting from the government's failure to take into account the respective political and business interests will cause a deepening of the crisis. As a consequence, an attempt to change the government or block the operation of the parliament may take place quite soon.

According to this scenario the main political players will not find a consensus on the distribution of power between the main bodies of the executive (the president and government) and the legislature. This in turn will increase instability and cause periodic crises, which will become more serious as the presidential election scheduled for autumn 2009 moves closer.

In the long run, this could mean selective reforms in separate areas of the economy, without the guarantee of creating a foundation for a steady and long-lasting development. This would also probably mean strengthening the principles of non-transparency in such strategic sectors of the national economy as gas trade with Russia.

Scenario 2: A 'Big Deal' between the major players

This scenario assumes that the three major political forces reach a settlement which serves their conflicting interests, thus paving

the way for a 'rainbow' coalition. Such a development could lead to the formal establishment of a coalition of the Party of Regions, BYuT and Our Ukraine. If no formal coalition agreement is possible, it could also imply that the main opposition parties support the ruling party or coalition with regard to individual political issues.

Formal or informal cooperation of the main political forces would allow for the necessary amendments of the constitution in order to precisely determine the separation of powers. This would be the precondition for a solid and enduring stabilisation of the country's political system.

However, this scenario is very unlikely, because of serious differences between the Party of Regions and BYuT. Tensions between Viktor Yushchenko and Yulia Tymoshenko, emanating from the latter's presidential ambitions, do not tend to favour compromise either.

In the long run, the choice of this path of development could lead to the eventual transformation of the present system into a democratic state governed by the rule of law, with a socially-oriented market economy. Before such a scenario is realised, the elites will have to reach a consensus regarding radical structural reforms to build a foundation for stable and long-lasting development. This would also require a change of mindset, namely granting absolute supremacy to legal regulations over unofficial arrangements between politics and business.

The analysis presented in this chapter does not provide much hope that the political elites will quickly change their attitudes and undertake the steps necessary for a realisation of the second scenario, which could eventually lead Ukraine forward on the path towards stable and democratic statehood and society. However, a number of observations make the picture appear perhaps less bleak.

Firstly, the antagonistic political players managed, in spring 2007, to overcome one of the worst political crises since Ukraine's independence through political compromise and without resorting to the use of force. Obviously a majority of Ukrainian politicians and citizens are united in the firm belief that a crisis escalating into violent confrontation could lead to a national tragedy. This attitude is supported by the heads of the security forces themselves, who have made it clear that they will not allow their troops to be used for activities that are in breach of the constitution.

Secondly, there is growing awareness among business elites that further development of the country and creation of conditions for unrestricted business activity are only possible if the 'rules of the game' change. These actors are becoming more and more favourable to the adoption of precise, unambiguous and generally applicable legal regulations to guarantee respect for constitutional rule on the one hand, and respect for property rights, freedom of business activity and favourable conditions for business involvement in European and global markets on the other.

Ultimately, the political pluralism existing in Ukraine puts the country into a totally different category from the vast majority of post-Soviet countries. This pluralism enables true political competition and offers citizens a genuine possibility of choice. A diverse, independent and free media – considering the relative weakness of the non-governmental sector – play a major role in promoting the standards of democracy and transparency in public life.

All these phenomena prove that the potential for change and sustainable development exists in Ukraine. Whether this potential can be used constructively – or not – depends on the strategic choice of the political and economic elites and on the future evolution of Ukrainian society.

A window to the world? Oligarchs and foreign policy in Ukraine

Rosaria Puglisi

2

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NB This chapter only covers events in Ukraine up until July 2007.

Introduction

With the crystallisation of pro-European positions among the leading figures of the country's economic elite in the aftermath of the Orange Revolution, the century-long Ukrainian dilemma of choosing between an East-oriented and West-oriented foreign policy gained new momentum. In their effort to acquire social legitimisation, to consolidate their ownership rights and to expand control over business assets across Ukraine's borders, a number of prominent Ukrainian businessmen became active supporters of Ukraine's engagement in the international community, thus playing a potentially important role in the setting of their country's foreign policy preferences.

Following President Yushchenko's election, commitment towards Ukraine's European orientation, at least at a rhetorical level, and possibly even aiming at EU membership, became common currency in the Ukrainian domestic debate. Even with the appointment of the allegedly pro-Russian government of Prime Minister Yanukovich in August 2006, pro-European positions went, by and large, unchallenged. Despite conflicting in virtually every realm of Ukrainian politics, both President and Prime Minister claimed to agree that a European future was the way forward for Ukraine (their differences, the Prime Minister would specify, lay in terms of what strategy to adopt, rather than the ultimate objective).

In this wider context, the individual interests of some Ukrainian entrepreneurs who had, in the previous decade, plundered Ukraine's wealth through less-than-transparent deals, came to overlap with the country's interest in closer interaction with and integration into the international community. The increasing attractiveness of European political standards and rule of law, seen as providing a guarantee to their economic activities *vis-à-vis* the uncertainties generated by the unstable Ukrainian legal and political system (from which they had themselves previously

profited), coupled with alluring investment prospects on the territory of EU member states, were these businessmen's key motivation.

While a tendency towards some forms of 'Europeanisation' and adaptation to Western business standards was already present before the Orange Revolution, the events of winter 2004 proved a powerful catalyst and made this trend public. The oligarchs feared that the 2004 presidential elections would be a watershed and the regime change that followed would signify a potential 'end of history' for their power and property. The Orange Revolution and the lack of substantial changes in its aftermath gave them the sense of urgency and the audacity to restyle themselves as Western-oriented Ukrainian patriots in order to distance themselves from the now disgraced Kuchma regime.

Playing a possible balancing role in the deeply divided and contentious domestic political arena, the oligarchs' contribution to Ukraine's processes of integration could yet prove significant. Although essentially motivated by personal interests, they might nonetheless become unintentional promoters of irreversible change and lock Ukraine into a process of binding political and economic reforms by default.

Oligarchs before and after the Orange Revolution

Like many post-Soviet societies, following independence, Ukraine experienced the emergence of an oligarchic system. In the mid-1990s, political influence, proximity to the sources of political power and control over political institutions allowed some powerful entrepreneurs to acquire exclusive authority over economic wealth and to secure property rights over former state assets undergoing privatisation. In exchange, they provided support for the establishment and the consolidation of a semi-authoritarian regime revolving around the central figure of Ukraine's second President, Leonid Kuchma.

The demise of the Kuchma regime, with the failure to elect a successor immediately connected to the President's inner circle in the 2004 elections, generated expectations that a new political elite would come to power. However, despite vocal reassurances that the umbilical cord between business and politics that had characterised the first decade of Ukraine's independence would

finally be severed, the political and economic groups orbiting around the newly elected President Yushchenko failed to induce substantial changes. The golden opportunity to put the interaction between political power and business on an entirely new footing was thus missed in the Orange Coalition's first year in power.

With the spring 2006 parliamentary elections, the return to power of a Party of Regions majority, and the *déjà-vu* appointment of Viktor Yanukovich as Prime Minister, the history of oligarchic power in Ukraine came full circle. Big business figures were back in the spotlight, but under altered political and economic conditions. In an environment where the presidency had become one of the many competing centres of power and the number of access points to institutional power had multiplied, the oligarchs' influence over decision-making processes changed significantly.

The emergence of an oligarchic structure under Kuchma. In Ukraine, as in Russia, an economic elite appeared as a result of the late 1980s/early 1990s economic reforms.[1] Wealth was accumulated through four main channels. First, through the trade of metals and chemicals bought in Ukraine at state-regulated prices (equal to 10% of world prices at the time) and sold abroad at full market prices. Second, through the trade of products (like Russian gas) imported at subsidised exchange rates and sold in hard currency. Third, through subsidised credits issued at 20% interest a year when inflation was running at 10.155%. Fourth, through budget subsidies (equal to 8.1% of GDP in 1992 and 10.8% in 1993) concentrated mainly in the agricultural sector, and in the gas and the coal industry.[2] Insider privatisation (or *nomenklatura* privatisation) provided a further opportunity for the consolidation of the economic elite, turning state enterprise directors into a property-owning class.[3] Business and political elites became enmeshed in a mutually dependent rent-seeker/rent-giver relationship. In this exchange, powerful economic actors were provided with a political *krysha* (roof or protection) to conduct murky business deals, while political leaders received economic support to consolidate their positions of authority. In the eight years of the two Kuchma presidencies, this system reached perfection. An oligarchic system emerged and consolidated thanks to the special privileges awarded by the President and his administration to the members of his inner circle. The President's

1. Throughout this chapter, the definition of oligarchs is applied to powerful economic actors who take control of political institutions and through continued control over them pursue their own narrow interests, even in disregard of the general public interest. Although a generalisation, the term 'economic elite' is often used interchangeably with 'oligarchs'.

2. Anders Aslund, 'Problems with Economic Transformation in Ukraine', paper presented at the Fifth Dubrovnik Conference on Transition Economies, 23-25 June 1999. See: http://wwwceip.org/files/Publications/webnote10.asp?from=pubproject. On the emergence of the Russian economic elite, cf. Anders Aslund, 'Russia's Collapse', *Foreign Affairs*, September/October 1999, pp. 64-77. For an analysis of the early stages of oligarchic power in Ukraine, see Rosaria Puglisi, 'The Rise of the Ukrainian Oligarchy', *Democratization*, vol. 10, no. 3, Autumn 2003, pp. 99-123.

3. For an overview of the privatisation programme, see Igor Filatotchev et al., 'Privatisation and Industrial Restructuring in Ukraine', *Communist Economies and Economic Transformation*, vol. 8, no. 2, 1996, pp. 185-203.

patronage network set relations between political power and business on new foundations. Closeness to the President guaranteed access to the administration, redistribution and utilisation of state financial or administrative resources, and in this way large fortunes were made virtually overnight. During his first mandate (1994-98), the President's 'personal rulership' to some extent played an 'integrative role' over a potentially heterogeneous political environment, temporarily unifying competing elite clans through the redistribution of material incentives and rewards.[4] The allocation of favours and economic benefits rather than ideology, the rule of law or the leader's charisma constituted the cement of this system, while a sense of loyalty and dependence informed formal political and administrative relations.[5] Redistribution of resources, promises of privileged access to the privatisation of strategic assets and management of profitable state enterprises were all used to reward loyal supporters. Conversely, exclusion from all these opportunities served as a punishment for those who challenged the president's authority. Asymmetrical control over the political institutions created a dividing line of divergent interests and possibilities between big and small/medium-sized enterprises. Political power allowed figures from big business to shape the rules of the market to suit their own preferences, defending their newly acquired property rights and preserving their privileges. Small and medium-sized businesses, in contrast, were generally remote from political power and were therefore exposed to the full force of market fluctuations and to the unpredictability of the bureaucratic economic environment. Because of the gradual but ineluctable transition towards an authoritarian rather than democratic political regime, the consolidation of the presidency as the central political institution in the country and its isolation from other political forces and public opinion at large (all aspects increasingly evident during his second mandate), President Kuchma and his administration became instrumental in the rise, stratification and entrenchment of the Ukrainian oligarchs in the country's economic and political system. Leaning on a powerful circle of business actors who could provide support against potential challenges from outsiders became for the presidency a politically rational strategy. A 'partial reform equilibrium' sealed the alliance between the executive and parts of the economic elite.[6] Economic liberalisation was pushed only as far as allowing the privatisation of state assets,

4. On personal rulership, see Guenther Roth, 'Personal Rulership, Patrimonialism and Empire-Building in the New States', *World Politics*, vol. 20, January 1968, pp. 194-206; on the effects of patrimonialism on fragmented societies, see Gerald A. Heeger, *The Politics of Underdevelopment* (London: Macmillan, 1974).

5. Michael Bratton and Nicholas Van de Walle, 'Neopatrimonial Regimes and Transitions in Africa', *World Politics*, vol. 46, no. 4, June 1994, pp. 453-89. For a discussion on patrimonial authoritarianism in Russia see Celeste Wallander, 'Russian Transimperialism and Its Implications', *Washington Quarterly*, Spring, 30:2, 2007, pp. 107-122.

6. For an academic discussion of partial reform equilibrium, see Joel Hellman, 'Winners Take All: The Politics of Partial Reforms in Postcommunist Transitions', *World Politics*, vol. 50, no. 2, February 1998, pp. 203-34; see also Joel Hellman, Geraint Jones and Daniel Kaufman, 'Seize the State, Seize the Day: State Capture and Influence in Transition Economies', *Journal of Comparative Economics*, no. 31, 2003, pp. 751-73.

but not the correction of market distortions. The 'selective introduction of market mechanisms' and the consequent generation of concentrated rents prompted a small group of actors, net winners under these conditions, to work actively for the preservation of the *status quo*.The oligarchs' accumulation of wealth and the endurance of the Kuchma regime, even in open disregard of rising popular discontent, became mutually reinforcing phenomena. The systematic extraction of rents had lasting and deleterious repercussions on Ukrainian society. The distribution of income and the allocation of funds within a narrow constituency, the corruption of the state apparatus and the consequent expansion of the illegal economy, the lack of accountability and the resulting isolation of the political leadership weakened the capacity of the Ukrainian state.[7] Evidence of exceptional difficulties in the economic field and a persistent lack of visible economic results during his first term, coupled with utter contempt for public opposition, fatally alienated the President from civil society.[8] The systematic ousting from political institutions and exclusion from resources redistribution mechanisms of sections of the elite that had originally emerged within his circle (like former Governor of the National Bank and 1999-2001 Prime Minister Viktor Yushchenko and 1999-2001 Deputy Prime Minister Yulia Tymoshenko) gave momentum to a political opposition movement that made fighting against the corruption and the excesses of the Kuchma regime the core of its electoral manifesto.

Missed opportunities under Yushchenko. The separation of business and politics was one of the main demands of the protestors who came out into the streets during the Orange Revolution. Coming to power as Prime Minister in January 2005, Yulia Tymoshenko promised the review of 3,000 allegedly unlawful privatisations that had been carried out during the Kuchma presidency. In the immediate aftermath of the Orange Revolution, prominent oligarchs who had occupied central stage during the Kuchma years disappeared from the public scene. Fearing retribution and a challenge to their contested ownership rights, some took up residence abroad, others simply kept a low profile, waiting for the storm to subside. In his 2006 annual address to Parliament, President Yushchenko proudly announced the dismantling of oligarchy in Ukraine. 'The system of oligarchic control over the economy has been weakened and deprived of support by the state', he

7. Joel Hellman, 'Winners Take All...', op. cit. in note 6.

8. Kuchma failed to resign even following the explosion of the Gongadze case and the ensuing mass movement 'Ukraine without Kuchma' in 2000-2001.

boasted.[9] In actual fact, beyond boisterous threats and emphatic promises, the Yushchenko leadership did little to readdress the balance of power between business and politics. If the role and influence of big business representatives changed qualitatively following the demise of the Kuchma regime, this was more the result of a number of different, accidentally related factors, than the outcome of a deliberate policy endorsed by the new President and his team. Itself plagued by internal, structural issues that weakened its determination to move against patronage networks, the Orange leadership failed to endorse a coherent approach to substantial reforms in this sphere. The Orange leadership's greatest (and only) success in their campaign towards fairer business-politics relations was the reprivatisation of the steel giant Kyvorizhstal. In a widely publicised auction, hailed by Ukrainian commentators as 'the end of an era when well-connected tycoons ruled Ukraine',[10] the government sold Kryvorizhstal to the Indian company Mittal Steel for $4.84 billion, equal to one fifth of the Ukrainian state budget. The plant had been initially privatised in the run-up to the 2004 presidential elections by a consortium set up by Viktor Pinchuk (President Kuchma's son-in-law) and Rinat Akhmetov (Viktor Yanukovich's main financial supporter in the 2004 presidential race). The selling price at that time had been $800 million.In spite of Interior Minister Lutsenko's announcement that 1,700 legal cases had been initiated for alleged violations of the privatisation process,[11] Kryvorizhstal was the only one to be finalised in court.[12] The looming prospect of large-scale reprivatisations created uncertainty in the Ukrainian business environment, affecting also those foreign investors President Yushchenko had tried to woo in the aftermath of the revolution. Writing in those days, a *Financial Times* commentator advised that, in order to avoid political distortions of the market and to minimise investors' anxiety, the review of past privatisation deals should be 'limited in scope, governed by transparent rules and completed within a clearly stated and very brief time'.[13] Instead, following Yulia Tymoshenko's dismissal from her Prime Ministerial post in early autumn 2005, the Ukrainian authorities opted for an all-round 'forgive and forget' strategy. The new Prime Minister, Yurii Ekhanurov, swiftly reassured the public that Kryvorizhstal would be the last reprivatisation and that he would resist popular pressure to reconsider previously concluded deals.[14] 'The process of reprivatisation in Ukraine is over, full stop.

9. *UT1 TV*, as reported in BBC Monitoring Service in English, 9 February 2006.

10. *UT1 TV*, as reported in BBC Monitoring research in English, 24 October 2005.

11. Oleksander Paskhaver and Lena Verkhovoda, 'Privatizatsiya do i posle oranzhevoi revolutsii', Working Paper, Tsentr Sotsialno-ekonomicheskikh Issledovanii (Kyiv: CASE Ukraina, 2006).

12. Pinchuk's minority shares in the insurance company Oranta were also returned to the state, while the fate of Pinchuk's contested property of the Nikopol ferro-alloy plant remains to be adjudicated by the court. Oleksander Paskhaver and Lena Verkhovoda, op. cit. in note 11.

13. 'Ukraine: An Exemplary Start', *Financial Times*, 26 October 2005, editorial comment.

14. Tom Warner, 'Sale Ends Ukrainian 'Re-privatisations'', *Financial Times* 26 October 2005.

We have delivered on whatever promises and pledges were given in Independence Square during the revolution', Prime Minister Ekhanurov remarked in November 2005.[15] While attempts were made to work out a method of peaceful settlement of disputed privatisations, according to which, in exchange for a negotiated compensation, owners would be entitled to keep the privatised company, no peaceful settlement ever took place.[16] The process of reprivatisation was closed in the same way it had been emphatically opened, namely as a result of a political decision. The question of the 'settlement of disputed privatisations' (or additional, possibly voluntary payments to be made by oligarchs to compensate the state for the acquisition of assets at below-market prices) was not even touched upon during the meeting President Yushchenko held with 20 leading business representatives in October 2005.[17] According to press reports, in a long, conciliatory speech, the President invited his guests to invest in industrial production, to pay taxes and to give up on corruption, but made no reference to past privatisations. Upon leaving the meeting, some of those who the Ukrainian media were already calling 'ex-oligarchs' appeared visibly relieved that, as Rinat Akhmetov put it, 'the word reprivatisation does not exist anymore'. Eduard Shifrin shrugged at the idea of making additional payments, controversially claiming compensation for the investments he had made in rundown industrial facilities. Viktor Pinchuk rejected accusations of corruption, but admitted, 'mistakes were made'.[18] The first 'Council of the Oligarchs' (as the press dubbed the meeting) marked an important turning point in relations between the Orange leadership and big business. Explaining the purpose of the gathering, Prime Minister Ekhanurov pointed out: 'We really want these people to become truly dedicated, with a strong national sense, and (...) a middle class, and [we want them to] be very sincerely involved in our business promotion and development'.[19] With the organisation of the meeting, the President extended a friendly hand to business representatives and proposed a truce to them: business would have to become socially responsible and, in exchange, no financial claims would be made upon them to amend past mistakes. Disappointed Ukrainian observers judged the move a *faux pas* on the part of the President, another missed opportunity to set the previous record straight and recover additional badly needed budgetary resources.[20] However, the Orange leadership also had internal and structural reasons to avoid a

15. The Honorable Yurii I. Ekhanurov, Prime Minister of Ukraine, speech at the Carnegie Endowment for Peace, Washington, 1 November 2005, published in the *Ukraine Action Report*, no. 597, article 1.

16. Oleksander Paskhaver and Lena Verkhovoda, op. cit.

17. The list of attendees at the meeting offers an interesting insight as to who the Presidential Secretariat considered the core of Ukraine's economic elite: Rinat Akhmetov (SCM), Vyacheslav Boguslaev (Motor Sich), Vladimir Boiko (Maryupol Metallurgical Kombinat), Vitalii Haiduk (IUD), Andrei Kluyev (Ukrpodshipnik), Ihor Kolomoisky (Privat bank), Valentin Landik (Nord), Viktor Pinchuk (Interpipe), Vladimir Polyachenko (Kyievgostroi), Aleksei Poroshenko (Ukrprominvest), Georgii Skudar (Novocramatorskii car factory), Aleksander Slobodyan (Obolon), Grigorii Surkis (Slavutich), Evhenii Utkin (Kvazar-Mikro), Valerii Khoroshkovskii (Inter TV), Eduard Shifrin (Zaporozhstal'), Nikolay Yankovskii (Stirol), Aleksandr Yaroslavskii (Ukrsibbank). Leonid Chernovetskii (Praveksbank) was invited but did not participate. Sergei Modra and A. Andrevskaya, 'Yushchenko pokazal eks-oligarkham mesta ikh byloi lobbistkoi slavy', *Ukrainska Pravda website*, 10 October 2005.

18. Sergei Modra, 'Akhmetov: Ya bolshe lyublyu chai pit' doma. Surkis: Ya ne mogu byt' vragom prezidenta, Pinchuk: by ne khotelos vnov' idti v deputaty', *Ukrainska Pravda website*, 15 October 2005.

19. The Honorable Yurii I. Ekhanurov, op. cit. in note 15.

20. Author's interview, Kyiv, 6 November 2006.

frontal attack on oligarchic interests. A number of big and medium-sized businessmen (the *minigarchs*[21]) had played an active role in the revolution, standing by the President during the campaign and staffing his inner circle in the post-revolution period. Petro Poroshenko (Secretary of the Security and Defence Council) and David Zhvanya (former Minister for Emergency Situations), Evhen Chervonenko (former Minister of Transport), Ivan Plachkov (Fuel and Energy Minister), Alkesei Ivchenko (Head of Ukraine's gas and oil monopoly structure Naftohaz Ukraina), Oleksander Morozov (MP and Head of the State Savings Bank of Ukraine), Stanislav Arzhevitin (Deputy Emergency Minister and Chairman of Azhio Bank Board of Directors), Serhii Taruta (co-owner of the Donetsk-based Industrial Union of Donbass), Hares Yussef (businessman and presidential advisor) were some of the most prominent names.[22] Allegations about their corruption and the wealth they had earned as a result of their proximity to President Yushchenko were widespread in the Ukrainian media.

Oligarchs in a changed political environment. The dismissal of the Tymoshenko government in the autumn of 2005, as a result of the Prime Minister's squabbles with Secretary of the Security and Defence Council Poroshenko, was interpreted by many as a sign that the oligarchic wing in the President's circle (the so-called *lyubi druzy*, the 'dear friends') had prevailed. Mykola Tomenko, one of Tymoshenko's closest allies, accused President Yushchenko of 'wobbling between the interests of Ukraine and those of his personal friends'. He claimed that a new Kuchma-like structure of power had emerged, with Yushchenko having become a 'hostage' of the old system. 'Today the President's entourage is trying to recreate the set-up pioneered during Kuchma's rule, when certain businessmen-turned-ministers ensured the well-being of the presidential family', Tomenko concluded.[23]

Despite the persisting interconnection and mutual dependency between business and politics, Tomenko was wrong on one account: Yushchenko's Ukraine was not Kuchma's Ukraine. Although not necessarily as a result of deliberate political moves induced by the Orange leadership, a number of key factors had changed. Branding it a 'bourgeois revolution', a Ukrainian commentator succinctly summed up the spirit and the significance of the social and political transformations that followed the events of 2004.[24] In addition to a widespread but ephemeral sense of

21. The expression is Oleh Havrylyshyn's. Workshop on Business and State Relations in Russia and Ukraine, Jacyk Program for the Study of Ukraine and CERES, Toronto, 30 November 2006.

22. Sergey Leshchenko, 'Viktor Yushchenko's Political Orbits', *Ukrainska Pravda* website, 20 January 2006, as reported in *BBC Monitoring Service*, UK, in English, 5 February 2006.

23. Mikola Tomenko, 'Changes are Only About to Begin, or is the Second Phase of the Orange Revolution Possible?', *Ukrainska Pravda* website, 30 September 2005.

24. Author's interview, Kyiv, 9 February 2007.

empowerment among ordinary citizens, the Orange Revolution brought about substantial adjustments in the balance of power between institutions and in the interaction between institutions and elites. Hastily introduced in December 2004, as a compromise to resolve the constitutional impasse created by the rigging of the presidential elections, the constitutional reforms set in place an inherently unstable institutional system. Even more dangerously, they failed to provide mechanisms to peacefully manage the awkward cohabitation between the opposing President and Prime Minister. Despite their many serious shortcomings, however, the constitutional reforms produced one single positive result: they contributed to the dismantling of the complex architecture of power that had grown around the presidency in the Kuchma years. Under Yushchenko, the presidency became one of the many competing centres of power, dispersing the presence and influence of economic interests over state institutions. The resultant dispersal of power promoted a certain degree of pluralism and compelled conflicting economic forces to work towards broader coalition and consensus building.

In the specific case of business-politics relations, the gradual but inescapable erosion of authority imposed on the presidency as a result of the constitutional reforms multiplied the number of access points to political structures afforded to economic clans. Business became emancipated from the tight tutelage that President Kuchma used to exercise, thus reversing a previously consolidated relationship of power. If before the revolution politics ruled business, the Orange Revolution gave the opportunity to big and medium-sized businesses to take power directly into their own hands.[25] As a result of what somebody called 'the war of millionaires against billionaires', the monopolistic control of power enjoyed by oligarchs before the revolution was broken and some form of competition was introduced into the system.[26] The 2006 parliamentary elections proved a remarkable opportunity for business groups to access political institutions *en masse*. Oligarchs and economic actors had gained increasingly wide representation in the legislature since independence, but the first elections since the Orange Revolution saw a real breakthrough in this regard.[27] Commentators painted a gloomy picture of a political process that had lost its ideological character and had become 'monetised'. With a 'price list' set for all key posts, analysts reported that candidates would simply buy places in party lists from the party

25. Ibid.

26. Author's interview, 15 February 2007.

27. For a comparison with previously elected parliaments see Rosaria Puglisi, 'The Rise of the Ukrainian Oligarchy', op. cit. in note 2.

leaders.[28] Some blamed recently introduced proportional representation for what they called the *oligarchisation* of power.[29] Former Deputy Speaker of Parliament and former ally of Yushchenko, Oleksander Zinchenko, predicted that oligarchs would end up controlling parliamentary factions. 'It is obvious even now', he remarked, 'that money is playing the defining role as far as March's parliamentary elections are concerned. All political parties or blocs include oligarchs and they, I can assure you, are playing key roles'.[30] According to an urban legend widely circulated even by high-ranking politicians (including Yulia Tymoshenko), among its 450 members, the new parliament counted at least 300 dollar-millionaires (for an outline of the representation of business interests in the 2006 parliamentary factions, see table 1 at the end of this chapter).[31] Statistics were never compiled on the actual number of business representatives who entered parliament. Yet, oligarchs had obviously adopted different strategies of interaction with the institutional power. Rinat Akhmetov, who had previously been a withdrawn figure in terms of public life, ran and won a seat with the Party of Regions, whereas Viktor Pinchuk announced that his decision as to whether to take part in the elections or not depended on the guarantees that the Yushchenko leadership would provide in terms of protection of his property rights.[32] Eventually, he did not run.With the appointment of the Yanukovich government in summer 2006, the emphasis shifted back to the uncontested primacy of business over politics. An atmosphere of *déjà vu* pervaded the corridors of power. Ukrainian observers labelled Yanukovich's government 'the new/old government'.[33] Old faces of the Kuchma administration resurfaced in previously unthinkable permutations. New/old ministers and the Prime Minister's advisors were deployed in a turf war with the President and his circles for the control (both at a national and at a regional level) of the *vertikal vlasti* (the hierarchy of power structures).[34] Some of the first and most controversial steps of the Yanukovich government gave a clear indication that the personal interests of influential business people would remain a factor to be reckoned with within the state administration. Plans for the restoration of free economic zones, the selective granting of VAT refunds to export companies, the careful drafting of rules for the privatisation of land and regional energy companies and the unveiling of the 2007 state budget constituted, in the eyes of some Ukrainian commentators,

28. Author's interview, Kyiv, 9 February 2007.

29. T. Khrush, 'How to stop the Oligarchisation of Power', *The Day Weekly Digest*, in English, no. 2, 31 January 2006.

30. *Interfax*, 16 January 2006.

31. T. Khrush, op. cit in note 29.

32. Sergei Modra, 'Akhmetov: Ya bolshe lyublyu chai pit' doma...', op. cit. in note 18. Pinchuk had been an MP in the two previous legislatures.

33. Tatiana Kremen and Andrei Smirnov, '100 dnei zastoya', *Korrespondent*, no. 44 (233), 11 November 2006, pp.18-22.

34. On the re-staffing of national and regional institutions with personnel loyal to PM Yanukovich, see 'The Friar's Greed...', *Ostrov website* (Donetsk), 31 August 2006, as reprinted in *BBC Monitoring Service*, in English, 5 September 2006. On the Yushchenko-Yanukovich confrontational personnel policy, see Yulia Mostovaya, 'Self-destruction Strategy' , *Zerkalo Nedeli on the Web*, no. 39 (618), 14-20 October 2006.

a serious setback to the prospects of a freemarket economy in Ukraine and displayed the firm control of powerful economic actors over policy-making.[35] In a contradictory turn of events compared to the early days of the Orange leadership, a general climate of uncertainty and political strife contributed to securing oligarchic control over the institutions. As a counterbalance to the authority of Yanukovich's Party of Regions, by its own admission a business party and a concrete expression of the industrial interests of the so-called Donetsk clan, in autumn 2006 President Yushchenko harnessed support in a breakaway faction of the Donetsk group, Sergey Taruta's Industrial Union of Donbass (IUD). Faced with an Orange Coalition in disarray, a lack of strategic thinking among his own team, a crumbling power base (within his own party, Nasha Ukraina), and plummeting popularity rates, with the appointment of Vitalii Haiduk (IUD co-owner) as Secretary of the Security and Defence Council and Oleksander Chaly (former deputy Foreign Minister but also close to the IUD's leadership) as deputy head of the Presidential Secretariat, the signal was given that a new alliance between the President and one of the most powerful financial-industrial groups of the country had been sealed.

Social legitimisation and economic liberty

After the Orange Revolution, the presence and influence of oligarchs on Ukrainian politics changed qualitatively. Following a period of meditative withdrawal, big businessmen reappeared on the country's social and political scene reinvigorated and ready to engage in a full-scale campaign to clear their names and rebuild their reputations The events of winter 2004 and their aftermath proved, from this perspective, to be a watershed with regard to the oligarchs' role in Ukrainian society.Having eluded threats of property redistribution, they chose to come out of the shadows in which they had lived after the collapse of the Kuchma regime and to become public figures again. Some went into parliament. Others stayed clear of official political positions but engaged in high-profile, socially-oriented projects. By and large, they strove to do away with the image of corrupt, arrogant plutocrats, even violent thugs, that years of fast and easy capital accumulation had earned them. Vociferously rejecting the label of oligarchs, they now presented

35. See, for example, Sergei Soroka, 'Budget Azarova: Smertitel'ny vystrel po liberalizovannoi ekonomike', *Ukrainiska Pravda* website, 20 September 2006; Natalia Yatsenko, 'Billions of Illusions. Coalition's Omnipotence and the President's Veto: Can This Fragile Construction Guarantee Ukraine's Transparent and Effective Economic Development?', *Zerkalo Nedeli on the web*, no. 47, 9-15 December 2006; Natalia. Yatsenko, 'Full Speed Ahead, Anticrisis Coalition Initiates the Revival Free Economic Zones and Techno-Parks', *Zerkalo Nedeli on the Web* no. 29, 29 July-4 August 2006.

themselves in the benign guise of national capitalists. The narrative of a business elite, socially responsible and genuinely concerned with the well-being of its own country, was thus born. Beyond the makeover and the quest for a new public image, however, the oligarchs had substantial reasons for making this move. Not only had political conditions changed significantly since President Yushchenko's coming to power, but also economic conditions had altered (albeit almost irrespectively of political events).

The phase of primary capital accumulation that had characterised the Kuchma presidencies was over. The number and quality of assets expected to undergo privatisation was now relatively insignificant in comparison to the deluge of the mid- to late-1990s. In a phase of capital consolidation rather than capital expansion, big businessmen became aware that two conditions would have to be satisfied if the recent positive trends experienced by the Ukrainian economy in general and their companies in particular were to be sustained. Firstly, a system of transparent and more or less universally applied norms would need to be firmly established in Ukraine, thus carving in stone their ownership rights and granting their businesses the protection a court of law would provide. Secondly, industrial methods would need to be dramatically modernised, plants upgraded, and energy-saving technologies introduced. A shift was required from an extensive to an intensive approach to economic growth. In short, the Ukrainian economy had to become part of the world economy in order to fully benefit from the market opportunities on offer; but in order for this to happen, securing a constant inflow of foreign and domestic investment was crucial. In this perspective, paradoxically and for the first time since independence, the selfish, individual interests of some business representatives came to overlap with the interests of Ukraine in general. Some (although by no means all) oligarchs realised that the value of their businesses was related to and affected by the country's international reputation and political stability. The centuries-old Ukrainian foreign policy dilemma between an East/West geopolitical orientation thus acquired a new, unexpected and more sophisticated dimension, becoming a choice between two alternative models of economic development.

Not oligarchs but big business representatives. In October 2006, Kyiv's *beau monde* gathered for the premiere screening of a documentary, co-funded by Viktor Pinchuk and Steven Spiel-

berg, on the Shoah in Ukraine. At the end of the screening, Pinchuk, taking questions from the audience together with Spielberg and the film director Serhii Bukovsky, hinted that he envisaged the movie as part of a trilogy he might be willing to finance on the three great tragedies that had affected modern Ukraine, including *Holodomor* (the man-induced famine of the 1930s) and the Chernobyl nuclear disaster. Following the Orange Revolution, Viktor Pinchuk appeared as indisputably the most active (and successful) among former oligarchs in trying to recreate an image for himself as a philanthropist, a 'patriot' (as he put it) and as a man passionately concerned with Ukraine's development and integration into the international community. With its high profile and internationally attended events, the Yalta European Strategy (YES), the international network he set up in 2004 with the declared purpose of promoting 'the development of a just, free and prosperous Ukraine, to open the country to the rest of the world and to support Ukraine's membership of the European Union', was among Pinchuk's most successful endeavours.[36]

The social activism demonstrated by Pinchuk, however, was far from being an isolated phenomenon in Kyiv's business circles. Throughout 2006, a score of well-documented press reports on the oligarchs' numerous and munificent charity activities appeared in the papers, advertising the human as well as the civically engaged face of individuals whose reputation had so far been associated with illegal privatisations, corruption and murky business deals.[37] Hyhorii Surkis, former MP and ally of the Head of Kuchma's Presidential Administration, Viktor Medvechuk, threw himself into football and, in his capacity as President of the Ukrainian Football Federation, became the main sponsor of the successful joint Ukrainian-Polish bid to host the 2012 European Football Championship. Rinat Akhmetov, widely recognised as the richest man in Ukraine with his personal wealth estimated at $11.8 billion (see table 2 at the end of this chapter), one of the leaders of the notorious Donetsk clan and the most prominent financial supporter of Yanukovich's electoral race in the 2004 presidential elections, became a member of parliament for the Party of the Regions. Campaigning in his home constituency, he explained his motives for taking up politics as follows: 'I want a government of economic growth, (...) I want to defend Ukraine's national interests, (...) I want Ukraine to become rich, (...) I want there to be no poor people in Ukraine.'[38] The oligarchs' quest for

36. For more details on Yalta European Strategy see the organisation's website at http://www.yes-ukraine.org/en/programme2007.html. In addition to a number of initiatives targeting education, Pinchuk opened the Pinchuk Art Centre in September 2006, the only museum of contemporary art in Ukraine. The centre's website is available on http://pinchukartcentre.org/pages/russian/news.html.

37. As an example of such articles, see 'Obnyat' i ne plakat', *Korrespondent*, 23 December 2006, p. 5. Reporting on Akhmetov's $1 million donation to a Ukrainian orphanage, the article includes a large photograph portraying Akhmetov hugging and kissing some of the institution's little inmates. According to widespread rumours and press report, Akhmetov's reputation was tainted by something more than allegations of corruption. The killing and disappearance of previous owners of his companies has often been ascribed to him. See for example, 'Akhmetov idiot na Kiev', *Korrespondent*, 4 March 2006, p. 22 or the very controversial book by Sergei Kuzin, *Donetskaya Mafiya. Antologiya* (OAO Poligrafkniga: Kyiv, 2006).

38. *Ukraina TV*, Donetsk, 20 February 2006, as reported in *BBC Monitoring Service*, UK, in English, 20 February 2006.

recognition and social legitimisation, a phenomenon that Harley Balzer has called 'routinisation',[39] went hand in hand with efforts to reject all negative connotations associated with the popular idea of oligarchs.[40] In an interview to the weekly *Korrespondent* in September 2006, Surkis noted: 'We are used to say "oligarchs", but in other countries the word oligarch does not exist. Instead [expressions like] businessman, millionaire, billionaire [are used]. These are the most law-observant members of society, they pay taxes, they create employment, they create progress ...'.[41] Also, Akhmetov strongly rejected the label of oligarch: 'I am not an oligarch', he said, 'oligarchs are in government. For them being in government is the only way of making money. I can tell an oligarch from afar. (...) Oligarchs have not found their place in business and they never will. (...) In business they look like cows walking on ice. I succeeded as a businessman and made my money a long time ago'.[42]

The link between personal economic success, national responsibility and patriotism was evident in Pinchuk's line of reasoning, when he claimed that the appellations 'representative of big business' and 'national businessman' were synonymous with 'patriot'. 'The Ukrainian state owes its existence to the national business to a great extent', Pinchuk argued, as the high development rates achieved in its post-independence years and the emergence of a 'strong and united Ukraine' were twin results of national business efforts. 'If soon after independence, Ukraine had not had a young, powerful and ambitious economic force that tied itself to the national interest, its alternative history could have followed either a Central Asian or a neo-colonial path. We, the entrepreneurs (some of whom later would be called oligarchs) at once appreciated the value of independence.'[43] References to the oligarchs' alleged role in preserving the country's sovereignty, pursuing economic development, and improving Ukrainians' living standards were designed to strike a sympathetic chord among the general public, in a well-orchestrated attempt to revisit the past. Justifying the emergence of oligarchic structures as an economically rational response, a way to protect one's economic activity in an environment characterised by poor governance and weak rule of law, even the renowned Western economist Anders Aslund recognised the key role of oligarchs in establishing a virtuous circle of economic growth. Having made the shift from rent to production, the oligarchs had become, he

39. Harley Balzer, 'The Routinization of the New Russians?', *The Russian Review*, no. 62, January 2003, pp. 15-36.

40. Reflecting a commonly held view among the Ukrainian public, MP for the opposition party Bloc Yulia Tymoshenko Dmitrii Vydrin defined oligarchs as individuals who 'try to take both money and state authority under control. Therefore if there are oligarchs, there is no state authority; [as], to a certain extent they have replaced it'. Dmitrii Vydrin, 'Esli est' oligarchy, to net vlast", *Profil' Ukraina*, 12 February 2007, p. 23.

41. Aleksander Paskhover, 'Delo Pakhnet Miliardom', *Korrespondent*, no. 38, 30 September 2006, pp. 58-60.

42. *Ukraina TV*, Donetsk, 19h GMT, 20 February 2006, as reported in *BBC Monitoring Service*, UK, in English, 20 February 2006.

43. Viktor Pinchuk, 'We, the National Capitalists', *Zerkalo Nedeli on the web*, 17-23 December 2005.

concluded, the 'generators of an unprecedented boom' and had 'led to [their country's] economic recovery.'[44] However he seemed to overlook the fact that oligarchic structures had not merely reacted to the economic and political environment of the mid/late-1990s, but they had themselves contributed to shaping the general conditions of that environment. Big businessmen were, obviously, not passive victims of poor governance and weak rule of law, but, by pushing forward economic decisions that favoured their specific economic interests, they had endorsed and perpetrated economic mechanisms that were far from efficient. They had distorted competition, imposed decisions that did not necessarily reflect the interests of the general public, and failed to pay taxes. By doing so, they had depleted national resources, rather than straightforwardly fostered economic growth. Nonetheless, with a steady 7% annual growth rate and rising living standards for the first time in a generation, the Ukrainian public seemed prone to embrace Aslund's rhetoric equating oligarchs with economic development. Amid calls for the government to make use of the oligarchs' 'services and advice' by including them in a concerted effort of 'economic planning', even in Kyiv assessments made in democratic circles of the role of big business figures in society remained, at best, ambivalent.[45] Ukrainian commentators appeared torn between the urge to denounce past injustices committed by the oligarchs and gratitude towards a seemingly politically engaged entrepreneurial class, responsible for promoting the country's economic growth.

One commentator summed up this paradoxical situation as follows: 'Having got access to the shadow sphere of distribution of capital without any preliminary training these people [the oligarchs] (for the most part) grew into talented businessmen, who, in fact, made their fortunes through robbing the country and society. There are millionaires and multi-millionaires in Ukraine; now they provide workplaces for Ukrainian citizens at their enterprises. These people have also got power: the legislative, executive and presidential power. Once they had gained it, most of them turned out to be unable to formulate what the national interest is, what the state interest is and what public interest is. (...) Yet, due to the operation of their businesses and enterprises we can eat out in cafés and restaurants, we can buy apartments and high- quality locally-produced foods, we obtain quality service at dry-cleaner's and do not go around all dressed in the same clothes anymore. This country

44. Anders Aslund, 'Comparative Oligarchy: Russia, Ukraine and the United States', *CASE Centre for Social and Economic Research, Studies & Analysis* (Warsaw, April 2005). See also Anders Aslund, 'The Ancien Régime and the Oligarchs', in Anders Aslund and Michael McFaul (eds.), *Revolution in Orange: The Origins of Ukraine's Democratic Breakthrough*, (Washington, D.C.: Carnegie Endowment for International Peace, 2006), pp. 9-28.

45. Andrei Ermolaev, 'Akhmetov stroit korporativnuyu demokratiyu', *Profil' Ukraina*, 12 February 2007, p. 23.

survives in many respects due to private businesses. Yet the paradox is that it still survives despite the fact that the owners of businesses, whose goods and services we consume, are sitting in the councils and governments at all levels and are thus impeding the development of the country.'[46] From this perspective, the oligarchs' quest for social legitimisation seemed, therefore, successful. Despite evident contradictions, in terms of public opinion their reputations had been, by and large, restored as law-abiding, socially committed, patriotically-minded Ukrainian citizens.[47]

Primary consumers of globalisation. After the years of double-digit negative growth that had followed the collapse of the Soviet Union, the Ukrainian economy started experiencing a positive trend at the turn of the new millennium. A positive but ephemeral conjuncture of increased foreign demand for major Ukrainian exports, i.e. metals, chemicals and machinery (+11% nominal growth in 2006 in comparison to a 5% decline in 2005), together with rising household consumption (+18% in 2006 in comparison to 2005) was responsible for the 7.1% GDP year-on-year growth recorded in 2006. Positive indicators had been registered already in 2001 (+9.2%), 2003 (+9.6) and 2004 (+12.1%).[48]

In 2006, natural gas price hikes and political instability after the March parliamentary elections failed to impact negatively on the economy, as had in fact been expected. A joke circulated in Kyiv that the Ukrainian economy performed better when feuding political forces turned their attention away from economic planning.

Cheaper production costs (related to lower raw material prices and labour costs) had up to then proved the main source of competitive advantage for Ukrainian industry on the world markets. Significantly, the metallurgical sector, 80% of whose production was export-oriented, played a crucial role in the country's economic renaissance, accounting for 41% of its 2005 exports (see table 4 at the end of this chapter).

However, based primarily on the export of raw materials, endowed with obsolete Soviet-era technology and dependent on massive energy consumption, Ukrainian industry appeared fated to collapse if radical transformations were not introduced swiftly. That this pattern of development was unsustainable in the long term was evident to many, including big business figures, many of whom owed their own wealth to metal and metallurgy exports (see tables 2 and 3 at the end of this chapter).

46. Yulia Mostovaya, 'Self-destruction Strategy', *Zerkalo Nedeli on the Web*, no 39, 14-20 October 2006.

47. Comments of a Ukrainian weekly on oligarchs' charity efforts in support of a children's hospital provide another interesting example of this trend. 'We will remain suspicious still for a long time about the big money of those who organised financial pyramids in the early 1990s, speculated on compensation certificates in the mid-1990s, [took advantage of] an unprecedented wave of shadow privatisations at the beginning of the 2000s. But when with their money, these people help children's lives, everything else becomes of secondary importance'. 'Legalizatsiya', *Vlast' Den'g*, no.51-52, 2006, p. 3.

48. IMF data on GDP growth available on http://www.imf.org/external/data.htm; for sectoral data, see for example Dragon Capital, Macro Research, 2006 Overview, unpublished paper.

In addition to the unstable perspectives of long-term growth, the oligarchs' wealth risked being adversely affected also by different conditions in relation to ownership distribution. After a phase of capital primary accumulation during the Kuchma years, the Ukrainian private sector was, in the aftermath of the Orange Revolution, essentially formed. Having seen the Orange leadership abdicate from any attempt at property redistribution and with all major privatisation opportunities exhausted, oligarchs were now fighting over the ownership of individual plants, either in court or through hostile takeovers.

With the dizzy business opportunities of the 1990s rapidly fading and the clear understanding that the legendary 700-800% annual revenues allowed by the unregulated and corrupt post-Soviet environment could no longer be replicated, leading business representatives inaugurated a two-pronged expansion strategy. They moved firstly towards the acquisition of assets abroad and, secondly, towards the capitalisation of their companies on international stock markets as channels through which to transform what economists defined as their companies' 'quality of growth.'[49]

Experts were indeed advising that, in order to maintain the economy's positive results, a shift had to take place from an extensive to an intensive model of development, i.e. from a model based on the exploitation of natural resources, to a model where technology and capital investment would lead to the production of added value goods; in other words, 'from a Soviet to a European model of development.'[50]

First among the leading Ukrainian business representatives, Rinat Akhmetov had had his eyes riveted on the global financial markets even before the Orange Revolution. In an attempt to increase shareholder value and market capitalisation, his companies had been gradually introducing international accounting standards. Foreign managers had been hired. Improving on transparency and corporate governance had become System Capital Management's (SCM) stated objectives within a wider perspective aiming at creating 'the most effective management structure for our business.' SCM representatives were confident that the group would be listed on foreign stock exchanges within one year.[51] International capital markets were increasingly seen by a number of Ukrainian companies as the main source of finance for the gradual *perestroika* they had already started. Transparency and

49. Author's interview, Kyiv, 16 February 2007.

50. Author's interview, Kyiv, 14 February 2007.

51. Roman Olearchyk, 'Ukrainian Billionnaire Oligarchs Eager to Westernise', *Financial Times*, 31 October 2006.

international credibility were seen as vital for this purpose. In a *Financial Times* interview, *Finansy i Kredit* owner Kostyantin Zhevago explained: 'Our goal is to look like any other company listed in the US or the UK. We understand we need to move fast and efficiently to remain competitive.'[52] A number of medium-sized companies had already listed shares on the London Stock Exchange, while other large companies had established a partnership with international financial organisations, like the EBRD and the Japanese Bank for International Co-operation, willing to fund their modernisation efforts.[53] Acquisition of assets on foreign markets was the other element in the oligarchs' expansion strategy. Because of its growing engagement on the European markets, the Industrial Union of Donbass (IUD) was seen by some as the most powerful 'agent for Europeanisation' within Ukrainian economic and political circles.[54] After its $468 million acquisition of the Huta Czestochova steel mill in Poland, in 2007 IUD was preparing to participate in a bid for the privatisation of the Polish state energy company Elsen, originally part of the Huta Czestochova group.[55] IUD Polish subsidiary, IUD Polska also revealed plans to acquire majority shares in the state-owned Gdansk Shipyards (3,000 employers) and Gdynia Shipyards (6,000 employees). While negotiations were still ongoing, IUD was viewed by its Polish counterparts as the most promising investor, given the Ukrainian group's capacity to secure stable rolled steel provisions from its Huta Czestochova mill.[56] IUD also had interests in Hungary, where it had acquired the Dunaferr mill.[57] Ukrainian companies abroad also proved active in the banking sector. In 2007, the Privat group opened a branch of its Privatbank in Lisbon, to service the large Ukrainian immigrant community in Portugal.[58] A number of Ukrainian banks had also opened their representative offices abroad (rather than fully-fledged branches, a more complex administrative operation): VABank and Nadra in Budapest, Ukreximbank in New York and London, Forum in Prague, First Ukrainian International Bank in London and Moscow.[59]

Although strongly motivated by ambitious plans for business expansion, Ukrainian oligarchs' quest for Western markets was not prompted by exclusively economic reasons. Opening up Ukraine to the international community was an integral part of the oligarchs' efforts to acquire social legitimisation and business consolidation, as they needed, in the cynical words of a Ukrainian

52. Ibid.

53. In February 2007, the Industrial Union of Donbass obtained credits for $150 million from the EBRD and $120 million from the Japanese Bank for International Co-operation for the upgrading of its Alchevsky metal plant. *Ukrainska Pravda website*, 2 February 2007.

54. Author's interview, Kyiv, 15 February 2007. With one of its co-presidents sitting in the chair of Head of the Security and Defence Council (Vitalii Haiduk) and one of its previous advisors working as Deputy Head of President Yushchenko's Secretariat, IUD was well placed to enhance its agenda of Europeanisation, see page 65.

55. http://gazeta.delo.ua/?date=2007-02-05&id=18756

56. *Kyiv Post*, 25 January 2007, pp. 1 and 8.

57. IUD was not the only Ukrainian company active on the European markets. After buying the controlling shares in a leading Polish car manufacturer in 2005, in 2007 Ukravto Corporation, owner of the major Ukrainian car plant, ZAZ, and producer of economy-class, Ukrainian-designed cars like Tavria and Slavuta, participated in the bid for the privatisation of Daewoo Automobile Romania. *Kyiv Post*, 25 January 2007, pp. 1 and 8.

58. See: http://gazeta.deloua/?date=2007-01-23&id=16778.

59. Ibid.

commentator, a 'global environment' on which to spend the money they had earned in the previous decade.[60] Promoting Ukraine's membership in the EU and widening Ukraine's investment opportunities on the world market became intertwined (although not unanimously advocated) themes in the discourse of big business representatives.

Viktor Pinchuk's creation, the Yalta European Strategy (YES), proved an important instrument in an approach that YES Director Inna Pidluska defined as 'soft integration.'[61] Employing culture as the medium to create a more favourable environment for Ukraine's integration into the EU, Pinchuk's foundation focused on raising Ukraine's profile, both among the EU general public and the EU political and economic elites. A 2005 YES-promoted survey branded Ukraine 'number one favourite candidate to accession in all European countries'. With as many as 51% of the Europeans interviewed in the poll declaring themselves to be in favour of Ukraine joining the European Union, the message sent by the YES leadership was that the idea of Ukraine as a potential member of the EU was becoming increasingly entrenched within the EU public. Any opposition raised by EU policy-makers amounted, therefore, to political speculation and did not reflect the majority will of the European people.[62] In its Agenda 2020, YES called unequivocally for Ukraine's membership in the EU by 2020. The document stated: 'Ukraine's future lies firmly in the European Union. The country's tradition has been a profoundly European one. Its history is rich on the one hand and difficult on the other. The people of Ukraine cannot be held to account for everything they had to endure in the past. All the more reason for Europe to respect and honour the achievements of the Ukrainian people. Their aspirations should be treated as a voice in favour of a stronger and more active European Union'.[63] More YES initiatives targeted political and economic decision-making circles. Since the appearance of the newly elected President Yushchenko at the 2005 Davos World Economic Forum, Ukraine-related events have become something of a tradition at the Swiss resort, serving to promote Ukraine's image and attract world leaders' attention to issues important for the country's development. In 2007, Pinchuk treated the more than 300 prestigious guests who attended the YES-sponsored luncheon-conference 'Where is Ukraine Heading?' to Ukrainian traditional dishes like borsch and cherry dumplings. During the event, to an audience includ-

60. Author's interview, Kyiv, 13 February 2007.

61. Author's interview, Kyiv, 8 February 2007.

62. Details of the survey are available on the YES webpage. See: http://www.yes-ukraine.org/en/survey/november.html.

63. For the full text of Agenda 2020, see http://www.yes-ukraine.org/en/survey/agenda_2020.html.

ing Latvian President Vaira Vike-Freiberga, EU Enlargement Commissioner Olli Rehn and former Polish President Alexander Kwasniewski, Prime Minister Yanukovich admitted: 'The modernisation of the Ukrainian economy is impossible without its integration into the world economic system.'[64]

Because of their increasing attraction towards the international arena and their interest in seeing Ukraine as a fully-fledged member of the international community, oligarchs came to be seen as 'primary consumers of globalisation', the most powerful force capable of propelling Ukraine onto the world scene.[65]

The idea of Europe. The growing drive towards Western markets and international trade institutions was not, however, a unanimous and generalised tendency among Ukrainian businesses. Stereotypes and prejudices regarding trade relations with the West and with Russia still prevailed. This was especially true in a situation in which entire industrial sectors were surviving thanks to generous government handouts and felt, therefore, too vulnerable to face international competition.

Research conducted by a Ukrainian think tank highlighted misgivings and conflicting attitudes among different business sectors as regards support for Ukrainian bid for membership of the WTO and prospects for a still-to-come Free Trade Area with the EU. Well aware that formal membership of trading organisations would bring down quotas for Ukrainian products and thus enhance their industrial potential, sectors drawing heavily on export, like metallurgy or chemicals, lobbied actively for Ukraine's integration into the world markets.[66]

At the other end of the spectrum, however, the need to at best reform and at worst abolish the system of state subsidies, as a precondition to WTO and EU membership, coupled with the expected requirement that Ukraine adopt costly EU and international standards, provoked substantial concern within the least technologically advanced sectors (i.e. agriculture, transport, some companies engaged in machine building). Protectionism designed to keep potentially powerful foreign competitors out of the Ukrainian markets appeared as an attractive life-saving option also for sectors that were going through a phase of consolidation (i.e. banking and finance).[67]

In business circles, the idea of Europe was, however, generally positively received. The EU was associated with increased effi-

64. Mikola. Siruk, 'Promoting The Ukrainian Way', *The Day Weekly Digest*, no. 3, 30 January 2007.

65. Andrei Ermolaev, op. cit. in note 45.

66. Rumours circulated in Kyiv that Pinchuk was sponsoring the activity of a law firm supporting Ukraine's bid into the WTO. Author's interview, 6 November 2006.

67. The Ukrainian version of the research paper coordinated by Olha Shumylo is available at: http://www.icps.com.ua/doc/FTA_Impact_U.pdf.

ciency, more advanced technology and higher legal and production standards. 'It is better to make your money with the Russians and to protect it with the Europeans', an oligarch was anecdotally quoted as saying.[68] As an economic commentator put it, the question both for the political and the economic elite was no longer 'where to go?' but 'how to get there?'.[69]

The EU was seen as offering potentially vast opportunities, but with no clear membership or association perspective in sight, Brussels appeared as a distant dream. Ukrainian analysts saw the government's efforts to keep the question of bilateral relations high on the EU agenda as unilateral ('You look like an idiot if you try to "approximate" with somebody who does not want to be "approximated" with you', one bitterly concluded) and were concerned that EU internal protectionism would either hamper trade opportunities for Ukrainian business or relegate Ukrainian companies to the subordinate role of subcontractors on the European markets.[70]

Although positive, the idea of Europe was also a rather indistinct one. The political elite had emphatically embraced a pro-European rhetoric, but observers doubted that they fully understood and were ready to implement the obligations deriving from a closer association with the EU. Many were convinced that political statements served exclusively a short-term opportunistic purpose and would be unlikely to go beyond a declaratory stage. 'Fantasy' and 'illusion' were the words most commonly used by Ukrainian commentators when referring to their government's promises to work towards the introduction of European standards in Ukraine.[71] EU officials characterised the Ukrainian elite's attitude towards EU integration as aimed at getting the 'best of both worlds', selectively emphasising their rights to trade preferences, while overlooking their commitments towards the consolidation of democratic practices and rule of law.[72]

Also in business terms, there was some concern that the introduction of costly European standards (for example as far as employees' social security was concerned) would require radical transformations in the ordinary practices of many Ukrainian enterprises, thus running the risk of undermining their exports' competitively low prices.[73]

While striving towards an ideal that they could possibly not afford, did not fully understand and of the value of whose imple-

68. Author's interview, Kyiv, 4 October 2006.

69. Author's interview, Kyiv, 14 February 2007.

70. Author's interview, Kyiv, 14 February 2007.

71. Several interviews, Kyiv, February 2007.

72. Author's interview, Kyiv, 7 March 2007.

73. Author's interview, Kyiv, 13 February 2007.

mentation they were not entirely convinced, the Ukrainian elite was affected by what an opposition MP defined as 'political schizophrenia': 'They aspire towards EU standards, but they still live in an Asian satrapy'.[74]

Interestingly, the whole issue of NATO accession had been kept skilfully dormant in the pro-Western rhetoric of Ukrainian oligarchs. Aware that any reference to the North-Atlantic alliance might provoke negative reactions among a more naturally Russian-leaning public in the Eastern regions, business representatives appeared particularly careful to avoid this slippery slope. At the political level, since his appointment and most likely following Russian advice, Prime Minister Yanukovich had successfully decoupled the issue of NATO membership from EU integration. Soviet stereotypes regarding NATO still prevailed in Ukraine and the Ukrainian public had consistently expressed their opposition to possible membership. According to a December 2006 survey, 45% of Ukrainians were categorically against membership, with opposition characteristically concentrated in the Russian-speaking Crimea and Donetsk regions (74.4%).[75]

Russia's shadow

If the EU was a remote dream, Russia was, in stark contrast, an immediate, short-term reality. Still the number one trading partner for Ukraine (see table 5 at the end of this chapter), Russia represented an important point of reference also in terms of business perspectives. In their strategy of expansion, Ukrainian companies showed that they were ready to seize any opportunity at hand, willing to move, as one Ukrainian economist put it, 'everywhere markets are.'[76]

In February 2007, news circulated of a merger between Serhii Taruta's IUD and the Russian Metalloinvest, owned by Alisher Usman. With a capitalisation of about $20 billion, the project would create one of the largest and most competitive steel groups in the world, producing an estimated 20 million tons a year. The 2005 merger of Mittal and Arcelor, which together controlled 10% of the world steel market, had convinced Russian and Ukrainian producers that joining forces would be the only way to stave off foreign competition and strengthen their already significant presence on the world markets. As a result of the merger, branded the 'marriage of oligarchs' by the Ukrainian press, the

74. Author's interview, Kyiv, 15 February 2007.

75. *Den'*, 6 February 2007.

76. Author's interview, Kyiv, 8 February 2007.

Ukrainians would gain access to cheap raw materials, while the Russians would gain privileged access to European markets, through IUD's Polish and Hungarian subsidiaries. IUD had been locked for some time in disputes with its Ukrainian competitors over the prices of raw materials, finally resulting in IUD buying cheaper metal from Brazil rather than from neighbouring Ukrainian companies. The operation with Metalloinvest would solve IUD's problems of supply, but, at the same time, it would bring Usman's long-term ambition to establish 'an Eurasian group joining together the largest metal producers in Ukraine, Russia and Kazakhstan' one step closer.[77] For Ukrainian companies, doing business with Russia was an easy option. Geographical proximity, the use of Russian as the region's *lingua franca*, a common historical past and shared economic habits established during the Soviet period made this relationship comfortable; 'like doing business with your brother', as one Ukrainian analyst summarised it.[78] However, similar foreign trade structures and overlapping industrial potential made Russia and Ukraine more likely competitors than allies on the world markets (significantly, Russian metallurgy was also heavily export-oriented).

Russian industry's reliance on obsolete technology and the relatively wide availability of raw materials promised Ukrainian business a temporary respite against the urgency of industrial restructuring. However, failing to produce state-of-the-art-technology, the Russian model of extensive economic development provided no incentive or instruments for Ukraine to catch up with the ongoing world-wide technological revolution.[79] Vague possibilities of largely profitable but unclearly regulated business deals (especially projects of co-operation for the exploitation and commercialisation of energy resources from the Far East of Russia) appeared as the swan song of post-Soviet 'wild capitalism', a style of doing business that, Ukrainians realised, would disappear in a structured and regulated economic environment.

In Kyiv, the feeling was widespread that, apart from these sorts of deals and a vast consumer market for Ukrainian agricultural products, Russia had little to offer: the type of cooperation it proposed had a temporary rather than long-lasting character and above all it was clear that whatever it was prepared to trade would involve a political price.

With estimated capital resources several times greater than that of the Ukrainian oligarchs, the presence of Russian business

77. Aleksander Paskhover, 'Svadba Oligarkhov', *Korrespondent*, 24 February 2007, pp. 18-22.

78. Author's interview, Kyiv, 14 February 2007.

79. For an opposing view, pointing at information technology as one of the core factors in Russia' economic growth see Andrei P. Tsygankov, 'Projecting Confidence, not Fear: Russia's Post-Imperial Assertiveness', *Orbis*, Fall 2006, pp. 667-90.

in Ukraine was perceived as a real threat to Ukrainian companies, because of their aggressiveness and rapaciousness, determination and capability to seize control of the most attractive Ukrainian assets.[80] Ukraine's energy pipelines, for example, had constantly been coveted by Russia since the collapse of the Soviet Union. Fearing that losing control over some of the country's strategic assets would endanger Ukraine's security and sovereignty, Ukrainian nationalists had rejected several attempts made with the Kremlin's political support and the connivance of some Ukrainian political and economic forces to establish a joint Russian-Ukrainian consortium to oversee the management of the pipeline network.[81]

In addition to Russian companies, Ukrainians were concerned about the Russian authorities' direct management and political use of economic affairs.[82] Moscow's wrangling even with faithful Belarus over gas prices had dispelled illusions that political loyalty would be rewarded with preferential energy rates. On the contrary, with a Russian ban on Ukrainian agricultural products pending and an attempted moratorium on the import of Ukrainian pipes (unsuitable for import because allegedly containing radioactive material, when the metal used for its production was in fact imported from Russia), Ukrainians experienced at first hand Moscow's tendency to use trade wars as an instrument of political pressure.[83]

Through economic leverage on so many different levels, Moscow had been striving to keep Kyiv in its political orbit, preventing it from shifting West through earlier accession to membership of the WTO, tighter association with the EU (even in the form of a free trade area) or even NATO accession. Co-operation within the four-sided Single Economic Space (SES), comprising Russia, Ukraine, Belarus and Kazakhstan, had been presented as an alternative to other international forms of economic co-operation.

Since the Kuchma years, Ukrainian political elites had skilfully played the perspective of SES membership as a way to secure Russian political support. While pledging loyalty towards the organisation, they had in fact systematically obstructed the practical implementation of agreements that, it was felt, risked diminishing Ukraine's sovereignty. By applying this ambiguous approach, Ukraine had undermined effective establishment of the SES, thus performing what a Ukrainian MP called a *tikhii sabotazh* (quiet sabotage).[84]

80. According to the paper *Finansy*, the richest man in Ukraine, Rinat Akhmetov, was three times poorer than the richest man in Russia, Oleg Daripaska: http://gazeta.delo.ua/?date=2007-02-13&id=20024. Russian corporations are world class in terms of size; in several industries, including energy metals and chemicals, Russian companies compete for places in the world top 10.

81. On the latest scandal on a possible Ukrainian-Russian energy consortium and consequent last-minute legislation to prevent strategic assets to be sold off to Russia without consent of the main political institutions, see Andrei Eremenko, 'Zakon 'O Trube': kak zalatats' dyry', *Zerkalo Nedeli on the web*, no. 5, 10-16 February 2007.

82. Reversing this argument, Dimitrii Trenin argues interestingly that Russian foreign policy decisions are instead dictated by private and corporate decisions. Dimitrii Trenin, 'Russia Redefines Itself and its Relations with the West', *The Washington Quarterly*, Spring 2007, 30:2, pp 95-105. Daniel Treisman has forged the expression 'silovarchs' to characterise a new business elite emerged from the network of security services and law enforcement veterans (the so-called *siloviky*) during the Putin years. Daniel. Treisman, 'Putin's Silovarchs', *Orbis*, Winter 2007, pp. 141-53.

83. For more details on the pipelines moratorium, see Katerina Panova and Andrei Smirnov, 'Zheleznaya khvatka', *Korrespondent*, 22 June 2006, pp. 36-37.

84. Although counterintuitive, given President Kuchma's vocal support for SES and his enthusiastic signature of the SES founding agreement in the autumn 2003, this interpretation is widespread in Kyiv political circles. A demonstration of its credibility lies in the fact that, despite Russian attempts to depict the SES as an emerging EU-like structure, very little of what has been proposed has actually been translated into agreements and very little of what is contained in those agreements has been eventually implemented. Author's interviews, Kyiv, 15 February 2007.

The Ukrainian position that integration in the SES would follow, not precede, the creation of a Free Trade Area with the EU and would not go as far as the establishment of a customs union was dictated by two important considerations, significantly shared both within Ukrainian political and economic circles, including that of Prime Minister Yanukovich.[85] Firstly, that a free trade area between Russia and Ukraine already existed on paper, but its practical functioning had thus far been obstructed by Russia's political use of trade disputes. Secondly, that setting up a customs union with Russia, Belarus and Kazakhstan would prevent the establishment of a customs union with the EU, which required trade concessions to be negotiated individually with single countries rather than the whole bloc.[86] Seen more as a political than as an economic project, the SES had failed to capture the economic elite's imagination.

On this complex chessboard of intertwining economic and political interests, the Ukrainian oligarchs played an ambivalent game. A journalist who interviewed several big business figures characterised them as 'split personalities', looking East or West, speaking Russian or English, acting aggressively or amiably according to the business opportunities they had set their eyes on.[87]

Inclined to grab any possible short-term benefit deriving from the legendary economic deals the Russians could propose, most of them were, however, aware of the potential political costs that this closer interaction might involve. They were thus set to prevent Russians from irreversibly penetrating the fabric of the Ukrainian economy. Fearing but admiring their Russian counterparts, Ukrainian oligarchs thought they could outwit them or come to an agreement with them to extract the best possible deals for their own companies. Rinat Akhmetov's unconfirmed energy arrangement with Gazprom for the provision of 2 billion cubic metres of gas over a 5-year period at privately negotiated prices vividly illustrates this attitude.[88]

However, as close as they were and attracted as they might have felt towards Russian business, they were particularly wary of the risks that a closer interaction with Moscow might involve. If in the years following the end of the Soviet Union the Ukrainian economic elite might have perceived itself as naturally inclined towards Russia, in 2007 Ukrainian oligarchs' absolute priority was to preserve their independence while, at a the same time, enhancing their business profits. Confident that in Brussels'

85. Although confirmed by Prime Minister Yanukovich during his visit to Brussels in September 2006, the position found some considerable opposition within the government, for example by Deputy Prime Minister Azarov. Author's interview, Kyiv, 15 February 2007.

86. European Commission, 'Reactions to Draft Agreement establishing a Single Economic Space by Russia, Ukraine, Belarus and Kazakhstan', Information to the Press circulated by the Delegation of the European Commission to Ukraine on 17 September 2003.

87. Author's interview, 6 November 2006.

88. In early 2007, Metinvest, part of the SCM group, was granted a licence allowing it direct access to foreign energy markets. The licence gave Metinvest the possibility to buy 2 billion cubic metres of gas for a 5 year period at a set price, on either the Ukrainian or foreign markets, by-passing the intermediation of the highly contested Swiss-registered Rosukrenergo. Metinvest would then distribute the Russian gas to other SCM companies. The Ukrainian media speculated that 500 such licences had already been awarded, but besides Akhmetov's SCM, no company had the political weight to hold direct negotiations with Gazprom and the Kremlin to make the licence effective. Aleksander Paskhover and Andrei. Smirnov, 'Pryamo v gaz, Korrespondent, 16 September 2006, pp. 22-24.

rather than Moscow's shadow they would be in a better position to maintain control over their country's economic wealth and promote their companies' growth, they became, in the words of a Ukrainian commentator, 'instinctively European.'[89] As an MP concluded, the EU offered them a 'better *krysha*' (roof or protection) than Russia.[90]

Conclusion

The Orange Revolution and its aftermath have produced a sea-change in the oligarchs' perception of time and space. Up until the end of the Kuchma presidency, the 2004 presidential elections represented their 'end of history' timeframe, marking the potential loss of their power and property. Yet, elections came and went and the oligarchs realised that, having survived the stormy days of the leadership change, their empires were there to stay and they themselves had a personal stake in the future of Ukraine.

During the Kuchma years, precariousness had been the name of the game, and exporting capital abroad the instinctive reaction to domestic instability. However, in a situation in which their ownership rights became recognised, oligarchs started to connect their personal success to their own country's success, aware that Ukraine's rating on the international markets would clearly affect the value of their own assets. For the first time since independence, the oligarchs' pragmatic and individual interests thus came to coincide with their country's interests.

In this perspective and against the background of a generally unstable and rhetoric-prone domestic political environment, Ukrainian big businessmen came to play a pivotal role in promoting their country's integration into the international community and adoption of international standards. The intrinsically selfish objectives of increasing their own assets' value at home while expanding their business opportunities abroad came to serve as a powerful catalyst in a situation characterised by a lack of concrete membership perspectives emanating from the EU side and weak political will on the side of the Ukrainian leadership.

Operating as a bridge over the gap created by political constraints, oligarchs could thus provide a valuable contribution in a medium-term process, leading Ukraine towards economic devel-

89. Author's interview, Kyiv, 15 February 2007.

90. Ibid.

opment, technological modernisation, improved living standards for the population and consolidated democratic practices.

However, two important issues remain to be addressed in this seemingly optimistic scenario. Firstly, the economic elite in Ukraine (and especially its top ranks, i.e. the oligarchs) are not a cohesive group. Active support for integration in the international community is not generalised within business circles and individual interests still prevail.

Not only mistrust and apprehension of the world market, but the specific preferences of big businessmen who are close to or form part of the country's political leadership (both within Prime Minister Yanukovich's and President Yushchenko's circles) might derail western-oriented efforts to the advantage of tighter bonds with Russia. As long as Russia views Ukraine as the main battlefield in its zero-sum geostrategic game with the West, Ukrainian business representatives are likely to become Russia's willing instruments in this confrontation. The murky deals concluded around energy issues with Russia are a clear illustration of this risk.

Moreover, the oligarchs' drive towards Western business standards is not an automatic guarantee of their democratic credentials. Business figures like Viktor Pinchuk and Rinat Akhmetov clearly enjoy wider international exposure than a number of top-ranking political figures. As a result, they are set to become the main instigators in the adoption of internationally-accepted business practices. However, the question as to whether they could also serve as instruments for the consolidation of political democracy in Ukraine rests on a knife edge.

International experience also in the so-called second and third waves of democratisations in Latin America and Southern Europe in the 1970s and 1980s testifies to the important role played by some of these countries' economic elites in the processes of political transition from authoritarian to democratic regimes.[91] However, examples also abound of countries characterised by positive economic growth, a stable political and economic environment, with oligarchs in power and no substantial democracy – Russia under Putin being one of them. In other words, striving towards economic growth does not necessarily result in a transition towards fully democratic institutions.[92]

From this point of view, it is legitimate to wonder whether the continued presence and influence of the oligarchs in the Ukrainian political system might be conducive to a return to forms of

what Celeste Wallander defines as 'patrimonial authoritarianism'.[93] During his first year in office, Prime Minister Yanukovich has demonstrated a remarkable tendency to secure tight control over all structures of power, reducing other institutions (like the Presidency) to almost political irrelevance.

The influence of big business representatives on this process has appeared scattered and ambiguous, pointing to business leaders' concern that instability might undermine the 'country's image on the international scene' and economic growth.[94] However, while oligarchs have appeared to be more inclined towards forms of corporative democracy, where risks of instability and political challenges are effectively minimised, they have also demonstrated their determination to keep in check the state's role in the management of the economy.[95] This has helped guarantee a degree of economic pluralism and independence of the economic spheres *vis-à-vis* political decision-making and has precluded possibilities for the creation of a Putin-like political system in Ukraine.

Undeniably, the central question in political-business relations in Ukraine remains the need to restore a degree of 'normality' in the balance of power between the two spheres of interests; in other words, the need to create a situation within which economic representatives lobby for their own sectoral and individual interests through transparent and institutionalised mechanisms rather than impose backstage decisions that risk having an adverse effect on the interests of society at large.

The international community, primarily the EU and Ukraine's individual partner countries, already provide important support in this direction through mechanisms aimed at helping introduce and consolidate democratic governance and internationally-accepted business practices (e.g. the EU ENP Action Plan). However, increased efforts by the international community towards liberal engagement with business circles in Ukraine, exposing members of the economic elite to what Celeste Wallander calls 'the liberalising effects of marketisation, competition and diversification of interests and social power' may contribute to this process towards 'normality'.[96]

91. See, for example Guillermo O'Donnell et al. (eds.), 'Entrepreneurs and the Transition Process: The Brazilian Case', in *Transitions from Authoritarian Rule. Comparative Perspectives* (Baltimore: The Johns Hopkins University Press, 1986) pp. 137-53.

92. I am grateful to Olga Savarin for this consideration.

93. Illustrating the Russian model, Celeste Wallander describes patrimonial authoritarianism as 'a political system based on holding power in order to create access and distribute rents'. Celeste Wallander, 'Russian Transimperialism and Its Implications', op. cit.in note 5, p. 116.

94. Rinat Akhmetov, quoted on *Ukrainska Pravda website*, 3 April 2007.

95. Andrei Ermolaev, op. cit. in note 45.

96. Celeste Wallander, 'Russian Transimperialism and Its Implications', op. cit. in note 5, p. 118.

Table 1:
Main business affiliations within the parliamentary factions in the Verkhovna Rada elected in March 2006

Party	Main figure	Holding/major company	Sectors	Main political/business connections
PARTY OF REGIONS	Rinat Akhmetov	System Capital Management (90% of shares belonging to Akhmetov, 10% to his wife), market value $12.144 billion	Industry and metallurgy (steel)	Allegedly the main financial supporter of Yanukovich's 2006 presidential campaign. One of the 4 leading figures in the party, Boris Kolesnikov (MP and former head of Donetsk regional Council) and Vladimir Kozak (head of Ukrainian Railways) are considered among his closest allies in Parliament
	Viktor Yanukovich jr, Taras Chornovil, Raisa Bohatyreva	No major business companies, but control over a number of local enterprises	Banking, media, energy	Proximity to PM Yanukovich is considered the group's primary asset
	Andrei Kluyev (DPM in charge of energy issues) and Sergei Kluyev	Ukrpodshipnik	Light metallurgy	Efim Zvyagil'skii (former PM and current MP); Vladimir Rybak (DPM), Vladimir Logvinenko (Donetsk regional governor)
BLOC YULIA TYMOSHENKO	Yulia Tymoshenko	Personal wealth estimated in the region of $1 billion	Energy (oil and gas), connections with gas dealers; agriculture	Kolomoitskii of the group Privat is rumoured to have sponsored her campaign
	Buryak brothers and Kostantin Zhevago	The Buryaks own Brokbusiness bank, Zhevago owns the group 'Finansy i kredit'	Banking and metallurgy	Some connections with Akhmetov
	Aleksander Edin	Monopolist in rail transportation (estimated 70% of all rail transit in Ukraine)	Transport	Connected with the circle of previous transport minister Kirpa
	Teriela Vakadze	Ukravto, AvtoZAZ	Car industry	
	Iosif Vinsky	Personal wealth estimated at $200 million		Previous member of the Socialist Party, allegedly used to control all the party's financial flows
	Bohdan Hubskii		Food industry	Edina Ukraina founding member

Source: 'Dengi Dvigatel' Politiki', material published by the Kyiv Gorshenin Institute of Management and the International Institute of Political Expertise in Moscow on 2 February 2007. Available at: http://www.kipu.com.ua/Articles/2007.02/23_money.html.

Table 2:

The 15 richest Ukrainians

Ranking	Name	Main Business	Value
1	RINAT AKMETOV	Energy, food & beverage industry, machine building, metallurgy and coal industries, sports and telecommunications	$11.8 billion
2	VIKTOR PINCHUK	Media, pipe manufacturing	$3.7 billion
3	IHOR KOLOMOJSKY	Banking, ferroalloy and ore industry, oil production and refining	$2.8 billion
4	HENNADY BOGOLUBOV	Banking, ferroalloy and ore industry, oil production and refining	$2.4 billion
5	KONSTANTIN ZHEVAGO	Banking, iron ore industry, truck manufacturing	$1.9 billion
6	SERHIY TARUTA	Metallurgical industry	$1.7 billion
7	VITALIY HAYDUK	Metallurgical industry	$1.7 billion
8	DMYTRO FIRTASH	Natural gas production, transportation, chemical industry	$1.4 billion
9	OLEKSIY MARTYNOV	Banking, ferroalloy and ore industry, oil production and refining	$1.4 billion
10	VALERIY KHOROSHKOVSKY	Media, metallurgy	$930 million
11	VOLODYMYR MATVIENKO	Banking $890 million	
12	VASYL KHMELNYTSKY	Financial services, utilities, real estate	$729 million
13	OLEKSANDR YAROSLAVSKY	Banking, chemical industry	$709 million
14	VIKTOR NUSENKIS	Energy, metallurgical and coal industry	$691 million
15	PETRO POROSHENKO	Confectionary, automobile industry, beverages	$505 million

Source: *Kyiv Post*, Special Insert, 29 June 2006.

Table 3:

The Forbes Magazine's 7 world-ranking Ukrainian billionaires

World Ranking	Name	Estimated Wealth (in bn $)	Sector	Political Connections
214	Rinat Akhmetov	4	Metallurgy, primarily steel	MP for the Party of Regions, one of the 4 leading figures in the party
323	Viktor Pinchuk	2.8	Metallurgy	Son-in-law of former President Kuchma
488	Serhii Taruta	2	Metallurgy	Former Deputy Chairman of his Industrial Union of Donbass, Oleksander Chaly is Deputy Head of President Yushchenko's Secretariat
488	Vitalii Haiduk	2	Metallurgy	Co-owner of Industrial Union of Donbass, he was from Sept 2006 to May 2007 Head of the President Yushchenko-appointed Security and Defence Council
788	Ihor Kolomoysky	1.2	Banking	Rumoured to have financed Yulia Tymoshenko's campaign, allegedly close also to Nasha Ukraina
799	Hennadii Boholyubov	1.2	Banking	Co-owner of Kolomoisky's group 'Privat'
891	Kostyantin Zhevago	1	Banking	MP for the Bloc of Yulia Tymoshenko

Source: Forbes, *The World's Billionnaires*, published on 8 March 2007, available at http://www.forbes.com/lists/2007/10/07billionaires_The-Worlds-Billionaires_CountryOfCitizen_20.html.

Table 4:

Ukrainian foreign trade in 2005 by product % of total

Export		Import	
Metals and metallurgy	41	**Minerals**	32
Minerals	13.7	**Machinery**	17.6
Chemicals	8.7	**Transport**	8.9
Machinery	8.3	**Chemicals**	8.6
Agricultural products	5	**Metals and metallurgy**	6.8
Transport	4.8	**Plastic and plastic products**	5.4
Foodstuffs	3.8	**Foodstuffs**	4
Live animals and deriving products	2.1	**Textiles**	3.9
Other	12.6	**Other**	12.8

Source: *Korrespondent*, 18 March 2006, p. 39, quoting Ukrainian State Statistics Department Data.

Table 5:

Ukrainian foreign trade in 2005 by geographical distribution % of total

Export		Import	
Russia	21.9	**Russia**	35.5
Turkey	5.9	**Germany**	9.4
Italy	5.5	**Turkmenistan**	7.4
Germany	3.8	**China**	6
Poland	2,9	**Poland**	3.9
USA	2.8	**Italy**	2.9
Belarus	2.6	**Belarus**	2.6
Egypt	2.3	**France**	2.2
Others	52.3	**Others**	31.1

Source: *Korrespondent*, 18 March 2006, p. 40, quoting Ukrainian State Statistics Department Data.

Ukraine and its relations with the EU in the context of the European Neighbourhood Policy

Kataryna Wolczuk

3

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Introduction

The launch of the European Neighbourhood Policy (ENP) coincided with the Orange Revolution in Ukraine. This conjuncture of events accounts for what has amounted to a fundamental shift in Ukraine's policy towards the EU. Until 2004, relations with the EU were largely perceived as belonging to the domain of foreign policy and were regarded as of little relevance to domestic politics and policy-making. Since 2005, however, 'European integration' has become a matter of domestic policy-making.

It is thanks to the ENP that the EU stepped in to provide a more detailed and explicit blueprint for the Ukrainian authorities in the form of the Action Plan (AP). This guidance fell on more fertile ground than under the Kuchma regime (1994-2004). The rise to power of new elites with a greater commitment to Europe in the aftermath of the Orange Revolution led to a swift 'domestication' of the EU-defined reform agenda. For the first time, Ukrainian reform policy followed the guidance of the EU.

Having said that, the actual impact of the AP on domestic change has been relatively limited. The reforms envisaged in the AP pose a formidable challenge for a country that has seen its state institutions and public standards deteriorate in the decade and a half since the collapse of the USSR. Democratic achievements resulting from the Orange Revolution need to be consolidated into the 'root-and-branch' reform of the state itself. And yet, even if the Orange Revolution of late 2004 brought fresh winds of change, serious efforts at introducing reform foundered almost immediately in the atmosphere of intensified political rivalry and heightened political instability in Ukraine.

This has had a profound impact on the implementation of EU conditionality. Overall ENP has failed to mobilise politicians. *Evrointegratsia* (European Integration) has remained an abstract

and distant prospect for many of them, and as such incapable of overriding short-term domestic considerations. Without clear political leadership on European issues and an effective coordinating mechanism within the government, the implementation of the AP was effectively conducted by, and left to the discretion of, middle-level bureaucrats (civil servants).[1]

Making European integration a pivot of domestic reforms in Ukraine is hampered by antipathy towards the ENP, at least among those in Ukraine who actually know anything about it. It is the absence of the membership perspective that fundamentally weakens the ENP's attractiveness in the eyes of pro-European Ukrainians. This is because the Ukrainian authorities under Kuchma turned the prospect of membership into a real litmus test of EU's genuine interest in Ukraine, and thereby vastly restricted the mobilising potential of any alternative arrangements. The incentive of inclusion in the internal market – the key 'carrot' of the ENP – though generous from the EU's point of view, falls short of the expectations of Ukrainian elites and society, given already existing expectations.

Nevertheless, despite all these odds, the ENP is making a difference in Ukraine. With the AP, the EU has provided much-needed guidelines and a focus for domestic policy-making in Ukraine. Ukrainians have been keen to seize the opportunity provided by the AP to prove their 'Europe-worthiness'. Since the Orange Revolution, the Ukrainian authorities have embarked on implementing the challenging economic and political reforms outlined in the AP in order to achieve their goal – a concrete prospect of membership. For them, the ENP is not regarded as an end in itself. Aware of the 'enlargement fatigue' prevailing within the EU, Ukrainian proponents of European integration have been eager to make the best of – what they regard as – a 'transitional framework'. By implementing the AP, they intended to prove Ukraine's 'Europe-worthiness' and move closer towards a membership perspective.

Given that this perspective is not forthcoming, much depends on the Enhanced Agreement and its capacity to mobilise the Ukrainian domestic actors. It needs not only to substantively clarify and enhance the prospects of Ukraine in comparison to the Partnership and Cooperation Agreement, but also – through evolutionary clauses – give recognition to Ukraine's aspirations of moving closer to the EU.

1. Since administrative and bureaucratic structures in Ukraine are still shaped by the Soviet past and differ significantly from the Western concept of civil service, the terms 'bureaucrats' and 'bureaucracy' are used in this context throughout this chapter and elsewhere in this *Chaillot Paper*.

This chapter focuses on the domestic underpinnings and implications of Ukrainian attitudes and policy towards the EU. It will seek to shed light on the questions as to why the ENP has had a relatively limited impact on Ukraine. It will also analyse the mismatch between what is on offer from the EU and what is needed in Ukraine.

The chapter consists of two parts. The first part aims to examine, first, the motivations and expectations of the Ukrainian elites and society in terms of their relations with the EU and, second, the impact of the ENP on domestic change in Ukraine. The second part shifts the focus onto the implications for the EU. It highlights the mismatch between the supply and demand sides of EU conditionality on the basis of the progress with the implementation of the AP. In particular, it examines the discrepancy between what the EU provides under the ENP framework and what Ukraine requires in order to turn European integration into a stronger drive for comprehensive domestic reforms. The final section will focus on the way forward and, especially, on the extent to which the new Enhanced Agreement is likely to frame relations between Ukraine and the EU in a new and dynamic way.

Ukrainian elites' and public attitudes towards the EU

Why Europe? Ukraine's 'European choice' prior to 2005

Ukraine presents a whole range of geographical, cultural, historical, economic and security reasons for wishing to move closer to the EU. However, until 2004, these aspirations were largely inconsequential in terms of domestic developments. This is because of the combination of a particular national perception of the EU and specific elites' interests which confined the pro-European orientation to the foreign policy domain.

Unlike the case of Russia or Turkey, Ukraine's geographic location in Europe is self-evident.[2] This geographical justification has always gone hand-in-hand with historical claims to Europeanness.[3] This is, admittedly, 'Europeanness seen through the prism of a cycle of several centuries'.[4] Ukraine's historical and geographical claims to an European identity have underpinned its demands for inclusion in contemporary Europe, marked by the borders of the EU. Ukrainians tend to see the EU as a civilisa-

2. Ukraine's Europeanness is underlined by the frequent reference to the fact that the geographical centre of Europe, marked by the Vienna Geographic Society in 1911, is in the Transcarpathian region in western Ukraine. See Judy Batt, 'Transcarpathia: Peripheral Region at the "Centre of Europe"', in Judy Batt and Kataryna Wolczuk (eds.), *Region, State and Identity in Central and Eastern Europe* (London: Frank Cass, 2002), p. 155. However, several other countries in the region, including Poland, Lithuania, Belarus and Slovakia, have put forward similar claims to being the geographical centres of Europe.

3. This included the often-referred to fact that in the eleventh century, Anna, the daughter of the Kievan-Rus ruler, Yaroslav the Wise, became the Queen of France through marriage to Henri I.

4. Catherine Guicherd, 'The Enlarged EU's Eastern Border. Integrating Ukraine, Belarus and Moldova in the European Project', *SWP-Studie*, Stiftung Wissenschaft und Politik, Berlin, 2002, p. 16.

tion-based geopolitical entity, a perception shared initially by most post-communist European countries.

The economic cost-benefit analysis of integration along the alternative geopolitical vectors – namely, the EU versus the Russia-dominated Eastern Bloc – however vague and rudimentary, seems to favour the Western vector over the Eastern one.[5] The goal of joining the EU implied a desire to reverse Ukraine's technological backwardness and lack of competitiveness by gaining access to the funds, investments, technologies and assistance that come with membership of the Union, let alone access to its markets. Because Russia and other CIS countries remained Ukraine's vital trading partners, Ukraine ran the risk of locking itself into economic and political dependency on the latter without the prospect of modernising itself (by attracting Western funds, expertise and foreign investment, and improving the regulatory environment) and thereby raising living standards.

However, the intertwining of politics and business interests created strong incentives for maintaining close economic ties with Russia, often reflecting the specific interests of power elites in Ukraine (as discussed by Pawel Wolowski in Chapter One). This was reflected in the so-called multi-vectored foreign policy conducted under Kuchma (as pointed out by Sabine Fischer in Chapter Four). As a result, Ukraine entered into a commitment with different partners without undertaking a transparent and explicit analysis of the costs and benefits of pursuing integration along different vectors or even an overall assessment of the compatibility of simultaneous integration with the EU and Russia-centred bloc (cf. the Common Economic Space or CES.[6])

With economic issues playing a more ambivalent role, it has been primarily geopolitical and security considerations that have since 1991 motivated Ukrainian policy-makers to capitalise on Ukraine's European location and to seek membership of European sub-regional and regional institutions, such as the EU and NATO. The assertion of independence followed by Euro-Atlantic integration as an inherent foreign policy goal has been largely a response to Russia's difficulty accepting Ukraine's sovereignty, fuelled by doubts regarding the legitimacy and viability of an independent Ukraine. In particular, since the latter half of the 1990s Ukraine has put a premium on seeking closer relations with the EU. Aspirations to EU membership were expressed earlier and more persistently than aspirations to NATO membership.[7]

5. See Roman Wolczuk, *Ukraine's Foreign and Security Policy 1991-2000* (London and New York: RoutledgeCurzon, 2003).

6. One of the very few analyses was undertaken in the report 'Ukraine-EU: on the Road to 4 Freedoms', published in 2003 by the Ministry of the Economy and European Integration.

7. Paradoxically, however, it was in the context of the latter that Ukraine made greater strides, following its unexpected and somewhat secretive decision to seek NATO membership in May 2002. NATO extended the prospect of membership to Ukraine, subject to political and military reforms. However, in the aftermath of the 2006 parliamentary elections, Ukraine's aspirations to NATO membership were put on hold due to the objections of the Eastern Ukrainian political elites, who have turned it into a major political issue.

Until 2004 the overemphasis on geopolitics distorted Ukraine's priorities *vis-à-vis* the EU. Focusing on independence, the Ukrainian elites cherished the idea that independent Ukraine's sheer size and geopolitical significance as a counterbalance to Russia would guarantee it attention from the western institutions. Indeed, the sporadic increase in US interest in Ukraine buttressed this conviction and accounted for a sense of complacency on the part of the Ukrainian elites, stemming from the assumption that Ukraine was simply 'too important to fail'.

Due to this fixation with geopolitics, Ukrainian elites were slow in realising that for the EU, Ukraine's democratic development and economic performance matter far more than its size, geopolitical location and refusal to re-integrate with Russia. Because of this under-estimation of the political, legal and economic dimensions, Ukraine has paid little attention to the importance of meeting contractual obligations with the Union, such as fulfilling the obligations under the Partnership and Cooperation Agreement (PCA), thereby suffering a considerable loss of credibility in the EU. The crucial realisation that its geopolitical 'attractiveness' – i.e. as a counterbalance to Russia – is far from sufficient to secure Ukraine's integration with Europe was only achieved in the aftermath of the Orange Revolution.

In essence, Ukrainian elites' incentive for participation in European integration appears similar to that driving post-communist states' 'return to Europe', namely historical and geographical reasons, as well as the economic and security benefits of membership of the EU. Ukraine, however, differs from other Central and East European states in terms of the fact that the latter displayed a stronger commitment to domestic reforms in order to benefit from closer integration with the EU and were encouraged by a clear perspective of enlargement.

From the late 1990s, the Ukrainian elites expressed the desire to move closer to Europe and to this end made declarations about joining the EU. However, the apparent consensus on closer integration with the EU was accompanied by some dissension on the optimal strategy for pursuing this integration (for example, together with Russia or not). Nevertheless, the fact that even the hardline communists, with their pro-Russian foreign policy orientation, did not object to Ukraine joining the EU, indicates the extent to which supporting European integration became the accepted wisdom, which no mainstream political actor dares to question.

This is because Ukrainian independence has been firmly envisioned in terms of regaining the balance between the East and West, as both these geographical and cultural entities have shaped Ukraine over time, despite the West being more often than not 'squeezed out' by the East, i.e. by Russia's domination.[8] In other words, Ukraine's independence has been inherently linked to its assertion of its Europeanness. Despite his coming to power on a platform of economic pragmatism and pro-Russian orientation, upon his accession to power in 1994 Kuchma soon began to draw from the repertoire of ideas elaborated by twentieth century Ukrainian intellectuals about Ukraine's organic distinctiveness from Russia.[9] From this perspective, with innate Europeanness being a marker of Ukrainian identity, there appears no viable alternative to proclaiming 'an entry into Europe' (*vhid v Evropu*) and demanding the EU's endorsement of this choice by extending the prospect of membership to Ukraine.

Yet despite defining their country as European, the elites remained impervious to Europeanisation. While the benefits of participation in European integration were not lost on the Ukrainian elites, they were incapable of and/or unwilling to usher in the reforms in support of these intentions. European integration was regarded as an exclusively foreign policy matter and remained essentially insignificant in terms of domestic policy-making. The interests grouped around the president – which benefited from the control of the executive branch of power – militated against concerted efforts to implement far-reaching reforms. So despite making repeated declarations in external fora, the concrete implications of the 'European choice' barely featured in the domestic political debate, nor did they inform policy-making in Kyiv.

Symptomatically, none of the political forces (including the pro-European ones) prior to 2004 believed that the EU has a strong influence on Ukraine.[10] The EU's impact on Ukraine's domestic politics was perceived as marginal, in contrast to the influence of the US and Russia.

The Ukrainian political class and European integration since 2005

How has Ukraine's strategy towards the EU changed since the Orange Revolution and the launch of the ENP? What are the atti-

8. Kataryna Wolczuk, 'History, Europe and the "National Idea": the Official Narrative of National Identity in Ukraine', *Nationalities Papers*, vol. 28, no. 4, December 2000, pp. 672-94.

9. Mykola Riabchuk, 'Niejasne Pogranicze. Tozsamosc Ukrainska na Skrzyzowaniu Wschodu I Zachodu', *Przeglad Polityczny*, no. 59, 2003, pp.130-8.

10. See Kataryna Wolczuk, 'Integration without Europeanisation: Ukraine and Its Policy Towards the European Union', Robert Schuman Centre for Advanced Studies, European University Institute, *EUI RSCAS Working Papers*, no. 2004/15, 2004.

tudes and expectations of the Ukrainian political class *vis-à-vis* the EU? How do they view the ENP?

The access to power of new elites had far-reaching effects on Ukraine's policy towards the EU. While Kuchma's regime followed 'integration by declaration',[11] the new political elites, which came to power in 2005, were energised by the Orange Revolution and keen to distance themselves from the inertia on EU-related matters that had characterised the Kuchma era. They declared that a new chapter in Ukraine's relations with the EU had opened and promised to close the glaring gap between declarations and domestic policy-making that had been so evident under Kuchma. Importantly, in their interactions with EU officials, while continuing to plead for 'inclusion in Europe', the Ukrainian authorities became less reliant on geopolitical ('Ukraine as a bulwark against Russia') and historical arguments than on evidence of domestic change. This is hardly surprising: the Orange Revolution provided the Ukrainians with new, bolder arguments – especially based on democratisation – for inclusion in Europe, in contrast to much of the Kuchma era. However, it soon became apparent that while the 'Orange' elites proclaimed a European vocation for Ukraine, they lacked the political machinery and management skills needed to deliver on these declarations. Thus the strong identification they have professed with Europe has not been backed up by the political will and policy-making capacity necessary to override domestic opposition to change. No effective leadership on European issues was evident during the period when the Orange elites were in power (January 2005-September 2006) or under Yanukovych's government (September 2006-September 2007).

Despite the realisation that Ukraine's integration with the EU hinges on the progress of domestic reforms, new political dynamics, including renewed political competition as well as changes in the constitutional framework, made domestic and foreign policy-making precarious and vulnerable to unexpected upheavals. So even though it looked as though Ukraine would put the political instability that characterised it in the Kuchma years behind it, 'post-Kuchma Ukraine' has been anything but stable in political terms. The profound uncertainty prevailing as to how political actors operate under the 'new rules of the game' has affected all areas of policy-making, including EU-related matters.

11. James Sherr, *Ukraine's New Time of Troubles* (Camberley, UK: Conflict Studies Research Centre, 1998), p. 12.

Even after the ill-conceived constitutional reform enacted in January 2006, Ukraine remains a semi-presidential republic. The President retained control over the foreign and defence ministries along with other significant appointive powers, but it is unclear how these ministers are to function in a Cabinet during cohabitation, i.e. when different political forces control the presidency and the Cabinet. Thus, unless the constitutional framework is thoroughly revised and clarified (as suggested in Chapter One of this volume), institutional rivalry is built into the political system of Ukraine.

This institutional rivalry has had a direct bearing on foreign policy-making. Under Kuchma, the President was squarely in charge of foreign policy-making. However since 2006 there has been a noticeable ambiguity in foreign policy-making, as Prime Minister Yanukovych sought to conduct a policy *vis-à-vis* Russia and the EU that was independent of that of the President. This included the pressure put on the foreign minister, Borys Tarasiuk, to resign from the Yanukovych government, which he finally did in January 2007, despite being part of the ministerial cabinet appointed by the president. This created much confusion and uncertainty as to who was speaking on behalf of Ukraine in the international arena, including in the context of interactions with the EU. The Cabinet and the Presidential Secretariat have been competing for primacy on EU-related matters, further weakening the overall coordination mechanism.

Nominally, all mainstream political forces favour European integration. None of the five parties (including the Communist Party) elected to the 2006 and 2007 parliaments have disputed this goal by advocating an alternative framework for political integration.[12] But Ukraine's moves towards European integration, despite being in principle supported by all the mainstream political actors, has not helped to overcome conflict and confrontation in the domestic sphere.

Ukraine's political conflicts do not focus on differences over 'Europe'. Despite a great number of differences between the 'blue' and 'orange' elites, Yanukovych's government did not reject the EU membership objective (in contrast to its attitude to NATO membership) or radically change the strategy. It merely announced a more pragmatic approach towards the EU. Yanukovych implied that without a membership perspective, the degree of Ukraine's compliance with the EU-defined norms and

12. The initiatives, such as the Common Economic Space with Russia, Belarus and Kazakhstan (CES), are seen as a vehicle for economic - and not political - integration.

standards would be based on a cost-benefits analysis. Upon becoming prime minister in September 2006, Yanukovych sought to distance himself from the 'Euroromanticism' of President Yushchenko and avoided commitments *vis-à-vis* the EU other than those already made by the 'Orange' governments. This reflected the fact that the interests of big business represented in the Party of Regions came once again to play an influential role in foreign policy. They dictated the focus on more 'pragmatic' aspects of cooperation, above all securing access to the European market through the Free Trade Area, while at the same time not being against membership of the Union in the long-term perspective. This implied a broad continuity with the Kuchma era and the 'Orange' elites. Most importantly, Yanukovych's government has not revoked the ENP AP, thereby extending the political mandate for its implementation. Despite some wavering, the new government did not pull out of the customs regime with Transnistria, despite being pressurised to do so by the business lobby in the Party of Regions. In practice, however, it paid less attention to enacting EU conditionality than the 'Orange' elites, despite the latter's lack of political unity and administrative experience to implement reforms.

The protracted institutional disarray, the acrimonious dismissal of foreign minister Borys Tarasiuk, and the spring 2007 constitutional crisis can only have had a negative impact on Ukraine's ability to conduct a clear policy *vis-à-vis* the EU (let alone on its image and credibility within the Union).

The Ukrainian public and European integration

Having outlined the elite and government-level attitudes towards the EU, the question then emerges as to what extent the Ukrainian public contributes actively to foreign policy-making in general and European integration in particular, and whether the Orange Revolution has wrought any changes in this regard.

In the late 1990s, the Ukrainian ruling elites proclaimed the 'European choice' without any real public debate on the issue. However this proclamation was not at odds with public opinion, which was largely supportive of the European orientation. The EU is held in high esteem in Ukraine and Ukraine's membership is seen as desirable. But at the same time Europe is not the only choice for Ukrainian citizens. Even though there is a high level of

support for European integration (around 48-55 percent), the alternative option, the Eastern vector, tends to command an even higher level of support (68 percent in a 2005 survey). However, nowhere in Ukraine does the *exclusive* 'Eastern option' command the highest support, indicating that the Ukrainian public is not overly oriented towards Russia and the post-Soviet space. In fact, Ukrainians want to 'have it all', as evidenced by simultaneous support for closer integration with the EU and Russia by approximately one third of the Ukrainian population. These multi-vectored preferences suggest that even though the public is keen on European integration, it sees no contradiction between seeking EU membership and closer political and economic ties with Russia/the CIS.

There are pronounced regional differences with regard to the degree of support for closer integration with the EU. The western and central provinces are most favourably disposed, whereas the east and south are somewhat less so. However, even in the most sceptical regions, the degree of support is comparable to that in the East-Central European states prior to their accession to the EU. Moreover, relations with the EU are considerably less divisive in Ukraine than are relations with Russia, the US and NATO. Of all key foreign policy priorities, relations with the EU evoke least controversies and tensions across Ukraine, so it is a 'safe' option for the elites to pursue.

Despite this positive image of the EU, during Kuchma's presidency, the Ukrainian public did not see the 'European choice' as relevant to their own lives.

Under Kuchma, only every fifth inhabitant of Ukraine believed that European integration was in the interest of all the people in Ukraine. The rest tended to believe that it was – above all – the president, business people or pro-government politicians who were most interested in Ukraine's membership of the EU. According to a different 2003 survey, 93 percent of those surveyed assumed that entering the EU would be useful for Ukraine, but only half of them were able to explain what the benefit(s) might be.[13] Interestingly, this trend became even more pronounced after the Orange Revolution with as many as half of the respondents expressing the belief that it was the new president who was most interested in Ukraine moving closer to the EU. Evidently, the 'Orange' elites failed in popularising and explaining their foreign policy preferences.

13. *Ukrainian Monitor*, no. 17, 21-27 April 2003.

Evident in the data is the continued perceived lack of a link between EU membership and benefits for the population at large. In that respect, the example of new East-Central European member states, where accession to the EU was accompanied by extensive reforms of the public sphere and improvement of standards of public life, appears to have been lost on the Ukrainian public. Despite the 2004 and 2007 enlargement, the Ukrainian people did not see a connection between preparations for joining the Union by their western neighbours and the improved standards of living enjoyed in those countries. This kind of support, devoid of knowledge and understanding of the EU, was identified in other post-communist states.[14] In Ukraine, however, it means that the public does not play an active role in pushing for the European vector. Despite being perceived by the western media as a geopolitical choice between the East and the West, the impact of the Orange Revolution on the foreign policy orientation of the public has been marginal. The Orange Revolution has not changed anything insofar as the detachment of Ukrainian society from foreign policy-making is concerned.

Apparent disparities on foreign policy orientation between the political class and society are significantly mitigated by societal disinterest in foreign policy issues in general. This leaves the Ukrainian elites with a relatively free hand when it comes to the conduct of foreign policy. European integration has tended to be an elite-driven project across all post-communist countries and Ukraine is not an exception in that respect. In contrast to relations with Russia and NATO, relations with the EU are for the main part not politicised and are unlikely to become so, given the relative consensus of the political class in this regard. At the same time, with weak societal involvement, it is almost exclusively the dynamics at the elite level that determine the country's relations with the EU and the pace of domestic reforms undertaken to achieve foreign policy goals.

The elites' reception of and attitudes towards the ENP

Notwithstanding internal political conflicts and societal ambivalence, there has been another major obstacle to acting on reform in line with EU guidelines: the ENP failed to raise the credibility of the EU within the Ukrainian political class. This was at least partly owing to the way that Kuchma's legacy shaped Ukrainians'

14. According to Pridham, the nature of European integration remained abstract for many people in – what became – new member states until the actual accession negotiations started. See Geoffrey Pridham, *Designing Democracy. EU Enlargement and Regime Change in Post-Communist Europe* (London: Palgrave, 2005), pp. 174-87.

attitude to, and perception of, the EU. The litmus test of the EU's credibility in Ukraine was an offer of a membership perspective.[15] While propelling to power alternative elites, the Orange Revolution revived the prominence of symbolism over 'substance' in Ukraine's relations with the EU, especially in the immediate aftermath of the eventful presidential elections of 2004. Many observers in Ukraine believed that the EU could not continue to decline Ukraine's membership aspirations after its demonstration of support for European values during the tumultuous days of mass protests against electoral fraud. They believed that the 'Hour of Europe' in Ukraine would be reciprocated by an 'Hour of Ukraine' in Europe. But, even though Ukraine's profile has been significantly raised in the European media and public opinion, this has not led to the symbolic breakthrough in relations that had been hoped for in Ukraine.

The fact that the EU insisted on conducting relations in the framework of the ENP made Ukrainians feel that the EU did not know how (or perhaps was reluctant) to respond positively to the Orange Revolution. The AP was negotiated during 2004 and largely completed by the time the Orange Revolution took place. The new leadership of Ukraine was given the option to 'take it or leave it'. Instead of revising the AP, the EU, in recognition of the momentous change that had taken place in Ukraine, provided symbolic acknowledgment by adopting a List of Additional Measures in February 2005. Most of the points simply reasserted priorities of the AP with an important caveat: a promise of opening negotiations on the new Enhanced Agreement upon the fulfilment of the political criteria of the AP and with regard to, above all, the principle of free and fair parliamentary 2006 elections. Until that time, the AP was rather vague as to how Ukraine would be rewarded for pursuing reforms stipulated in the AP. During the negotiations, the Ukrainian side insisted on a new Enhanced Agreement but managed only to obtain a vague commitment to opening negotiations upon the fulfilment of the AP, leaving it effectively at the discretion of the Union. Despite this firm commitment provided in the list, these measures have been regarded in Ukraine as an inadequate response to its defence of 'European values' during the Orange Revolution.

The disillusionment was all the more tangible as the Orange Revolution created such high expectations *vis-à-vis* the EU that the new framework for relations – with its focus on pragmatic aspects

15. Kataryna Wolczuk, 'Integration without Europeanisation', op. cit. in note 10.

of cooperation without spelling out the *finalité* of relations – could not satisfy the Ukrainians. Even the name of the policy invokes indignation, as the very term 'European neighbourhood' implicitly locates Ukraine outside (the boundaries of) Europe. Thus, having expressed reservations about the suitability of the Action Plan negotiated under Kuchma to post-Kuchma Ukraine, the new Ukrainian leadership only reluctantly agreed to sign the Action Plan in February 2005. Despite their lingering disappointment with the ENP, the new 'Orange' authorities accepted it but only as a temporary, rather than definitive, framework for relations.

In these circumstances, even though European integration is regarded as desirable by the political elites, neither the EU's stance towards Ukraine nor domestic developments resulted in the greater salience of EU policy for the Ukrainian political class. Owing to the absence of the much-vaunted positive signal from Brussels on membership – the only one the Ukrainian politicians can readily interpret without being intimately familiar with the complexity of the EU – *Evrointegratsia* has remained a vague project, detached from everyday politics. This is because the long-term nature of the project and the lack of a clear-cut prospect of EU membership makes unspecified 'closer relations' with the EU a project too vague to 'focus the minds' of many politicians in Ukraine. As a result, it tends to be easily overshadowed by shorter-term considerations. So, even though – unlike the controversial issue of integration with NATO – the process of moving closer to the EU is not openly contested, its progress easily becomes a hostage to vested political and economic interests and administrative inefficiencies.

From foreign to domestic policies: the impact of the ENP on domestic change in Ukraine

Given the internal situation in Ukraine, what kind of impact has the European Neighbourhood Policy, in general, and the EU-Ukraine Action Plan, in particular, had on the process of domestic change?

In terms of the supply side, the design of the ENP reflects the desire of the EU to project its 'normative power' in its neighbourhood, but without incurring excessive costs and commitments from the Union. Launched by the EU in 2004, the Policy aims to

'promote stability and prosperity' through stimulating political and economic reforms in its neighbourhood. These reforms are to be achieved by transposing the EU's values, norms and standards in exchange for 'access to the single market'. The ENP, which focuses on bilateral relations, uses 'soft law' instruments, which are added on top of existing contractual relations with individual partner countries. In the case of Ukraine this is the Partnership and Cooperation Agreement (PCA) between the EU and Ukraine. Thus, the ENP offers a dynamic and flexible framework. Such a framework was needed to develop an integrated, comprehensive, cross-pillar approach with overcomes fragmentation along EC/EU pillars. One of the ENP principles enhancing flexibility is a differentiated approach on the basis of the progress achieved in individual countries. However, despite the emphasis on differentiation, there is no explicit link between the offered framework for relations and the particular aspirations of the individual partner countries *vis-à-vis* the EU.

As in the case of enlargement, the EU aims to export its normative order to the countries outside its borders. The main instrument of the ENP is a jointly agreed Action Plan, which consists of an extensive list of objectives that partner countries are required to fulfil in order to benefit from closer integration with the EU. The Action Plan requires adherence to Community norms and values, such as democracy and human rights, as well as the standards of the Union as a whole (i.e. much of the *acquis*). This demands complex, extensive and costly domestic adjustments in ENP partner countries. This is based on the conviction that these two types of conditionality are mutually enhancing. The neighbours are to benefit from developing and modernising their economies through anchoring them in the European model of governance.[16] Yet, while clearly borrowing many elements from the enlargement strategy,[17] the ENP is not an alternative to enlargement or, at the least, is 'enlargement-neutral'.

That the Action Plan envisages transposing the standards of the Union as a whole (i.e. much of the *acquis*) is hardly surprising given that much of the *acquis* pertains to the functioning of the single market, access to which is a key reward for implementing the reforms. Thus the AP consists of a long list of objectives, organised into six chapters (see box below) that Ukraine needs to pursue, ranging from holding free and fair elections to revising company law and adopting a nuclear waste strategy.

16. ENEPO (EU Eastern Neighbourhood: Economic Potential and Future Development), 'Working Paper on concepts and definitions of institutional development (harmonization) and methodology of measuring them', June 2007, p. 9. Available at: http: www.case-ukraine.com.ua.

17. Judith Kelley, 'New Wine in Old Wineskins: Promoting Political Reforms through the New European Neighbourhood Policy, *Journal of Common Market Studies*, vol. 44, no. 1, 2006, pp. 29-55.

Given the wide-ranging nature of the AP, this agenda touches on almost all aspects of the functioning of the state. This is because the application of EU law has some bearing on almost every aspect of public policy-making and implementation. Therefore, the enactment of EU-defined changes depends not only on consistent, visible commitment from the highest state authorities, but also on the effective involvement of all levels of government. In practice, this requires creating an appropriate coordinating framework and developing a considerable administrative capacity. In the accession countries, the demands of the adoption of the *acquis* were of such magnitude that the governments had no choice but to establish an effective coordinating mechanism. This has taken the form of a strong, committed 'core executive' capable of coordinating EU-related matters over a number of sectors, overriding domestic 'veto players' and securing the swift passage of a large volume of laws through parliament to align their domestic legislation with the *acquis*.

Key Sections of the Action Plan

2.1 Political dialogue and reform
2.2 Economic and social reform and development
2.3 Trade, market and regulatory reforms
2.4 Cooperation in justice and home affairs
2.5 Transport, energy, information society and environment
2.6 People-to-people contacts

With the elites preoccupied with power struggles in the aftermath of the Orange Revolution, no political leadership on European matters emerged in Ukraine. No longer-term overall strategy beyond the implementation of the AP was defined. In particular, no new strategic documents defining Ukraine's policy towards the EU were adopted. Thus, key documents adopted by Kuchma, such as the 1998 'Strategy on Ukraine's Integration with the European Union', which by 2005 were clearly outdated, remained in force. With the new elites missing out on an opportunity to work out a coherent, long-term strategic framework, European integration became effectively equated with the implementation of the three-year AP (February 2005 – February 2008).

In this context, the adoption of the 'Road Map on the Implementation of the AP' by the first 'Orange' Tymoshenko government in the spring of 2005 was the most important event in the

'domestication' of an EU-defined reform agenda. Adopted through a resolution of the Cabinet of Ministers (and renewed on an annual basis), it became binding for the agencies within the executive branch. Reflecting the structure of the AP, the 2005 Road Map listed 350 measures indicating how, when and by which institutions the objectives of the AP are to be enacted. Even though the AP itself was too general to guide policy-making, the fact that it was 'domesticated' through the adoption of the Road Map was decisive in terms of its impact on domestic policy-making. The Road Map induced greater openness and transparency, with key documents being available in the public domain, than any other government programme ever before.

At the same time, however, there was no radical reform of the institutional framework for European integration. Even though successive governments, regardless of their political hue, endorsed the AP, the creation of an efficient institutional framework for dealing with EU matters has fallen victim to political conflicts and institutional competition. The way that these matters were coordinated changed during the mandates of each of the governments when Ukraine was attempting to implement the AP criteria but without noticeable improvement. The institutional framework has been so ineffective that it is difficult at times to locate where EU-related policy-making takes place.[18] This has important implications for Ukraine's ability to implement the AP but also for the quality of its dealings with EU institutions, most of all the European Commission.

The coordination between the government and parliament on EU-related matters has been particularly weak, a corollary of the volatile political climate in Ukraine. Even though legal approximation is a pivotal aspect of any *acquis*-related priorities, the Ukrainian parliament has shown little interest in the AP. While there are no declared opponents of closer relations with the EU, this consensus hardly enhances the functioning of the Verkhovna Rada. As an institution, the parliament has not focused on legal approximation, despite its crucial role in any closer relations with the EU. The only exception was the concerted effort to pass legislation related to Ukraine's WTO accession, reflecting a rare coincidence of the economic interests of both the parliamentary majority and opposition in late 2006.

The AP's implementation has been left to the discretion of bureaucrats, with responsibility for, and expertise in, EU-related

18. Alan Mayhew et al, 'Ukraine's European Choice: A review of the mechanism for the implementation of Ukraine's policy towards the European Union', Final Report of a Scoping Study for the Government of Ukraine, 2005. (Unpublished paper).

matters. And it is the bureaucrats who responded to EU conditionality most consistently. These emergent bureaucratic enclaves, originally created under Kuchma's presidency in key ministries, have been seeking to implement domestic reforms under the banner of European integration, taking advantage of the political mandate to do so from the respective governments.

The fact that despite the inherent shortcomings of Ukraine's administrative apparatus, sections of the bureaucracy have started to implement the AP, without strong and consistent support from the political class, may indicate the reform potential within the state apparatus itself and the empowering effect of the EU on domestic actors within Ukraine. In the course of AP implementation, some bureaucrats have been pressuring the political class into action. In this way the AP has helped to overturn the hierarchy by departing from the exclusionary decision-making processes and imposing more openness. Also, it is the energetic response to the AP on the part of sections of the Ukrainian bureaucracy that has made the implementation of the AP possible, especially as it made it relatively immune to the political instability which has engulfed Ukraine since the Orange Revolution.

In such a context, what constitutes implementation has been left to the discretion of bodies vested with the enactment of specific priorities. Even though the Road Map is a much more detailed document than the AP, it does not actually specify the measures required to implement the AP as it contains a number of measures, formulated in such general terms that virtually any form of action can be defined as implementation.[19] In AP implementation, ministries' officials act on their own initiative, as there has been no political overview, monitoring and sanctioning, making it an essentially bottom-up process, dependent on the capacity and determination of individual officials rather than institutions. This has impacted on the way that the AP is implemented to the extent that any action can be defined as implementation. For example, the Road Map lists preparing a draft concept or draft law as an implementation measure. While such tasks can be performed by the bureaucracy, the subsequent approval, adoption and implementation of such a draft document is beyond bureaucrats' competence. Given the politicians' limited interest in the AP and weak institutional coordination between the executive branch and the parliament, draft documents do not often

19. Razumkov Centre, *Ukraina-EC: Vid Planu Diy Do Posylenoi Uhody*, Kyiv, 2007.

have a chance of being actually implemented, despite the pressure from within the bureaucracy.[20] Without strong political drive and oversight, this has resulted in a highly fragmented, decentralised and uneven implementation.

This is hardly surprising given that the implementation of the AP has taken place in the context of unreformed Ukrainian post-Soviet bureaucracy, which suffers from a number of weaknesses. These include cumbersome decision-making processes, low administrative competence, unclear division of competencies, and lack of coordination and resources. For example, there is no effective prioritisation based on regulatory impact assessment analysis or cost-benefits analysis – a standard modern technique for policy planning. Without conducting cost-benefits analysis with a view to adopting the *acquis* across a number of sectors, Ukraine is unable to effectively prioritise and selectively adopt parts of the *acquis* in order to maximise benefits resulting from the ENP.

The diffusion of responsibilities across a number of actors means that no horizontal capacity for coordination has developed at a time when cooperation between Ukraine and the EU has become much more complex and multi-dimensional. Ukraine's institutional framework has no capacity to deal with such demands. While operational control is spread across a number of units, there is no effective coordination between them. Several agencies claim to be responsible for the overall implementation of the AP (including the Secretariat on European Integration of the Cabinet of Ministers, the Secretariat of the President of Ukraine, the Ministry of Foreign Affairs, the Ministry of the Economy and the Ministry of Justice). This dispersal engenders competition between ministries, further limiting the flow of essential information and negatively affecting Ukraine's ability to work out its strategy and priorities *vis-à-vis* the EU.

Ultimately, without strong political leadership, an overarching strategy and an effective institutional framework, the enactment of the AP has been uncoordinated and has tended to be driven by short-term considerations. Progress has largely been down to the efforts of individuals within key ministries, operating without a clear set of priorities, sequencing of actions, planning, monitoring, and adequate resources. In many instances, the implementation of the AP in Ukraine amounts to little more than sending draft laws to parliament, without due consideration of

20. See, for example, SDLA, 'Overview of the Legal Adaptation of Ukraine with the *Acquis Communautaire*' (in Ukrainian), Kyiv, 2006.

their content, their subsequent passing/rejection and (if passed) enactment. Thus, in many areas the implementation of the AP is something of a 'paper exercise'. In this context, the activities within the various ministries could not but deliver limited results.

However, even if the actual adjustment in Ukraine has been limited, it has been the very first time that the EU has stepped in to promote *any* kind of domestic change. The EU's involvement has been responded to by at least some domestic actors, but has not occurred on the scale and to the extent needed to make a tangible impact on the standards of public life and socio-economic performance.

Implications for the EU: the ENP and its challenges in Ukraine

Given the internal obstacles to reforms in Ukraine, how effective is the ENP framework in stimulating domestic reforms in Ukraine? The impact of the ENP on Ukraine's relations with the EU so far highlights a number of contradictions between what is on offer from the EU and what is actually needed in Ukraine (the supply-demand sides).

The ENP has been described by an EU official as a bureaucratic response to a political question. The political question pertains to where the final borders of the EU should be drawn. The purpose of the ENP is to facilitate the projection of the EU's 'normative power' in the Union's neighbourhood, while minimising the effects on the internal functioning of the enlarged Union. In this way, the ENP bypasses the whole issue of membership. By providing a generous, even if vague, offer of prospective inclusion in the internal market to its neighbours, the Union hopes to entice them into accepting EU conditionality, while avoiding the risk of jeopardising deeper integration between the members of the enlarged Union.

In the light of the sources of the pro-European orientation in Ukraine outlined earlier in this chapter, it is pertinent to ask how the prospect of a 'stake in the internal market' resonates among the domestic actors. It is also worth considering what challenges such an offer presents for Ukraine. It is already evident that the prioritisation of the economic aspects and benefits of integration

under the auspices of the ENP (through the adoption of the *acquis*) plays a relatively weak role in stimulating comprehensive reforms in Ukraine. There are a number of interrelated reasons for this.

First, in order to mobilise strong and sustainable domestic support for reforms, 'Europe' has to be, above all, a *political* – and not predominantly economic – *project* for Ukraine. The focus on the largely economic and technocratic aspects of integration in order to extract economic benefits is not sufficient to override domestic barriers to comprehensive and deep reforms in the name of 'entering Europe'. This hinges on the mobilisation, empowerment and involvement of a number of domestic actors building an effective coalition in favour of reforms and 'Europe'.

During the process of accession to the EU, the political and economic transformation has become equated with preparation for membership. However, the pursuit of the Free Trade Area in the short term, and inclusion in the EU's single market in the longer term, does not seem to be able to sway the Ukrainian elite and society in the same way as the accession process in East-Central Europe and thereby overcome domestic barriers to reforms, including the self-serving political elites and societal ambivalence.

Incentives for and benefits from economic integration with the EU may become stronger as the reform process gains momentum, but in the short term, the appeal of the ENP is limited to sections of the bureaucracy and business sectors with a knowledge of, and/or interest in access to, the EU market. Admittedly, such interest has grown considerably in Ukraine since the Orange Revolution (see Chapter Two). However, three years after the ENP entered into operation, it is clear that the prospect of the 'access to the market' has not significantly widened the appeal of 'Europe' beyond a few stakeholders in the bureaucracy, business and civil society in Ukraine.

Second, it is difficult for the pro-European reformers to sell the ENP within Ukraine in the light of their own disappointment with the policy. While they have had considerable success in getting the message across about the preconditions for European integration (i.e. domestic reforms rather than geopolitical calculations), they find it difficult to explain what actual benefits are to be gained for Ukraine, given the uncertain type and scale of

benefits under the ENP. In order to increase its appeal, they have to present the ENP as a 'great opportunity'. But this is not easy given that the PCA already envisaged the creation of a Free Trade Area (FTA) between the EU and Ukraine, which is now presented as a big incentive by the ENP. Apart from the FTA, the *finalité* of Ukraine's relations with the EU remains uncertain. In general, prospects for relations between the EU and ENP states tend to be defined as 'more than cooperation but less than integration' or 'economic integration and political cooperation'. As such they do not lend themselves to easy explanation or understanding even at the level of political elites.[21] This matters because the reformers find it difficult to pressurise the political class into reforms, which is one of the key ways that European integration works in tandem with domestic factors to build a coalition for reforms.[22] The lack of clarity and certainty about the prospects makes it even more difficult to engage the public.

Third, for countries like Ukraine the balance of costs and benefits of pursuing EU-defined reforms is less attractive than for the countries with a concrete prospect of membership, however distant. The EU's strategy with the ENP relies on the appeal of economic benefits, which accrue from access to the EU market. These benefits are not limited to revenues from trade but include increased investment, enhanced competition and reduced corruption, which lead to greater economic efficiency, growth and welfare in partner countries. Because this access depends on compliance with the rules and standards of the internal market, the EU proposes that the countries in its neighbourhood adopt significant parts of the *acquis* related to the internal market. This includes institutional harmonisation in the economic sphere, which is wide in scope and encompasses all major horizontal policy areas, although the degree of harmonisation differs across different policy areas, being the highest for industrial products, sanitary and phyto-sanitary standards and competition policy.[23]

So far access to the internal market and institutional harmonisation has been used by the EU to deepen economic cooperation between developed market economies, which chose to eschew EU membership, but were keen to gain access to its market. Given that the key reward of the ENP is access to the single market, the extensive and costly transposition of the *acquis*

21. Within Ukraine, the term 'European integration' (*Evrointegratsia*) is used to describe current relations with the EU (including the PCA and the ENP), aspirations to membership as well as enacting EU conditionality through domestic reforms.

22. Wade Jacoby, 'Inspiration, Coalition, and Substitution. External Influences on Postcommunist Transformations', *World Politics*, vol. 58, July 2006, pp. 623-51.

23. ENEPO, op. cit. in note 16.

related to the market, besides meeting political criteria, is an essential prerequisite for any ENP state if it is to benefit from closer relations with the EU.

In the case of Ukraine, this offer presents a considerable challenge. This is not only because of entrenched political and business interests and the lack of the legislative and administrative capacity to enact the *acquis*, but also because of the high costs involved in bringing regulatory adaptation into line with the *acquis*. For example, the adoption of the EU's sanitary and phytosanitary regulations is one of the areas where not only adaptation costs are high but also domestic opposition is likely to be strong, especially in the light of uncertain benefits in terms of access to the market. Ukraine has a highly complex, inefficient system of food safety and quality regulation. Its reform would involve the adoption of a new legal framework aligned with the *acquis*, enactment of the new regulatory regime and institutional investment in a new physical infrastructure and human resources to operate under the new system (such as laboratories, certification etc).[24] In order to align its competition policy with EU norms, Ukraine needs to act in three areas: first, to pass the required legislation; second, to set up an institution independent of the government to take charge of competition policy; and, finally, it needs to provide access to legal redress in general and/or specialised courts. Each of these are considerable challenges as, for instance, not only the judicial branch needs to be reformed but lawyers and judges need to be trained in an entirely new approach to regulation of the market economy. Such retraining would require considerable human and financial resources.[25] The accession candidate states fulfilled the requirements and met the costs 'up-front' in anticipation of receiving the wide-ranging benefits associated with membership, including access to Structural Funds and the Common Agricultural Policy (CAP). However, it is already evident that the balance of costs and benefits is less attractive in the case of poorer and weaker states, like Ukraine, when only access to the internal market, but not formal membership, is on the cards.[26] The issue of 'front-loading' the reforms is recognised within the Commission:

> The EU seeks to encourage a very ambitious reform programme in partner countries, with many of the political and economic costs being up-front. Yet an important part of the incentives of

24. Olga Shumylo (ed.), *Assessment of the Implications of the Free Trade Area Agreement for Ukraine*, (Kyiv: ICPS, 2007), pp.72-82.

25. Alan Mayhew, *Recreating Europe. The European Union's Policy towards Central and Eastern Europe* (Cambridge: Cambridge University Press, 1998), pp. 221-23.

26. Tim Gould, 'The European Economic Area: a Model for the EU's Neighbourhood Policy? Ukraine's Place in the Wider Europe', *Perspectives on European Politics and Societies*, vol. 5, no. 2, 2004.

> the ENP – for instance in terms of market access and integration and other economic benefits – will only bear fruit later. This creates a real difficulty for partner countries in building the necessary domestic support for reforms.[27]

This drawback can be overcome by a more strategic, selective approach to the *acquis*. Following Alan Mayhew's advice to the candidate countries, the recipe for Ukraine should be to 'take on as much of the *acquis* as it can justify economically and can manage legally in order to gain and benefit from access to the single market, but keeping back costly and inappropriate approximation where there are no developmental benefits or immediate economic gains for the country'.[28] In other words, Ukraine's integration has to be selective in terms of the domains covered and based on benefits in each particular field.

The issue of selectivity is linked to the vexed but rarely confronted question of whether the *acquis* pertaining to the internal market is suitable for a weak state and economy like Ukraine. The attractiveness of EU conditionality stems from it being perceived as a ready-made set of policy prescriptions in the absence of effective domestic policy-making. But the suitability of the common market *acquis* to act as a template for post-communist reforms has been questioned.[29] As Mayhew has warned, 'a blind legalistic approach to approximation will lead to a reduction in the flexibility of the economy, and thus create additional constraints on the transformation process'.[30]

Rather than a blanket, mechanical approach to the *acquis*, partial and gradual harmonisation – to derive maximum benefits without overburdening the economy with EU regulations in non-essential areas such as social policy or environmental protection – is an optimal strategy. This is not only advisable in terms of political and administrative feasibility but also in order to ensure 'deep' compliance. 'If harmonisation is not supported by domestic actors, it can be easily offset with some countermeasures or become implemented discretionally'.[31] As Gonzalo Escribano has pointed out, 'many EU economic institutions are the result of economic development as much as they are the cause'.[32] Superficial transposition of legal norms and institutions would not only not have the desired benefits for the economy but, more damagingly, would strengthen the propensity to simulate 'reforms' in Ukraine.

27. Communication from the Commission on 'Strengthening the European Neighbourhood Policy'. http://europa.eu.int/comm/external_relations/we/doc/com03_104_en.pdf', 4 December 2006, p. 3.

28. Alan Mayhew, op. cit. in note 25, p. 225.

29. See Heather Grabbe, 'Europeanisation Goes East: Power and Uncertainty in the EU Accession Process', in Kevin Featherstone and Claudio Radaelli (eds.), *The Politics of Europeanisation* (Oxford: Oxford University Press), pp. 303-30.

30. Alan Mayhew, op. cit. in note 25, p. 224.

31. ENEPO op. cit. in note 16, p. 25.

32. Gonzalo Escribano, 'Europeanisation without Europe? The Mediterranean and the Neighbourhood Policy', Robert Schuman Centre for Advanced Studies, European University Institute, *EUI RSCAS Working Papers*, no. 19, 2006, p. 5.

Four, Ukraine's ability to derive benefits from partial economic harmonisation with the EU depends on clear prioritisation. Yet Ukraine faces two key obstacles even when it comes to working out its priorities: a lack of capacity and lack of certainty of what is required.

As demonstrated by the implementation of the AP, the capacity needed to work out clear priorities is missing in Ukraine. This is a corollary of the decentralised framework for dealing with EU-related matters. While there are pockets of expertise on the EU, nowhere is this expertise pooled together by administrative coordination and strong political leadership. The lack of capacity has been evident in the way that the Ukrainians prepared for the negotiations on the new Enhanced Agreement (see next section). However, Ukrainian think tanks started ground-breaking work on impact assessment of creating a Free Trade Area between Ukraine and the EU in order to initiate and inform the discussion on costs and benefits of integration in different sectors.[33] The specific discussions on preconditions and benefits and costs (involving business sectors with interest in access to the EU market) builds the support base for domestic reforms as a precondition for closer integration with the EU.

But there remains considerable uncertainty as to what is actually required of the ENP countries. The AP rarely names concrete measures needed to achieve priorities. 'Clearly worded as well as measurable and checkable points in particular (the so-called benchmarks) can be looked for in vain [in the AP]'.[34] Like other ENP states, Ukraine is left to its own devices to work its way through the *acquis* both in terms of defining priorities and implementing them.

Five, the question of the link between task, costs and reward is particularly vexed given that the ENP suffers from a credibility deficiency. The leverage of the EU in Ukraine is weakened not only because the membership perspective is not on offer but because it is ultimately unclear what the actual reward for enacting EU conditionality is. The prospect of access to the market at a future time and to an unspecified extent casts doubts on the credibility of the EU, especially considering the powerful protectionist forces within the EU. The incentive of a stake in the single market clashes with the interest-driven policies dominating the EU's approach to economic relations with non-members. This vagueness and uncertainty weakens the appeal to politicians and cre-

33. See Olga Shumylo (ed.), op. cit. in note 24.

34. ENEPO (EU Eastern Neighbourhood: Economic Potential and Future Development), 'Interim Report: Institutional Convergence of CIS towards European benchmarks', June 2007, p. 84.

ates difficulties for the bureaucracy. A lack of essential understanding of exactly what preparation Ukraine needs to do in order to derive specific benefits undermines the pivotal link between task and reward. Neither of them are clear enough within the ENP.

Finally, the wider regional context in which the ENP is operationalised in relations with Ukraine cannot be glossed over. While Ukrainians are disappointed by the EU's intransigence on the membership issue, the ENP heralded a sea change in the 'Russia first' policy pursued by the EU in the former Soviet Union. Up to 2004, Russia was at the top of the EU's policy priorities towards the Commonwealth of Independent States. Any new initiative was first developed and tested with Russia and then perhaps rolled out to other post-Soviet states. Under the ENP, the policy towards Russia and Ukraine has been decoupled to a more significant extent than ever before.

However, this uncoupling is not irreversible: large EU Member States continue to see Russia as the main partner and aim to create a sense of inclusion by linking policy initiatives towards Russia with initiatives towards other post-Soviet states. One analyst concluded that the ENP has not generated major ruptures between the policies of the EU towards Russia and Ukraine.[35] Because of the strategic nature of EU-Russia relations, the EU is inclined to offer to the Russians instruments and inclusion in policies, which are presented to Ukraine as a 'benefit' under the ENP. This was the case with the visa facilitation agreements between the EU and Russia and the EU and Ukraine respectively. In other words, Ukraine has to work for that which Russia gets for 'free'. This undermines the credibility of the EU's conditionality *vis-à-vis* Ukraine and induces not only cynicism but also uncertainty as to what it takes to advance relations with the EU.

In sum, as has been convincingly argued in academic literature, external actors can influence domestic trajectories if they work in tandem with domestic forces. In Ukraine domestic politics has not been conducive to initiating a comprehensive reform agenda. Yet the design and execution of the ENP itself did not provide a significant boost to the domestic reform efforts either. As the implementation of the AP in Ukraine has shown, the EU con-

35. Laure Delcour, 'Does the European Neighbourhood Policy Make a Difference? Policy Patterns and Reception in Ukraine and Russia', *European Political Economy Review*, no. 7, Summer 2007, p. 140.

fronts a number of challenges in making the ENP work and in order for it to make a difference in partner countries. Many of these problems are not new and were observed, for example, during the enlargement process. But combined with greater obstacles to domestic reforms present in post-Soviet countries such as Ukraine, the low effectiveness of the flagship foreign policy of the EU, the ENP, perpetuates the expectations-capabilities gap in the EU's foreign policy.

The way forward: the new Enhanced Agreement

Since 2005 ties between Ukraine and the EU have intensified. The EU and Ukraine have signed several significant agreements (on energy, aviation and a satellite navigation system). The Union has granted market economy status to Ukraine according to the EU Basic Antidumping Regulation, something that had long been sought by the Ukrainian government. Also, the EU and Ukraine have concluded negotiations on a visa facilitation agreement designed to help some groups in society, such as diplomats, students and scholars, to enter the Schengen zone. Also, Ukraine has started to benefit from access to the Twinning Programme, albeit on a limited scale so far.

The end of the 10-year period of the functioning of the PCA is an opportunity to revise the legal framework to renew solid legal foundations but also to instil a stronger sense of purpose and dynamism into relations.[36] No doubt, of all the developments in EU-Ukraine relations in recent years, the new agreement is the most important one, superseding the ENP. Dissatisfaction with the PCA and the 'soft' framework of the ENP means that the agreement carries a promise of both providing a real impetus to relations and a long-term sustainable framework. Unlike the ENP, the new agreement will contain 'hard' commitments, renegation on which could have legal implications for both sides.

The new agreement's salience stems from high expectations on the Ukrainian side. The Ukrainian foreign policy-makers have sought to move beyond the PCA for some time. This was one of the key demands raised during the negotiations on the AP in the course of 2004, which was only met after the Orange Revolution. The very prospect of the new agreement was a key mobilising factor in the implementation of the Action Plan.

36. This is not because the PCA was a poor agreement. In many respects, the PCA was a good-quality, innovative agreement. For example, the political chapter was particularly well prepared. But one needs to differentiate between the PCA's quality as a legal document and its reception as a political instrument in Ukraine, which affected its mobilising potential.

No doubt, this insistence on the new agreement is driven by Ukraine's quest for symbolic recognition of its 'European vocation'. It has been trying to use the ENP for what the PCA failed to provide – confirmation of Ukraine's European 'destination'. Soon foreign policy-makers became even more disappointed and frustrated with being grouped together with the EuroMed countries which have no chances of attaining EU membership.

In Ukraine this symbolic dimension is as important as specific economic benefits. Indeed, enhanced and clarified economic prospects under the new agreement would create a stronger sense of differentiation within the ENP and hence leave Ukraine with a sense of moving closer to the EU. Also within Ukraine, the focus on the shorter-term benefits of the ENP, without giving up on the membership perspective, would create a stronger alliance in favour of European integration between the 'Euroromantics' and the 'Europragmatists' among the Ukrainian elites. This alliance would positively affect the reform process. Even though the current prospects stop short of membership, pursuing economic integration is still a very ambitious agenda for Ukraine, given the scale of regulatory adjustments needed and related costs, and thus requires a strong consensus and political commitment. As Alexander Kwasniewski, former president of Poland and seasoned observer of Ukraine, noted: 'The prospect [of deeper economic and political integration with the EU] has been greatly strengthened by the new realism in the attitude of Ukraine's leaders toward Europe and their willingness to put the substance of integration before the theology of accession status'.[37] At the same time, the implementation of this agenda would make Ukraine's case for membership stronger, thus appealing to the 'Euroromantic' wing in Ukrainian politics.

However, the configuration of constraints on the EU's part make it difficult to meet Ukraine's expectations. At present, no strong mandate for a new agreement has been provided by the Council. The mandate merely asserts that 'through this Agreement, the European Union aims to build an increasingly close relationship with Ukraine, aimed at gradual economic integration and deepening of political cooperation'. Without a consensus in the Council, no strong incentives in the Enhanced Agreement are envisaged.

The EU's predicament lies in its desire to avoid setting a precedent by entering far-reaching commitments. The Agreement with

37. Commentary by Aleksander Kwasniewski, *The Wall Street Journal*, 7 September 2007.

Ukraine is likely to be the first one in a series of Neighbourhood-type agreements. At the same time, if differentiation as one of the key principles of the ENP is to become a reality, individual agreements have to offer 'value added' according to the specific circumstances of partner countries. But given the lack of consensus on the scale of benefits the EU should provide to the ENP countries, in practice the emphasis is likely to be on scaling down expectations across the board rather than amplification of differentiation. The Ukrainian case is also important because of the wider regional context: while not being covered by the ENP, Russia is unlikely to demand, and be satisfied with, less than Ukraine is offered.

But with Ukraine the emphasis on scaling down the expectations is not an optimal strategy if the EU does not want to have to contend with stronger demands for membership ('louder knocking on the door'). If there are no tangible benefits resulting from the post-PCA agreement, Ukraine will insist on being singled out. Far from being an impetus to the relations, the new agreement may turn into a source of contention, and share the fate of the PCA.

So in essence, the negotiations on the agreement present a challenge of balancing Ukraine's expectations with the constraints prevailing in the EU through a dynamic legal framework.

What type of agreement will emerge from the negotiations? The question of terminology and its political ramifications is of acute importance. Ukraine has been preoccupied with terminology and insists on an Association Agreement. Such an agreement offers the most privileged form of relations between the Union and third countries. The internal coherence of the ENP would also require that the new agreement is of an association type. The EuroMed countries already have Association Agreements, so logically relations with the Eastern neighbours should be upgraded too. But the association itself has no bearing on membership prospects. So Ukraine does not want any type of Association Agreement – it wants an agreement modelled on the Euro-agreements which opened the door to membership for East-Central European states in the 1990s. In other words, it wants its eligibility for membership enshrined in legal form. This thorny question of the *finalité* of relations will cast a shadow over the negotiation process but is unlikely to be resolved in the course of it.

The key attraction of the new agreement will be its binding character (in contrast to the AP which is essentially a 'soft law'

instrument, thereby leaving much discretion as to what commitments and obligations it entails for both parties). Also, according to the legal expert Christophe Hillion,[38] the agreement should be durable and lasting. This can be achieved by evolutionary clauses and an institutional framework, which would enable joint institutions to take binding decisions on the future evolution of the relations. Unless a decision-making body is created, any changes to the legal framework would only be achieved through a new agreement, as has been the case with the PCA. Also, to increase the leverage of the EU over Ukraine, the new agreement should allow for monitoring of Ukraine's compliance. It is in Ukraine's interest to agree to such asymmetrical monitoring.

While the optimal legal properties are fairly uncontroversial, the content of the agreement in terms of its scope and depth are more likely to generate extensive discussion. The agreement needs to be comprehensive and should include trade, energy, transportation, environment, CFSP and so-called third pillar issues. Provisions on the Free Trade Area will form the largest and most substantive part of the agreement. What will it contain? An inclusion of industrial goods is widely expected and relatively uncontroversial. But the provisions on trade in services and agricultural goods will be a key indicator of the EU's willingness to forego its own interests to offer tangible benefits to assist the neighbours. It has been argued that a shallow FTA, which is limited to an asymmetrical elimination of tariffs for industrial goods, would offer very little value added to the relations.[39] Yet, a 'deep' FTA requires extensive regulatory adaptation inside Ukraine. In order to provide Ukraine with incentives to embark on these adaptations, a clear-cut scenario for each sector should be aimed for. Clarifying the scale, stages and prerequisites for integration across a number of sectors would enable Ukraine to prioritise its regulatory alignment with the *acquis*, thereby increasing the likelihood of this actually happening.

However, the way the negotiations have been conducted throughout 2007 reflects the difficulties on both sides and runs the danger of increasing mutual apprehension. Without a strong mandate from the Council, the EU negotiating team has limited room for manoeuvre. On the Ukrainian side, despite making good progress on meeting WTO accession conditions in 2006, this precondition for opening the negotiations on the FTA was not met during 2007. The internal political crisis – responsible for

38. Christophe Hillion, 'The new relationship between the European Union and its ENP partners – Lessons from the future EU-Ukraine agreement', *Bulletin of Opinions dE*, no. 2, January-February 2007, Demos-Europa, Centre for European Strategy, Warsaw.

39. Michael Emerson, et al, *The Prospect of Deep Free Trade Between the EU and Ukraine* (Brussels: CEPS, 2006).

the delays with the WTO accession – also accounts for the disarray during preparations for negotiations in Ukraine. The lack of a strong political interest and a coordination mechanism is difficult for the bureaucrats – who make up the bulk of the Ukrainian negotiating team – to compensate for with their own commitment and expertise. Also, with the bureaucracy leading the negotiations, it may be difficult to subsequently persuade the political class of the importance of meeting the commitments and obligations resulting from the Agreement.

Conclusion

In 2005, the EU and Ukraine entered a qualitatively different stage of relations in comparison to the Kuchma era. Owing to the Orange Revolution and the ENP, the Ukrainian authorities accepted the EU-defined reform agenda as a precondition for closer relations with the EU. Democratic gains from the Orange Revolution paved the way for a more open political dialogue. But despite the acceptance of the reform agenda, the overall impetus for change has been too weak to make a real difference. This reflects domestic barriers to change and the EU's limited ability to influence developments in Ukraine through the ENP.

The ENP created a framework to project the EU's 'normative power' to induce changes in domestic structures and policies in neighbouring countries. In practice, however, the design of the ENP reflects the precarious balancing act between the Union's aspirations as a foreign actor and the interests and willingness of its Member States to bear the resulting costs. Thus, the evolution and implementation of the policy has been hampered by the difficulties both in specifying the benefits and devising tools and instruments to assist domestic reforms in 'target countries'.

Nevertheless, despite its limitations, the ENP has been instrumental in focusing minds on the preconditions of European integration in the context of Ukraine. It was the AP that brought the message home as to what *Evrointegratsia* is about. The discussion on Europe shifted from history, geography and geopolitics to European values, norms and standards. This shift in discourse represents a sea change, leaving behind the misunderstanding and frustration that characterised EU-Ukraine relations prior to the ENP.

Without denying some spectacular achievements of the Orange Revolution, much remains to be done in Ukraine to enact European values, norms and standards. But while the reform agenda of transforming the state has barely started, the momentum for change is gone. Can 'Europe' imbue Ukraine with the determination needed for a renewed and sustained reform effort?

As the implementation of the AP demonstrated, post-Soviet political, economic and administrative structures, institutions and practices in Ukraine make it difficult for the EU's policy guidelines to be acted on. There is an incomparably better understanding of preconditions for moving closer to the EU but the consensus, political will and capacity to do so remain in very short supply. Even though Ukraine has no declared opponents of European integration, the scale of reforms required and domestic barriers to enacting them mean that the challenges lying ahead of Ukraine on the 'road to Europe' are formidable.

Ukraine is not an easy partner for the EU. While expectations are running high, the credibility and capacity to take on obligations remain low. The relationship risks leading to foiled expectations on both sides and accumulating mutual distrust and suspicion. This is hardly surprising (but rarely appreciated in Ukraine) given that the attitude prevailing within the EU is that the neighbouring countries need to want to help themselves and only then can the EU be of assistance.

With all the domestic barriers to reforms, the overall consensus on European integration is unlikely to be translated into swift and effective enactment of EU conditionality under any Ukrainian government in the near future. In other words, Ukraine is unlikely to do what it needs to do of its own accord. This raises the importance of pressure, monitoring and assistance from the EU and its Member States for keeping up the momentum of change. And it will be in the context of the new agreement that the EU's willingness and capacity to assist Ukraine to becoming a stable and prosperous country – i.e. the 'ideal neighbour' the Union wishes to have – will be tested.

Ukraine as a regional actor

Sabine Fischer

4

Introduction

After his election in December 2004 Viktor Yushchenko turned the tide of Ukrainian foreign policy by replacing the 'multi-vector' policy of his predecessor with a clear orientation towards the EU and NATO. This 'turn towards the West' was accompanied by Kyiv's aspirations to regional leadership and the promotion of a belt of democratic states along the EU's eastern borders. In order to attain these goals, Kyiv sought to promote the revival of GUAM,[1] which later on was flanked by the Community of Democratic Choice (CDC). Another important regional initiative addressed the resolution of the protracted conflict in Transnistria. At the same time, Russia remained highly significant for Ukraine's domestic as well as external policies. Moscow greeted Kyiv's new initiatives with great suspicion and denounced them as inspired by external actors, aiming at rolling back Russian influence in its own backyard. Accordingly, relations between Kyiv and Moscow deteriorated quickly.

Three years after the Orange Revolution, Ukraine's regional policy has almost completely disappeared from the stage. After the parliamentary elections in March 2006 and the installation of the Anti-Crisis Coalition in August 2006, the country's foreign policy seemed to return to the multi-vector policy of the Kuchma era, again vacillating between Euro-Atlantic integration and closer alignment with Russia.

As Kataryna Wolczuk points out in Chapter Three of this *Chaillot Paper*, Ukraine's foreign policy orientation does not only involve a choice between different partners for political and economic cooperation. It is a strategic decision between two models of development, and as such essentially a decision on the identity and future of the country. It forms part of Ukraine's state and nation-building processes, and its outcome will have a decisive impact on the future of the region, and Europe in general. Will

1. The acronym is derived from the first letters of the four member states: Georgia, Ukraine, Azerbaijan and Moldova. The organisation was founded in 1997. Its acronym changed to GUUAM to take account of Uzbekistan's membership in 1999, but reverted to GUAM when Uzbekistan withdrew in 2002. In May 2006 the organisation was renamed GUAM Organisation for Democracy and Economic Development.

Ukraine manage to anchor itself firmly on the side of the EU and NATO despite Russian resistance? Will it be drawn back into the Russian orbit? Will it remain in its current, precarious position 'in between' the EU and Russia', a part of an unstable and fragmented region, sandwiched between two greater entities competing for influence? Or will *rapprochement* with the European Union and integration in the global economy finally be possible in cooperation with Russia, thus avoiding the further polarisation of the regional environment?

The reincarnation of the Orange Coalition, which was approved by the Verkhovna Rada on 18 December 2007 with a razor-thin majority, and this only after lengthy and difficult negotiations following the parliamentary elections on 30 September, does not guarantee substantial changes in the conflict-prone domestic constellations of the country. Therefore it remains practically impossible to forecast the direction which Ukraine will eventually take. Any of the above-mentioned options depends on developments not only in Ukraine, but also within the EU and Russia. The most desirable scenario would certainly be a joint *rapprochement*, because it would be the only option allowing for a reduction of tensions in the region. However, such a development would require profound changes in Russian domestic and foreign policy too. Such changes, however, are not to be expected in the short and medium-term future.

This chapter explores the development of Ukraine's regional policy and its relations with Russia. It seeks to identify the reasons why the regional initiatives pursued so dynamically by the early Yushchenko leadership failed to produce tangible results.

The first section explores the link between domestic politics and foreign policy, which is particularly strong in a country like Ukraine exposed to profound domestic changes. The second section investigates Ukraine's regional policy in the aftermath of the Orange Revolution, specifically with reference to GUAM, the CDC and the Yushchenko Plan for conflict resolution in Transnistria. Finally, the chapter focuses on Ukrainian-Russian relations. A short analysis of the two countries' foreign policies is followed by a closer look at three issues, which have almost constantly featured prominently on the bilateral agenda since December 2004: Russian-Ukrainian energy relations, debates about the future of the Black Sea Fleet (BSF), which are closely intertwined with the question of the status of the Crimea, and, finally, Ukraine's

involvement in Russian-led integration and cooperation in the former Soviet Union.

Foreign policy and domestic politics

Recent domestic disorder has led to doubt being expressed as to whether the 'Orange Revolution' really was a 'transition from post-communism to democracy'[2] or merely a transfer of power from one interest group to the other, thus allowing the dysfunctionality of 'pre-revolutionary' institutions to re-emerge and anti-revolutionary actors to regain influence.[3] An assessment of the impact of the Orange Revolution on Ukraine's post-Soviet transformation would certainly be premature. Charles Fairbanks' cautious appraisal of the 'coloured revolutions' as 'rites of passage, which (...) separate and symbolize two distinct periods, whereas the concept of "transition to democracy" has come to have a foggy indeterminacy'[4] is a good description of the underlying significance of the events, because it accurately gauges their impact, at the same time leaving the final outcome of the institutional transformation relatively open.

Domestic change is a crucial factor shaping foreign policy, and this is especially the case in countries shaken by cataclysmic internal events. In Ukraine, this nexus between domestic politics and foreign policy is particularly significant for two reasons: first, Ukrainian foreign policy-making suffers from domestic disagreement and infighting over the future external orientation of the country.[5] This absence of unity is very much a consequence of Ukraine's ethnicised regionalisation, which separates the Eastern and Southern parts from the Western part of the country and is regularly being exploited in power struggles in Kyiv. Secondly, as has been shown by Pawel Wolowski in Chapter One of this volume, the political process is severely hampered by an unstable and fluctuating institutional environment. This allows for antithetical positions to alternately or even simultaneously translate into foreign policy behaviour.

Foreign policy thinking in Orange and Blue

The foreign policy orientations of the Orange Coalition and the Party of Regions have often been interpreted as unambiguously

2. As it was interpreted by Michael McFaul in 2005. See Michael McFaul, 'Transitions from Postcommunism', in *Journal of Democracy*, vol. 16, no. 3, July 2005, pp. 5-19.

3. James Sherr, 'Ukraine's Scissors: between Internal Weakness and External Dependence', *Russia.Nei.Visions,* no. 9, March 2006.

4. Charles H. Fairbanks Jr, 'Revolution Reconsidered', in *Journal of Democracy*, vol. 18, no. 1, January 2007,pp. 42-57, p. 56.

5. This makes Ukraine different from Georgia, for example, where the Saakashvili government can build its policy of Euro-Atlantic integration on much broader public and elite support.

pro-Western and pro-Russian respectively. A closer look reveals a much more nuanced and multi-layered picture of both sides' foreign policy postures.

The Orange Coalition, which took power from President Kuchma at the beginning of 2005, emphasised Euro-Atlantic integration as its main foreign policy goal. This aspiration was complemented by a more active regional policy, addressing those states in the Western and Southern CIS who shared the desire for closer relations with the EU and NATO and greater autonomy from Russia.

At the same time, many of the steps taken after the Orange Revolution demonstrated the new leaders' awareness of Russia's importance in Ukraine's foreign and domestic policy.[6] Ukrainian pundits in 2005 cited two main reasons for this 'natural' phenomenon: '... on the one hand, Ukrainian citizens (the majority of them being voters) traditionally stand for the development of relations with Russia. On the other hand, without establishing reliable, predictable and constructive relations with Russia, the strategic goal of integration into the European and Euro-Atlantic institutions will be difficult to accomplish.'[7] One may add a third, economic reason: because breaking up with Russia would have the most severe consequences for the Ukrainian economy. Not only is Ukraine dependent on Russian energy deliveries, but the two countries also share production lines in important industrial sectors, such as aviation, metallurgy etc.[8] Thus, while securing internal democratisation through European and Euro-Atlantic integration, the Orange Coalition proclaimed a pragmatic approach towards Russia, aiming at preserving functioning relations with their Eastern neighbour.

The Party of Regions, on the other hand, did not display a purely pro-Russian, anti-Western foreign policy ideology. This image, cultivated thoroughly in Western, Russian and partly Ukrainian discourses around the 'Orange Revolution' and fostered by the blunt Russian support for Yanukovich during and after the 2004 election campaign, neglects the way in which Ukrainian foreign policy developed during the Kuchma era. This 'multi-vectoral' policy was never oriented towards deeper integration with Russia or unequivocal acceptance of Russian dominance over the CIS. On the contrary, it aimed at maintaining a balance between Ukraine's Eastern and Western neighbours. It was the Kuchma leadership who tabled NATO and EU membership –

6. F. Stephen Larrabee, 'Ukrainian Foreign and Security Policy after the Collapse of the Orange Coalition', in *Quid Ukraine's Strategic Security?*, ESF Working Paper no. 24, January 2007, pp. 30-6.

7. 'Section 4. Foreign and Security Policy', National Security & Defence, Razumkov Centre, Kyiv, no.5, 2005, p. 44.

8. David Lane, 'Perspektiven der ukrainischen Beziehungen mit der EU: Freihandel statt Marktwirtschaft', *Ukraine-Analysen*, no. 15, 2006.

albeit with much less commitment to what this implied in terms of domestic consequences and transformations.[9] It was also under Kuchma that Ukraine entered NATO's Partnership for Peace Initiative and negotiated the NATO-Ukraine Action Plan as well as the ENP Action Plan with the EU.

Hence, Yanukovich should not be regarded solely as the heir of a period of pro-Russian policy as opposed to the pro-Western policy promulgated by the Orange Coalition. Furthermore, the Party of Regions recently started displaying growing caution regarding economic integration with Russia and the activities of Russian business in Ukraine. Eastern Ukraine's business elites, who provide the most important support for the Party of Regions, are increasingly reorienting themselves away from Russia and towards economic integration with the European Union. As Rosaria Puglisi illustrates in Chapter Two, they show growing interest in certain international norms and business standards, which would help them protect the wealth they accumulated during the 1990s. The prospect of getting access to the European market also makes business circles more open to closer relations with the EU. These developments are rather new, and there are strong factors potentially pulling economic actors back into the Russian orbit. However, as Puglisi demonstrates in her chapter, the role of the so-called oligarchs is gradually shifting towards more congruence with the Western-oriented forces.

The above analysis shows that the main political camps' positions on foreign policy overlap significantly. However, this has not led to a foreign policy consensus, which could form a more stable basis for Ukraine's behaviour in the international arena. The reason for this lies basically in the inter-institutional competition and the weaknesses of political decision-making. In today's Ukraine, political actors still prefer to emphasise differences instead of similarities, thus exploiting foreign policy issues in domestic power struggles.

Foreign policy decision-making – under construction

The development of the foreign policy decision-making process reflects the general weakness of state structures in Ukraine and aggravates the emergence of a coherent foreign policy. After the 'Orange Revolution', and particularly after the 2006 parliamentary elections, this weakness allowed for competing interest

9. See Wolczuk, p. 90.

groups to exploit foreign policy decision-making in their struggle for power.

The Ukrainian constitution provides for a division of labour with regard to the conduct of foreign policy between the President, the Verkhovna Rada and the Cabinet of Ministers/Ministry of Foreign Affairs. While the President administers the country's foreign policy[10] and heads the National Council of Security and Defence, the Verkhovna Rada 'determines the principles of [domestic and] foreign policy',[11] and exerts indirect influence through the right to approve (or decline) the state budget and adopt (or dismiss) international treaties. The Cabinet of Ministers/Ministry of Foreign Affairs is responsible for foreign policy implementation.[12]

In the last years of the Kuchma era, the creation of informal institutions duplicating the constitutional organs increasingly aggravated democratic control over foreign policy-making. The expansion of the Presidential Administration and the gradual transfer to it of an ever-increasing number of competencies from other branches of power were a case in point. In November 2003 a law entered into force, which provided the Foreign Policy Department of the Presidential Administration with the right to oversee the activities of the Ministry of Foreign Affairs and control its staffing policy. 'As a result, the institution, which has no constitutionally specified functions and powers, effectively usurped the role of the foreign policy decision-making centre, transforming the Foreign Ministry into an institution that merely carries out orders.'[13]

The constitutional compromise negotiated during the Orange Revolution weakened the position of the President and his/her administration to the advantage of the other branches of power. The Orange leadership initiated a process of reorganisation of state structures aiming at reducing duplications and informal institutions, and enhancing transparency and efficiency. Several presidential decrees issued in 2005 confirmed the role of the Ministry of Foreign Affairs as a co-ordinator of foreign policy activities and thus reinstated its initial competencies. The internal structure of the Ministry was reorganised, the number of departments reduced and the staff reshuffled. However, by the end of 2005 these structural reforms had not resulted in more efficient policy-making. The importance and influence of single branches of power in the reorganised political system depended on individual figures and their ambitions. Thus, the relation-

10. By representing the state in international relations, administering the foreign policy activity of the State and conducting negotiations and concluding international treaties of Ukraine (Constitution of Ukraine, Art. 106/3: http://www.rada.gov.ua/const/conengl.htm); adopting decisions of the recognition of foreign states (Constitution of Ukraine, Art. 106/4); and appointing and dismissing heads of diplomatic missions of Ukraine to other states and to international organisations (Constitution of Ukraine, Art. 106/5).

11. Constitution of Ukraine, Art. 85/5: http://www.rada.gov.ua/const/conengl.htm.

12. Constitution of Ukraine, Art. 116/1.

13. 'A New Foreign Policy for Ukraine', in *National Security & Defence*, Razumkov Centre, Kyiv, no. 9, 2004, p. 5.

ships between those individuals were often the most important factor shaping the (dys)functioning of inter-institutional relations and the policy process.[14] The actions of the executive bodies remained badly-coordinated. Foreign policy was actually conducted by several institutions at the same time and resulted in Ukrainian foreign policy presenting contradictions on the international stage.

The strategic foundation of Ukraine's foreign policy also remained nebulous. The only official document outlining the 'Fundamentals of Ukrainian Foreign Policy' dates back to 1993. After the Orange Revolution it was considered obsolete. The new authorities announced that it would be replaced by a new document mirroring the manifold changes which had taken place since 1993. However, the year 2005 passed by without any measures being taken. With the parliamentary elections in March 2006 it became less and less likely that a law codifying Euro-Atlantic integration as the fundamental course of Ukraine's foreign policy would be adopted by the Rada. The conflict around Foreign Minister Tarasyuk, who lost much of his influence after the coming to power of the Anti-Crisis Coalition in August 2006, further paralysed decision-making on the issue.[15] The split between the President and his Foreign Minister on the one hand, and the Prime Minister and the majority in the Rada, on the other, became ever more obvious. In autumn 2006, several parliamentary factions worked on draft laws on foreign policy to replace the 1993 document. The blueprints ranged from Ukraine's quick accession to NATO and the EU over non-block status to far-reaching integration with the CIS and other organisations in the post-Soviet space.[16]

With a growing number of deputies from the Our Ukraine party defecting to the Party of Regions faction at the end of 2006 and the beginning of 2007, the situation became precarious. The Orange forces' chances of having a bill approved by the Rada were shrinking, while the growing Party of Regions faction together with their coalition partners were enjoying increasing support. Considering the general weakness of law implementation in Ukraine, such a step would most likely not have profound consequences for the conduct of foreign policy. The gradually shifting priorities of the Party of Regions described above also justifies doubts as to whether such a law would have had severe consequences for foreign policy-making. Nevertheless, a bill making the

14. Much of 2005 for example was overshadowed by the conflicts between Prime Minister Yulia Tymoshenko and Secretary of the National Security and Defence Council Petro Poroshenko, resulting in the government crisis in September 2005 and the ousting of both politicians.

15. Oleksandr Sushko and Nataliya Parkhomenko, 'Ukraine's Foreign Policy in 2006: Analysis and Prognostication', *Ukraine Monitor*, Policy Paper no. 9, 2006. Available at: www.cpcfpu.org.ua.

16. Oleksandr Sushko, 'Affecting Ukraine's Foreign Policy through Instruments of Law Making', *Ukrainian Monitor*, Policy Paper no. 8, 2006,. Available at: www.cpcfpu.org.ua.

idea of neutrality and integration with the CIS the cornerstone of Ukraine's foreign policy would send a strong signal to the outside world and further weaken the position of the President.

A closer look at foreign policy thinking and the decision-making process rebuts the assumption that with Yanukovich's return to power the Prime Minister's office simply reintroduced the 'multi-vector' policy of the Kuchma years. The Euro-Atlantic orientation has acquired a firmer status in Ukrainian foreign policy thinking and making than was the case before the Orange Revolution.[17] Despite their weakness, the Orange forces have managed to infiltrate the political system and to secure institutional representation. Parts of the 'Blue camp' have come to support economic integration with the EU, gradually moving closer to the positions of their political adversaries. However, Ukraine's political elites are still far from a foreign policy consensus. Their *rapprochement* remains rather clandestine, because various actors cannot resist the temptation to exploit foreign policy in domestic infighting. This prevents the opposing camps from emphasising obviously existing similarities, and locks foreign policy into domestic power struggles. However, as opposed to Kuchma's 'multi-vector' policy, in Ukraine today the 'vectors' do not form part of a single policy, but are pursued by different branches of power. Ukrainian foreign policy, ambiguous though it may be, is also therefore the expression of a new pluralism induced by the Orange Revolution.[18]

Ukraine as a regional leader?

Upon assuming office, the new Ukrainian leadership announced its intention to set new priorities in regional cooperation and make Ukraine a regional leader and promoter of democracy by gathering like-minded states on the road to European integration. In the words of former Foreign Minister Tarasyuk, 'this community should, as the Visegrad Group, help us in our *rapprochement* with the European Union. We have to support each other. Ukraine, which has already reached a higher level of democratic and economic development, has to support and pull the others in this direction. This is the leadership role Ukraine is supposed to play for objective reasons.'[19]

17. See also F. Stephen Larrabee, op. cit. in note 6, pp 30-36.

18. Author's interviews in Kyiv, June 2007.

19. Boris Tarasyuk, 'Ot nas ozhidayut real'nykh deystviy', [We are expected to act in reality], *Zerkalo Nedeli*, no. 15(543), 23 aprelya – 6 maya 2005. Available at: www.zn.ua.

GUAM – a sleeping beauty awakes?

When President Yushchenko announced his intention to reactivate GUAM in spring 2005, the organisation had been almost forgotten.[20] During the 10 years of its existence, it had never lived up to its founders' expectations to develop into a political, economic and infrastructural bridge between the Caspian region and Western Europe. The growing international isolation of Kuchma's regime, and its eventual turn towards Russia in 2002/2003, had further weakened the organisation.

At the Summit in Chisinau in April 2005 the Ukrainian leadership suggested transforming GUAM into a fully-fledged international organisation based on three main pillars: democratic changes and stability in the Black Sea/Caspian region, economic cooperation and development, and security cooperation.[21] Member States emphasised the potential of the organisation to become a trade bridge between East and West (in particular through cooperation in the energy field and the creation of a free trade area), and to have a role in security cooperation, namely with regard to the protracted conflicts on the territory of the former Soviet Union. The summit declaration advocated reintegration of the breakaway territories and peaceful coexistence of different ethnic groups in the respective states. GUAM also supported Georgian President Saakashvili's peace plan for South Ossetia and the Yushchenko Plan for Transnistria, and called upon OSCE member states to insist on the withdrawal of Russian troops from Moldova and Georgia. They highlighted their will to closely cooperate and support each other in the *rapprochement* with the EU, NATO and the US. In order to achieve these goals, the declaration concluded, GUAM should be transformed into a 'regional organisation aiming at democracy and development.'[22]

One year later, the GUAM Summit in Kyiv adopted the statute of the 'Organisation for Democracy and Development – GUAM'.[23] The summit triggered a debate about the creation of collective peacekeeping forces and civil policy units to be utilised in the conflict-resolution processes.[24] The organisation also set up a group of anti-terrorism experts from the security services of the member states and a 'Virtual Centre for Information Exchange in the Combat of Organised Crime.'[25] A further step towards the institutionalisation of the organisation was the creation of a General Secretariat in Kyiv during the first half of 2007.[26] Both the statute itself and measures undertaken following the summit

20. GUAM was founded by Georgia, Ukraine, Azerbaijan and Moldova in 1997. Uzbekistan joined in 1999 and withdrew its membership in 2006. Therefore the organisation will be referred to as GUAM (and not GUUAM) throughout this chapter.

21. Kommyunike Sammita GUAM [GUAM Summit Communiqué], 22 April 2005: www.guam.org.ua.; 'Chishinevskaya Deklaraciya glav gosudarstv GUAM' [Chisinau Declaration of the Heads of States of GUAM] 'Vo imya demokratiy, stabilnosti i razvitiya' [In the Name of Democracy, Stability and Development], 22 April 2005: www.guam.org.ua. See also 'Foreign and Security Policy', in '100 Days of the New Authorities: A View of Non-Governmental Think Tanks', *National Security and Defence*, no. 5/2005, p. 46.

22. 'Chishinevskaya Deklaraciya glav gosudarstv GUAM', op. cit. in note 21; 'Vo imya demokratii, stabilnosti i razvitiya', Chishinau, 22 aprelya 2005: www.guam.org.ua.

23. Ustav Organizacii za demokraciyu i ekonomicheskoe razvitie [Charter of the Organisation for Democracy and Economic Development]: www.guam.org.ua.

24. '100 Days of the New Authorities', op. cit. in note 21, p 56.

25. Author's interview in Kyiv, June 2007.

26. Author's interviews in Kyiv, June 2007.

revealed a change of priorities, shifting the initial emphasis on economic cooperation to political and security matters.[27]

GUAM members started to coordinate their policies on the international level. The organisation has observer status with the General Assembly of the United Nations and is currently trying to gather support for a resolution of the UN General Assembly on the protracted conflicts.[28] A similar strategy is used within the OSCE and the Council of Europe, where GUAM members coordinate their positions and speak for each other. GUAM also strives to build closer relations with the EU and NATO, as well as with individual EU and NATO member states. While both NATO and the EU are hesitant to enter into an official exchange with GUAM,[29] individual member states are showing signs of more openness to GUAM's aspirations, as demonstrated for example by Polish President Lech Kaczynski when visiting the 2007 GUAM Summit in Baku.[30]

The Ukrainian leadership's efforts to revive GUAM infused GUAM with a new dynamic. However, this development was inhibited by a number of factors. The withdrawal of Uzbekistan after the events in Andijan and its reorientation towards Russia demonstrated the impact Russia still exerts on developments in the region of which it does not approve.[31] Chisinau, under strong economic pressure due to Russian bans on Moldovan agricultural produce, has visibly reduced its engagement in GUAM recently and intensified contacts with Moscow. Rumours about a new Russian initiative for the regulation of the conflict in Transnistria, bypassing other external actors as well as Ukraine, were circulating in the months before the Baku summit. Moldovan President Voronin did not attend the summit, but went to Moscow instead in order to discuss conflict settlement in Transnistria.[32] It is difficult to forecast whether Moldova will follow the Uzbek example. In any case, the latest developments demonstrate how easily GUAM is sidelined by its member states. GUAM states also have experienced great difficulties in agreeing upon the details of cooperation. As a result, most plans to establish common security structures have not got beyond the drawing board stage and the GUAM agreement on free trade has not led to a significant increase in the volume of trade between member states. The organisation is further weakened by the fact that Ukraine as a key member has still not ratified its statute. Considering the domestic stalemate in Ukraine, this is unlikely to change in the near future.

27. Ustav Organizacii za demokratiyu i ekonomicheskogo razvitiya – GUAM, Kyiv, 23 May 2006: www.guam.org.ua. Kievskaya Deklaraciya o sozdanii Organizacii za demokratiyu i ekonomicheskoe razvitie – GUAM [Kyviv Declaration on the Creation of the Organisation for Democracy and Economic Development], Kyiv, 23 May 2006: www.guam.org.ua.

28. Author's interviews in Kyiv and Tbilisi, June/July 2007. Kommyunike Bakinskogo sammita GUAM [Baku Summit Communiqué], 19 June 2007: www.guam.org.ua.

29. Despite repeated invitations, neither the EU nor NATO have so far sent official delegations to GUAM summits. Author's interviews in Kyiv, June 2007.

30. Other non-GUAM members participating in the summit were Bulgaria, Estonia, Latvia, Lithuania, Romania, the US and Japan. 'Kommyunike Bakinskogo sammita GUAM', 19 June 2007: www.guam.org.ua.

31. 'GUAM teryaet bukvu' [GUAM loses a letter], *Zerkalo Nedeli*, no. 17(544), 13 May 2005: www.zn.ua.

32. Svetlana Gamova, 'Pridnestrovskaya ruletka' [Transnistrian Roulette], *Nezavisimaya Gazeta*, 27 June 2007: www.ng.ru.

The Community of Democratic Choice (CDC), also a Ukrainian-Georgian initiative, faced even bigger problems in its development. It was launched as a loose alliance of states including the Baltic countries, Ukraine, Moldova, Georgia and some South-East European countries (among them Romania), aiming at democracy, good governance, regional integration and *rapprochement* with the EU.[33] The initiative fizzled out soon after the first Summit in Kyiv in December 2005. There were only two more gatherings in 2006, organised by Lithuania and Romania, and no follow-up on the proposals discussed during the Kyiv summit. The last meeting did not even take place under the specific aegis of the CDC, but was merged by the Romanian organisers with a wider Black Sea initiative. In the words of a Ukrainian observer, CDC became both a victim of the weakness of Ukrainian foreign policy-making and the competition between Ukraine and Romania for regional leadership. Lack of support from the EU and NATO provides another reason for the initiative's failure.[34]

Transnistria – two steps forward, one step back?

From 1993 on, Ukraine had been involved in the so-called five-sided format, consisting of Russia, Ukraine and the OSCE as mediators and Moldova and Transnistria as conflict parties. Kyiv also has observer status with the Russian-Moldovan-Transnistrian peacekeeping forces. The Kuchma administration did not pursue a proactive approach with respect to the resolution of the conflict. Too many interests closed ranks to oppose any engagement that would have the effect of changing the *status quo*: Ukrainian business circles benefited from shadow trade and smuggling on the Ukrainian-Transnistrian border, and the political elite in Kyiv had no interest in conflicts with Russia over Transnistria.

This changed radically after the Orange Revolution. During the GUAM Summit in April 2005, Viktor Yushchenko launched a seven-point proposal for the Transnistrian-Moldovan conflict under the title 'To Settlement through Democracy'. This first draft contained all the aspects characterising the Ukrainian approach – and its shortcomings. Its key elements were: the democratisation of Transnistria; early elections to be held in Transnistria under the observation of the EU, the OSCE, the Council of Europe, Russia and the United States; closer involvement of the EU and the US in the negotiation process; transfor-

33. Borjomi Declaration, 12 August 2005: www.president.gov.ge.

34. Author's interview in Kyiv, June 2007.

mation of the (Russian) peacekeeping forces into an international mechanism of military and civilian observers under the aegis of the OSCE; the setting up of an observation mission to military-industrial enterprises in the region; and the monitoring of the Moldovan-Ukrainian border by OSCE teams from Ukrainian territory.[35]

The final version of the Yushchenko Plan was published one month later. It foresaw the reintegration of Transnistria as an autonomous entity with a 'special status' within 18 months. While Moldova was supposed to remain the sole subject of international law, Transnistria should have its own constitution, insignia, and the right to participate in foreign policy-making in matters affecting its interests. The plan reiterated the idea of early elections under international observation. It named Russia, Ukraine and the OSCE as guarantors of the settlement, who should, with the support of the EU and the US, work out an agreement on the special status of Transnistria.[36]

Yushchenko's initiative met with mixed reactions. A declaration of the Moldovan Parliament approved the plan in principle, at the same time expressing grave concerns. It pointed out that the Ukrainian proposal had not considered 'some settling principles, including those concerning: withdrawal of the Russian troops; demilitarisation, principles and conditions to democratise the zone; establishing of a transparent and legal control of the Transnistrian segment of the Moldovan-Ukrainian border'.[37] The declaration emphasised that the Plan endangered Moldovan sovereignty in conceding to Transnistria the right to have its own constitution, foreign policy and insignia. It expressed serious doubts as to whether free and democratic elections would be possible 'in conditions where the Constitution of the Republic of Moldova and international democratic standards are disregarded, political pluralism and freedom of expression are lacking, and manifestation of an attitude different from the imposed one is repressed.'[38] Instead, the Parliament claimed that democratisation in Transnistria should be viewed as a longer-term process and supervised by the international community. It also demanded stronger involvement of the EU than the Ukrainian plan had envisaged.

The EU displayed cautious openness with regard to a deeper involvement in the peace process. As a consequence it obtained, together with the US, observer status in the five-sided negotiation format (which has evolved since then to 5+2) as of September

35. Vladimir Socor, 'Poroshenko drafts, Yushchenko launches a plan for Transnistria', *Jamestown Foundation Monitor*, 27 April 2005.

36. 'Ukrainian Plan for settling the Transnistrian conflict', unofficial translation, May 2005. Jan Maksymiuk, 'Kyiv's Plan for Transnistria Gets Mixed Receptions', *RFE/RL Belarus and Ukraine Report*, 6 June 2005.

37. Decision on the Ukrainian Initiative Concerning the Settlement of the Transnistrian Conflict and Measures for Democratisation and Demilitarisation of the Transnistrian Zone, Chisinau, 10 June 2005; Annex 1: Declaration of the Parliament of the Republic of Moldova on the Ukrainian Initiative Concerning the Settlement of the Transnistrian Conflict.

38. Annex 2: Appeal of the Parliament of the Republic of Moldova on the Criteria of Democratisation of the Transnistrian Zone of the Republic of Moldova.

2005. In October 2005 Brussels launched the EU Border Assistance Mission (EUBAM) on the Moldovan-Ukrainian border, dispatching 60 EU customs and police experts to monitor the Transnistrian stretch of the border and advise local police and customs services.[39]

In December 2005 Ukraine and Moldova concluded an agreement on customs procedures for trade with Transnistria. Under this agreement, Ukraine committed itself to accepting Transnistrian goods only after certification by the Moldovan customs service. The measure aimed at depriving business circles not only in Transnistria, but also in Moldova, Ukraine and Russia, of the possibility of (re)exporting goods to Ukraine without paying taxes to Chisinau. Such exports made up a large part of Transnistrian revenues and, thus, had provided the economic basis of the breakaway regime in Tiraspol. While there had been similar agreements between Moldova and Ukraine before, implementation seemed to be more realistic with the Yushchenko government, given its proactive approach towards conflict settlement. However, Kyiv was slow in implementing the agreement, and massive EU pressure was needed to secure its entering into force. In summer 2006, a report by the International Crisis Group stated that 'the new customs regime is a bitter political pill for the Transniestrian regime, but only that; it does little economic damage', since it is not used by the external actors – including Ukraine – to put economic pressure on Transnistria.[40]

Internal turmoil played a decisive role for the development of Kyiv's Transnistria policy: the mastermind behind the early Transnistria policy of the new government was Petro Poroshenko, then General Secretary of the National Security and Defence Council. Apparently Poroshenko was in close contact with Moscow, possibly the reason for the predominant role ascribed to Russia in the plan.[41] This approach was heavily criticised by Yulia Tymoshenko, Petro Poroshenko's main domestic adversary. After both Poroshenko and Tymoshenko had been dismissed from the government in September 2005, conflict settlement slipped down the agenda. Elections in March 2006 and Yanukovich's return as Prime Minister brought the initiative to a complete standstill.

To sum up, the Orange Revolution created a temporary momentum in negotiations about the Transnistria conflict. Changes in the setting of the negotiation process as well as in the context of the conflict were the most important successes of the

39. Nicu Popescu, 'The EU In Moldova - Settling conflicts in the neighbourhood', *Occasional Paper* no. 60 (Paris: EUISS, October 2005), p. 11. The staff of EUBAM was doubled to 120 officers in 2007.

40. International Crisis Group, 'Moldova's uncertain future', *Europe Report* no. 175, 17 August 2006, p. 9.

41. Vladimir Socor, 'Poroshenko drafts', op. cit. in note 35.

Ukrainian initiative. The involvement of the EU and the US, and the successful employment of EUBAM, are clearly the result of the Ukrainian leadership's increased activities – and they continue. The same holds true for the Moldovan-Ukrainian border agreement and its – albeit limited – economic and political influence on Transnistria. However, one year after Yushchenko had first launched his 'To Settlement through Democratisation' initiative, the Ukrainian attempt at conflict resolution had lost momentum. Many of the suggestions made at the GUAM Summit in April 2005 and later on in the Yushchenko Plan for Transnistria were not taken up again, and the Ukrainian leadership quickly seemed to lose its grip on the issue. Kiyv's reluctant stance on the implementation of the customs agreement with Moldova can be seen as the result of internal pressure by actors interested in the maintenance of the *status quo* in trade relations with Transnistria. Against the backdrop of an unfolding internal crisis, these forces were obviously strong enough to block a more constructive policy on Transnistria.

Ukrainian-Russian relations after the Orange Revolution

Ukraine and Russia have a long and difficult common history. The two countries are linked through political and economic interdependencies as well as cultural, historical and language bonds. Changes in Russian-Ukrainian relations have been triggered not only by the Orange Revolution, but also by the transformation of Russian foreign policy after 2000. During the first half of the 1990s, relations between Russia and Ukraine were greatly affected by the problems resulting from the dissolution of the Soviet Union.[42] The 1997 Russia-Ukraine treaty temporarily regulated some of the issues at stake. However, many questions remained unresolved and were at the root of recurring tensions.

Ukraine's policy towards Russia: from a multi-vector approach to a multiplicity of approaches

Before 2005, Ukraine's approach towards relations with Russia was shaped by the Ukrainian government's 'multi-vector' policy. It unfolded against a regional background very different from today's: the EU had only just started to develop an independent

42. The most important of these revolved around the following questions: the status of the Black Sea Fleet, the question of Soviet property, the handling of Soviet nuclear weapons deployed on Ukrainian territory, the delineation and demarcation of the borders between the two countries.

policy towards the former Soviet Republics. The process of Eastern enlargement was in its infancy and absorbed most of Brussels' energy and attention. Russia was a weak player, paralysed by internal transformation processes. Political and economic crises, culminating in financial breakdown in autumn 1998, forced Russian policymakers to concentrate on internal matters and prevented them from pursuing a more assertive policy in the CIS.

In this specific situation, Ukraine reluctantly responded to Russia's attempts to create new institutional bodies on the territory of the former Soviet Union by only partly joining the CIS and related organisations and keeping its commitment at the lowest possible level. While Russia regarded the CIS as a vehicle to maintain tight links with its newly independent neighbours and to promote its interests, 'Ukraine's preferred option for the CIS (...) was that it became a body to help with the transition from former Soviet status to European statehood.'[43] From this perspective, the CIS provided a mechanism for the peaceful completion of the dissolution of the Soviet Union. Accordingly, Kyiv throughout the 1990s steadfastly declined any measures leading to deeper integration, including the idea of providing the CIS or related organisations with a supranational dimension. At the same time, Kyiv pursued a strongly Western-oriented policy, aiming at *rapprochement* with the key political institutions and becoming a member of the European political and economic community.

However, regional developments in recent years have changed Ukraine's situation profoundly. Following their enlargement processes, NATO and the EU now join borders with Ukraine. This has changed the political, economic and societal balance of Ukraine's relations with its western neighbours. Russia, on the other hand, has become increasingly sensitive concerning the EU's and NATO's influence on Ukraine and the post-Soviet space in general. By 2004, Ukraine found itself in the centre of a growing battle for influence between Russia on the one hand, and the EU on the other. This uncomfortable position made it ever more complicated for Kyiv to pursue a policy aiming at a balance between crucial (economic) relations with Russia and the political will to integrate with Western Europe.

At the same time, Brussels sent out more or less clear signals depriving Ukraine of a membership perspective. With the inauguration of the European Neighbourhood Policy (ENP) in 2002, it was made clear to Kyiv in cold print that it was destined to become

43. Roman Wolczuk, 'Ukraine – A Partial, but Reluctant CIS Member', in David Dusseault (ed.), 'The CIS: Form or Substance?', *Aleksanteri Papers* 2/2007, Aleksanteri Institute, University of Helsinki, pp. 131-49, p. 133.

part of the 'ring of friends' around the EU rather than a member of the club itself. At the same time, Ukraine was shaken by domestic scandals, shedding glaring light on the regime's endemic corruption and entanglement with organised crime. Growing isolation in relations with the EU and the US, and the need to secure assets as Kuchma's second term was coming to an end, led the regime to seek the Kremlin's support in the run-up to the December 2004 presidential elections.

The rest of the story is well-known and does not need to be repeated here. As will become clear in the following sections, the new Ukrainian leadership did not succeed in developing a new foreign policy strategy responding to the changes in the country's regional environment. Rather, foreign policy debates split in different camps which are still today unable to reconcile their views and merge the nation's interest in constructive relations with Russia with further *rapprochement* with the EU.

Russia's policy in the CIS: back to assertiveness

The coming to power of Vladimir Putin in 1999/2000 ushered in profound changes in Russia's foreign policy. The earthquake of the financial and economic crises in 1998 had sharpened the new Russian leadership's awareness that any foreign policy should aim at internal political and economic consolidation first, before striving for more ambitious goals on the international stage. The new leadership regarded Western Europe and the US as the most important partners for Russia's modernisation and integration into the global economy. The Kremlin quickly set out to bridge the gap between Russia and 'the West' caused by the 1999 Kosovo war.

The – increasingly authoritarian – consolidation of the Russian state was accompanied by the reorganisation and professionalisation of foreign policy-making. After the turmoil of the late 1990s, the government regained control over the decision-making process, and started to act more homogenously. From 2003 on, this process was accompanied by the emergence of a new self-confidence, which manifested itself in 2005 in the idea of 'sovereign democracy.'[44] Based on its energy wealth and growing financial independence from Western and international donors, Russia reclaimed a position as a global player and demanded to be treated as an equal partner.

44. Vyacheslav Surkov, 'Eto politicheskyj sinonim konkurentosposobnost' [Sovereignty is the political synonym for competitiveness], in Nikita Garadzha (ed.), *Suverenitet* (Moscow: Evropa, 2006), pp. 43-79, p. 72.

These shifts in Russia's attitudes towards the outside world also affected the Newly Independent States (NIS). Russia's policy towards its neighbourhood can be divided into two phases. From 2000 to 2004, Moscow tried to foster closer cooperation and integration between the NIS under Russian guidance. Instead of strengthening the CIS, which was perceived as increasingly dysfunctional, the Kremlin created new integration structures.[45] The goal of this reactivated regional policy was a unified economic space, a 'Eurasian integration model', which aimed at providing the NIS with a viable alternative to European integration processes.

The second phase of Russia's policy towards its neighbourhood after 2000 is closely connected with the 'colour revolutions' in Georgia and Ukraine. It reflects Russian policymakers' perception of these events, and the lessons they drew from them. The Orange Revolution provoked harsh reactions among Russia's political elite, anti-revolutionary paranoia and a feeling of besiegement. The events in Ukraine were basically interpreted as the result of Western (primarily US, but also EU) activities aiming at overthrowing Russia-friendly governments in the former Soviet Union and changing the balance of power in the region. The ultimate goal of this hidden agenda, as suspected by many observers and decision-makers in Moscow, was to induce a similar development in Russia proper, which would provide the 'West' with the opportunity to gain control over the country and its energy wealth. In 2005, after EU enlargement and the Orange Revolution, Russia was faced with the EU's growing significance in its zone of influence and with new governments in some NIS trying to shake off Russian dominance.[46] This perception led to Moscow adopting an increasingly assertive stance towards the region. Moscow refocused its integration efforts on those countries, which displayed – albeit limited – interest in closer cooperation. In its relations with 'deviant' states like Ukraine and Georgia, Russia retreated to a policy of economic pressure, linked with political threats.

The instruments used in this struggle for influence ranged from embargos on vital goods from these countries (wine and agricultural produce from Moldova, wine and mineral water from Georgia) and the exploitation of energy dependence to increased support from Moscow for the regimes in the breakaway regions in Georgia and Moldova. This does not imply that 'the Kremlin' dis-

45. The most important organisations created in this period are the Eurasian Economic Union and the Single Economic Space. Russia also reactivated the Collective Security Treaty of the CIS, which was transformed into the Collective Security Treaty Organisation in 2001.

46. See also Vsevolod Samokhvalov, 'Relations in the Russia-Ukraine-EU triangle: "zero-sum game" or not?', *Occasional Paper* no. 68 (Paris: EUISS, September 2007).

poses of full control over Russian economic actors like Gazprom or ruling elites in Transnistria, Abkhazia and South Ossetia, to the extent that it can utilise them deliberately against Kyiv, Chisinau or Tbilisi. However, where interests overlap, strong pressure on the respective governments emerges, as was already demonstrated in the case of Moldova's involvement in GUAM.

Basically, the colour revolutions confronted Moscow with the failure of its 'soft power' policy, aiming at the creation of an alternative integration model, which would ultimately draw the NIS back into Russia's orbit. In reaction to this, Moscow returned to bilateralism in its relations with its neighbours, using informal political and economic elite networks to maintain its influence, and exerting massive economic pressure where this influence was imperilled.

Celeste Wallander has coined the term 'transimperialism' to describe this *volte face* in the economisation of Russian foreign policy in the early Putin years. Against the background of an increasingly authoritarian political system based on control and the distribution of rents between patron and client, Russia has to find ways to integrate into the global economy without endangering the position of its ruling elites. According to Celeste Wallander, it resorts to transimperialism, which 'is the extension of Russian patrimonial authoritarianism into a globalized world. Russia can trade and invest without being open and permeable by selectively integrating transnational elite networks in the globalized international economic system and replicating the patron-client relations of power, dependency, and rent-seeking and distribution at the transnational level.' Thus, 'Russia can live with the Yushchenko government, for example, as long as Ukraine's internal political economy is sufficiently patrimonial and corrupt to prevent transatlantic standards of transparency and rule of law in its commercial dealings with Russia.'[47]

As will be demonstrated in the following section, transimperialism was indeed a strong determining factor in Ukrainian-Russian relations after the Orange Revolution. However, changing attitudes among Ukraine's political and economic elites put constraints on Russia's ability to use this leverage This implies a chance not only of protecting Ukraine against Russia's burgeoning transimperialism, but also of abolishing transimperialism as an instrument altogether, thus making Russia's (re)integration into a wider European community a possible option.

47. Celeste A. Wallander, 'Russian Transimperialism and Its Implications', in *The Washington Quarterly*, Spring 2007, pp. 107-121, pp. 118-19. 'Transimperialism is a form of geopolitics through commercial relationships and transnational patron-client relationships.'

Ukraine and Russia in the wake of the Orange Revolution

The success of the Orange Revolution came as a shock to Russia's policymakers. Moscow had expected neither the determination of the opposition movement nor the weakness of the Yanukovich camp it had supported so openly during the election campaign. The EU's cohesive support for democratic procedures in the Ukrainian elections was the third unwelcome surprise for Moscow. During the first months after the events on Maidan Nezalezhnosti, Russian policy towards Ukraine seemed to be paralysed by this threefold trauma.

Although Yushchenko paid his first foreign visit to Moscow two days after his inauguration in order to indicate that Russia remained of the utmost importance for his government, relations between the two countries remained chilly. New mechanisms for bilateral dialogue were created soon after the elections, but it took until the end of 2006 before they became operational.[48] Direct contacts between the heads of states remained sporadic. After the gas crisis in January 2006, meetings between the heads of government were interrupted for over a year.[49] Although verbal commitments attesting to the importance of good relations were exchanged between Kyiv and Moscow, old and new conflicts were simmering away beneath the surface.

The Ukrainian-Russian gas crisis

The most dramatic events were linked to the gas crisis in the winter of 2005/2006.

During the 2005 negotiations between Ukraine/Naftogaz and Russia/Gazprom on the conditions of gas supply to and the transfer of gas through Ukraine, Gazprom suggested a significant price increase (starting from $160 per tcm in summer to $230 per tcm in December 2005) as well as the transition from barter to cash payment.[50] The parties were not able to reach a compromise by the end of December 2005. Gazprom followed through with its threats and interrupted gas deliveries to Ukraine on 1 January. In reaction, Ukraine temporarily siphoned gas from the transit pipelines in order to secure its energy supply. Gas deliveries to the EU were affected for the first time ever since energy trade had started between the then Soviet Union and Western Europe. Under conditions of extreme pressure and opacity, an agreement was hammered out by 4 January 2006. The new contract provided a short-term solution for both sides, but had severe long-term implications for Ukraine's

48. In May 2005 the Ukraine-Russia Interstate Commission was created and replaced the dysfunctional Mixed Russian-Ukraine Cooperation Commission. It is headed by the two presidents and involves a wide range of government officials from both sides. Valeryi Chalyi, 'Ukraina-Rossiya: ne medovye 100 dnej' [Ukraine-Russia: 100 days have not been a Honeymoon], *Zerkalo Nedeli*, no. 18(546), 14-20 May 2005.

49. '240 days of government activity in the new format', *National Security & Defence*, Razumkov Centre, Kyiv, no. 3, 2007, p. 72.

50. The idea to end the barter of gas supplies and transport services had also been put forward by the new Ukrainian leadership as a way to reduce Ukraine's energy dependency. For the contractual basis of Russian-Ukrainian energy trade before the 4 January 2006 gas agreement, see Aleksandr Chaliy, 'Ukrainsko-rossiyskoe gazovoe soglashenie: putevoditel' k protivodeystviyu' [Ukrainian-Russian Gas Agreement: A Guide to Resistance], *Zerkalo Nedeli*, no. 1(580) 14, 14-20 January 2006.

position *vis-à-vis* Russia. It introduced Swiss-based RosUkrEnergo as an intermediate trader, and separated Ukrainian domestic supply from the transit of Russian/Central Asian gas through Ukraine to Western Europe. Gazprom accepted full cash payment for transit, with fees fixed for five years. The more problematic aspects of the agreement, however, concerned the role of RosUkrEnergo and UkrGazEnergo. RosUkrEnergo became the main operator of Ukrainian gas imports, buying Russian gas from Gazprom (at near market prices) and Central Asian gas (at lower prices) and selling a mix of both at an intermediate price to UkrGazEnergo, founded in February 2006, for domestic distribution.[51]

The emergence of two new actors in Russian-Ukrainian energy relations weakened the Ukrainian gas company Naftogaz Ukrainy. Its right to re-export Russian gas, as well as to cover domestic supply, was abrogated, which severely damaged the profitability of the company.[52] 'Some Ukrainian observers consider that the 4 January agreements have as their ultimate objective to bankrupt Navtogaz, which would facilitate the gas export pipeline's buyout by its indirect creditor – Gazprom.'[53] The lack of transparency not only of the negotiation process, but also of the actions of RosUkrEnergo and UkrGasEnergo, and the involvement in them of different Russian and Ukrainian business circles, deprived the Ukrainian state of any control over energy trade. Not only did the government lose its grip on domestic distribution and the re-export of Russian gas, conceding a virtual monopoly of Ukraine's gas supply to RosUkrEnergo and UkrGasEnergo. It also lost its say in the exact determination of the mix of Russian and Central Asian gas eventually delivered to Ukraine. Last but not least, and unlike the transit fees paid by Russia, the gas price charged by RosUkrEnergo is not fixed, but has to be renegotiated on a yearly basis.[54] Observers therefore called the agreement the 'Pearl Harbour' of Ukrainian energy diplomacy. It was seen as a major blow to Ukrainian 'energy sovereignty', one of the central goals proclaimed by the Orange Coalition.

What does the 2006 energy crisis reveal about Ukrainian-Russian relations?

As for Ukraine, events around 4 January 2006 showed that, despite the new leadership's commitment to the fight against corruption and energy dependency, there were still many influential actors interested in the maintenance of the *status quo* in energy relations with Russia. The blurred and unclear circumstances of

51. Margarita Balmaceda, 'Fatal Attraction: Rents of Dependency, Energy Dependency and the Yushchenko Presidency', unpublished paper presented to the Danilyw Research Seminar in Contemporary Ukrainian Studies, University of Ottawa, 12-14 October 2006, pp. 17-19. Arnaud Dubien, 'The Opacity of Russian-Ukrainian Energy Relations', *Russie.Nei.Visions* no. 9, May 2007, pp. 11-12.

52. Balmaceda, op. cit. in note 50, p. 18.

53. Dubien, op. cit. in note 50, p. 12.

54. It was maintained at $95 per tcm in 2006 and increased to $130 per tcm for 2007. Gazprom demands its adaptation to international gas prices by January 2008.

energy trade between Russia and Ukraine had provided Ukrainian business groups with boundless rent-seeking possibilities and thus had made the Ukrainian gas sector a 'magnet for corruption.'[55] These groups had a vital interest in maintaining a *status quo*, which guaranteed the continuation of energy rents. Actors supporting the precarious *status quo* were to be found in all political camps, although the Party of Regions probably benefited more as the gas crisis strengthened its position in the political system and contributed to Yanukovich's return to power. In other words, distorted energy relations had and still have a strong impact on the development of the Ukrainian political system, including Ukrainian foreign relations.

The Russian-Ukrainian energy crisis is also very telling with regard to Russia's approach towards Ukraine (and other NIS) after its humiliating defeat during the Orange Revolution. While Moscow obviously gave up openly interfering with domestic processes, Russian political and economic interest groups continue to shape developments in Ukraine to their own advantage. In the case of energy relations, Russian actors made use of shadow deals and opaque and corrupt energy sector structures in order to strengthen their economic influence. This economic impact can occasionally translate into political leverage. Thus, Gazprom softened its stance during the renegotiation of gas prices after Prime Minister Yanukovich had categorically denied any intention by Ukraine to join NATO during a visit to Brussels in autumn 2006. Its attitude became again more assertive after the inauguration of the new Tymoshenko government, and especially after the President, Prime Minister and Speaker of Parliament jointly published a letter calling for NATO to provide Ukraine with a Membership Action Plan at the Bucharest Summit on 18 January. The Russian energy sector should not be seen as a foreign policy tool under full control of the state.[56] In the case of energy relations with Ukraine, however, the state's interest in political control and the energy companies' desire for expansion of their assets and control of the pipeline systems in the CIS merged in an 'unholy alliance.'

Interpretations of the Ukrainian-Russian gas crisis in 2005/2006 abound, varying considerably in their assessment of the events. Some observers saw it basically as part of the economisation of Russian foreign policy and Gazprom's strategy to rationalise energy relations with the other NIS by increasing energy prices to world market level. According to this reading, Russia

55. Margarita Balmaceda, 'Rents of Energy Dependency, "Rent-Seeking Swamps", and Political Development: The Ukrainian Case in Comparative Perspective', unpublished conference paper, Berlin 2006, p. 24.

56. Andreas Wenger, 'Russian business power as a source of transnational conflict and cooperation', in Andreas Wenger, Jeronim Perovic, Robert W. Orttung (eds.), *Russian Business Power. The role of Russian business in foreign and security relations* (London and New York: Routledge, 2007) pp. 1-21.

rightfully aims at abolishing subsidies it had continued providing for 15 years after the breakdown of the Soviet Union. Others perceived it as a further illustration of Kremlin-led (and controlled) Russian neo-imperialism aiming at the restitution of total control over the post-Soviet territory – with the Ukrainian reform camp being victimised by a conspiracy of anti-reform forces in Kyiv and the Kremlin.

The reality of Ukrainian-Russian relations is more complex. In the energy sector transnational elite networks, operating partly or fully in the dark, shape economic and to a considerable extent also interstate relations between Russian and Ukraine. In such a constellation, it is impossible to distinguish between 'good' and 'bad', between 'pro-reform' and 'counter-reform', and ultimately between 'democratic' and 'anti-democratic' forces among business and political elites in Ukraine. The temptation to gain rents in a corrupt and intransparent energy sector still seems too strong for actors in all camps; they are all exposed to the risk of being drawn back into what Margarita Balmaceda calls 'rent-seeking swamps', undermining any coherent political or economic reform effort in the country. Hence, what started – at least nominally – as an effort to transform energy trade according to market rules, ended up in a shadow structure prone to corruption and inhibiting internal reforms in Ukraine.

The 2006 gas deal is an eloquent example of Russian transimperialism. However, this approach can only be successful if it falls on fertile ground in the countries Russia deals with. Obviously, the Orange Revolution has not led to the abolition of patrimonial elite structures in Ukraine, and after the return to power of the Party of Regions, these structures may have become even stronger again. This provides the Russians with a toehold enabling them to penetrate the political and economic system of their neighbour state. It remains to be seen whether the new Orange Coalition will be able to take effective action against these structures.

The Black Sea Fleet

The Black Sea Fleet, deployed at the Ukrainian port of Sebastopol on the Crimean peninsula, is another bone of contention between Ukraine and Russia. In the early 1990s, violent conflict seemed to be quite likely when pro-Russian forces in the Crimea were on the rise and won support from nationalist parties in Moscow.[57] The

57. The Russian Duma, dominated by nationalist parties, adopted several resolutions declaring the transfer of Crimea to Ukraine by Khrushchev illegal and Sebastopol to be a Russian city.

disagreement was settled in the Russian-Ukrainian treaty of 1997, which regulated the use of the Sebastopol port by parts of the Russian fleet until 2017. However, the modalities of the implementation of this agreement constitute a constant source of tension between Moscow and Kyiv.

At first sight, most disputed issues seem to be of a mostly technical character, like the status and functioning of Russian military courts in the Crimea, inspections of the fleet by Ukraine, environmental problems caused by the fleet etc.[58] Nevertheless they are closely linked to the question of the status of the Crimea and of Russian-Ukrainian cooperation on Ukrainian soil, and ultimately challenge Ukraine's sovereignty.[59]

Matters related to the deployment and management of the Black Sea Fleet are being negotiated in the framework of the Interstate Commission.[60] However, the Russian side employs a two-pronged tactic with regard to the BSF: while Russian negotiators demonstrate relative willingness to compromise on less important matters and thus ensure the continuation of this dialogue, Moscow tries to keep the discussion of more strategic issues on a higher political level and regularly links them with other relevant topics, like energy and economic relations.[61] The most blatant example of this was President Putin's suggestion in October 2006 to extend the presence of the BSF in Sebastopol beyond 2017 'at the Ukrainian leadership's request'.[62] Leaving aside the President's ultimate intention, the heterogeneity of Ukrainian reaction(s) clearly played into Moscow's hand: President Yushchenko immediately rejected the Russian 'suggestion', pointing at the fact that the Ukrainian constitution prohibits the presence of foreign troops on Ukrainian territory. Prime Minister Yanukovich ambiguously stated that the question would be subject to negotiations and depended on Ukrainian and Russian interests.[63] The Rada, dominated by supporters of Yanukovich's Anti-Crisis Coalition, during the same period refused to approve the creation of a commission to monitor the withdrawal of the BSF until 2017.[64]

Russia's policy also shapes the context of the BSF issue, which is closely linked to the status of the Crimea. It is not too far-fetched to speculate that the anti-NATO/anti-American demonstrations against NATO's Sea Breeze exercise in Crimea in June 2006 enjoyed strong Russian support.[65] Policymakers and deputies belonging to the Russian extreme right pay visits to the peninsula on a regular basis. Again, the fact that there are deep divisions

58. Vladimir Kravchenko, 'Cena prolongacii' [The Price of Extension], in *Zerkalo Nedeli*, no. 42 (621) 4-10 November 2006: www.zn.ua.

59. Elena Kovalova, 'Ukraine's Role in Changing Europe', in: Daniel Hamilton and Gerhard Mangott (eds.), *The New Eastern Europe: Ukraine, Belarus, Moldova* (Washington D.C.: Center for Transatlantic Relations, 2007), pp. 171-94.

60. See the description of the institutional mechanisms of bilateral dialogue at: www.mid.ru.

61. Vladimir Kravchenko, op. cit. in note 57.

62. Vladimir Socor, 'Putin Offers Ukraine "Protection" for Extending Russian Black Sea Fleet's Presence', The Jamestown Foundation, *Eurasia Daily Monitor*, vol. 3, issue no. 200, 30 October 2006, available at: www.jamestown.org. See also Vladimir Kravchenko, 'Chto ranshe bylo na ume, to teper' u Putina na yazike' [What has been in their minds previously, is now on Putin's tongue], in *Zerkalo Nedeli* no. 41 (620), 28 October-3 November 2006, www.zn.ua.

63. '240 Days of the Government Activity in the New Format', Razumkov Centre, *National Security & Defence*, no. 3, 2007, p. 72, op. cit. in note 49.

64. Vladimir Kravchenko, op. cit. in note 62.

65. Author's interview in Kyiv, June 2007.

within the Ukrainian political elite provides Moscow with manifold opportunities to influence domestic developments in the neighbouring country. Many of the Russian actions exacerbate the gaps between Ukrainian policymakers by putting forward far-reaching and provocative (and indeed often unviable) suggestions. A serious separatist movement in the Crimea is much less likely nowadays than it was at in the early 1990s. However, the fact that the Ukrainian political elite are so divided on the issue and the delay of solutions to ongoing problems regarding the BSF safeguards Moscow's leverage. Echoing the Russian attitude towards the protracted conflicts in Moldova and the South-Caucasus, Moscow is quite comfortable with the continuance of a *status quo* that allows it to exert political pressure on Ukraine.

The Single Economic Space

Ukraine's involvement in the Single Economic Space (SES) has also been a determining factor on the agenda of Russian-Ukrainian relations since the Orange Revolution. Through the creation of the SES in 2001-2003, Russia had aimed at drawing Ukraine closer into its own orbit.[66] The Kuchma administration, however, had refused to become deeply involved in this project and limited its engagement to the concessions necessary to assure Moscow's support in the pre-election campaign 2003/2004. From the very beginning, Ukraine was not prepared to go beyond a free trade area with the other three member states and agreed to participate in only a small number of the agreements signed in the framework of the SES.

After December 2004, expectations that the new Ukrainian government could be induced to embrace closer integration within this framework seemed to be even more doomed. The new leadership continued the attitude of the Kuchma administration and showed no willingness to move beyond it. Some of its supporters even saw a free trade zone among SES countries as being in contradiction with Ukraine's interest in quick integration with the EU.[67] Yanukovich's gradual return to power in 2006 raised hopes in Moscow that Ukraine might change its position with regard to SES integration.[68] However, Yanukovich's first statements made it clear that he would not deviate from the course taken by Yushchenko, as well as Kuchma, before 2004/05. He also pointed out that cooperation in the framework of the SES should not adversely affect either Ukraine's accession to the WTO or eco-

66. Lidiya Kosikova, 'EEP: 'Byt ili ne byt' [SES: To Be or not to Be], *Nezavisimaya Gazeta*, 27 February 2006.

67. 'EEP: Principialnye raznoglasiya sokhronyayutsya' [SES: Main disagreements persist], *Zerkalo Nedeli* no. 29 (556), 30 iyuniya 2005/30 June 2005. Aleksandr Sushko, Vassiliy Filipchuk, 'Eshche raz o EEP. Dlya tekh, kto eshche ne ponyal ili uzhe zabyl...' [For those who still do not understand – or have already forgotten...], *Zerkalo Nedeli* no. 23 (551) 18-24 iyuniya 2005/18-24 June 2005: www.zn.ue.

68. Irina Kozhukhar, 'Kiev menyaet otnoshenie k EEP' [Kyiv changes relations with SES], *Nezavisimaya Gazeta*, 19 June 2006.

nomic cooperation with the EU. Repeated suggestions from the Russian side that the WTO accession processes of both countries should be coordinated were met with equal reluctance by Yanukovich and Yushchenko.[69] The new government will certainly follow this line, and it is very likely that its reluctance with respect to intensified cooperation within any of the Russian-dominated frameworks will be even stronger.

Conclusion

This chapter's analysis presents a sobering picture of Ukraine's regional policy three years after the Orange Revolution: Kyiv's attempt to forge tighter relations with other Western-oriented post-Soviet republics has been thwarted, the Community of Democratic Choice has died a quick death, Moldova now seems to be breaking away from GUAM, possibly leaving an empty space in the 'democratic belt' alongside Russia's western borders. The Yushchenko Plan for the resolution of the conflict between Transnistria and Moldova is off the table, and Ukrainian-Russian relations remain tense. As outlined by Pawel Wolowski in Chapter One of this volume, the current domestic situation does not justify hope for improvement in the near future.

A monocausal explanation of the failure of the Orange leadership's regional policy would be too simplistic. Neither state weakness within Ukraine, nor Russian pressure, nor other factors alone are responsible for the decline of the dynamic initiatives which seemed to shake up the region in 2005. The various sections of this chapter demonstrate that the reasons for the failure of the Orange leadership's regional policy are to be found on various levels.

This analysis of the domestic background of Ukraine's foreign policy reveals the political elite still divided over many crucial issues with regard to the country's external orientation. While all important political parties have embraced tight economic cooperation/integration with the EU, there is no agreement between representatives of the two main camps over the question of *whether* Ukraine should engage in the post-Soviet space, and if so, *what form* this engagement should take. The Orange Coalition started with the idea of forming a coalition of democracy-oriented countries and fostering their *rapprochement* with the EU and NATO. The Party of Regions and the Anti-Crisis Coalition do not oppose *rap-*

69. '240 Days of the Government Activity in the New Format', op. cit. in note 49, p. 74,

prochement with the EU. However, they are reluctant to challenge Russian positions in the CIS. Therefore, they show no interest in pursuing any strategy which could irk Moscow. This concerns the formation of subregional coalitions like GUAM and the CDC, the change of the *status quo* in the Transnistrian conflict, or Ukraine's accession to NATO.

After the parliamentary elections in March 2006, the two opposing positions on regional policy were represented by different institutions in the political system. While President Yushchenko and Foreign Minister Boris Tarasyuk stood for an active and Western-oriented approach, the head of government and the parliamentary majority pulled in the other direction. Given the weaknesses and contradictions ingrained in institutional decision-making, the two sides could not but block each other, thus paralysing Ukraine's regional policy altogether.

The exploration of Ukrainian-Russian relations highlighted two other factors which constrain the conduct of a coherent regional policy by the Ukrainian leadership.

The development and outcome of the Russian-Ukrainian gas crisis validate the assumption that rent-seeking actors benefiting from the continuation of the *status quo* in energy relations are to be found in all political camps in Ukraine. Corruption and clientelism persist also in the reform-oriented parts of the political elite. This makes the whole political spectrum vulnerable to actions and deals opposing the declared goal of Ukraine's regional policy after the Orange Revolution, namely (energy) independence from Russia.

The Yushchenko leadership in its early phase failed to reconcile its pragmatic approach towards Russia with its regional initiatives. While Kyiv emphasised its willingness to return to productive and mutually beneficial relations with Moscow as quickly as possible, the rhetoric used in the context of GUAM and CDC was shaped by more or less openly anti-Russian attitudes. Kyiv's partners, primarily Georgia, took a more aggressive position towards Russia, thus letting Yushchenko's appeasing signals on the bilateral level ring hollow. The lack of a comprehensive strategy, constructively integrating regional initiatives and relations with Russia, weakened Ukraine's regional policy from the outset.

All this led to a decrease in regional activities after March 2006. As Ukraine's efforts towards regional cooperation were dwindling, the processes kicked off in 2005 lost momentum. Moldova

in particular started to drift back towards a more accommodating position towards Russia. Relations between Ukraine and Georgia cooled as the influence of the Party of Regions on Ukrainian foreign policy grew at the expense of President Yanukovich, who has a close personal relationship with Georgian President Saakashvili.

This highlights a general weakness of inter-state cooperation and/or integration in the post-Soviet space: political elites in the region have an essentially statist, neo-realist perception of international relations. Consequently, their openness to multilateral cooperation, not to speak of deeper integration with other states, remains rather limited. Inter-state relations are often based on personal relationships between heads of states or informal elite networks. Links between members of regional organisations like GUAM remain weak, and are easily cut off when a change of government or a broader elite change occurs in one of the countries. Under these circumstances, processes aiming at further integration proceed very slowly. In most cases they do not go beyond summit declarations. Consequently, neither the CIS, nor GUAM, nor any other organisation on the territory of the former Soviet Union, has so far generated effective economic or political cooperation.

Last but not least, Russia's ability to exert influence on regional developments in the CIS has proved to be still quite considerable. During and after the 'coloured revolutions' policymakers in Moscow showed increasing readiness to actively use the tools at their disposal to undermine processes they perceived as detrimental to Russia's interests. This left Ukraine's allies, especially Moldova, in a precarious dilemma, thus further weakening their commitment to subregional cooperation. Although Moscow is not able to (positively) shape the former Soviet space according to its own dictates, it obviously has the (negative) power to undermine integration efforts it cannot control.

The ultimate factor weakening Ukraine's position as a regional leader has been the lack of support from important external actors, namely the EU and NATO. Contradictory signals regarding NATO accession, and obvious reluctance on the part of the EU to give Ukraine a membership perspective, have not only led to a loss of credibility within the country, but also weakened Ukraine's position in the region and *vis-à-vis* Russia. At the same time, disagreements with Russia have negatively influenced the attitude of individual EU Member States towards Kyiv. The EU's cohesive

support for the Orange Revolution in November/December 2004 was soon replaced by disagreements between those Member States, who supported Kyiv's aspirations towards EU membership, and others, who balked at the risk of tensions with Russia. The EU displayed this indecisive attitude not only in bilateral relations with Ukraine, but also towards Kiyv's regional aspirations. Its reluctance to lend political support to the Yushchenko Plan and GUAM, and internal disputes over the involvement of individual Member States in the CDC, are a case in point.

Under these circumstances, the Orange leadership's regional initiatives could not but produce modest results. If anything, they raised awareness of the most pressing problems in the region – without being able to change the structure of regional relations. Three years after the Orange Revolution, Ukraine still finds itself stuck 'in between' Russia and the EU. It has not succeeded in its attempt to become a regional player in its own right. A positive turn of events in the future is dependent on domestic developments in Ukraine, but also on the policies of its most important neighbours, Russia and the EU.

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Abbreviations

AP	Action Plan
BSF	Black Sea Fleet
BYuT	Bloc of Yulia Tymoshenko
CAP	Common Agricultural Policy
CDC	Community of Democratic Choice
CEO	Chief Executive Officer
CFSP	Common Foreign and Security Policy
CIS	Confederation of Independent States
EBRD	European Bank for Reconstruction and Development
ENP	European Neighbourhood Policy
FDI	Foreign Direct Investment
FTA	Free Trade Area
GDP	Gross Domestic Product
GUAM	Georgia, Ukraine, Azerbaijan and Moldova (later renamed the Organisation for Democracy and Economic Development)
IUD	Industrial Union of Donbass
MP	Member of Parliament
NATO	North Atlantic Treaty Organisation
NIS	Newly Independent States
OSCE	Organisation for Security and Co-operation in Europe
OU	Our Ukraine
PCA	Partnership and Cooperation Agreement
PR	Party of Regions
SES	Single Economic Space
SPFU	State Property Fund of Ukraine
tcm	thousand cubic metres
USSR	Union of Soviet Socialist Republics
VAT	Value Added Tax
WTO	World Trade Organisation
YES	Yalta European Strategy

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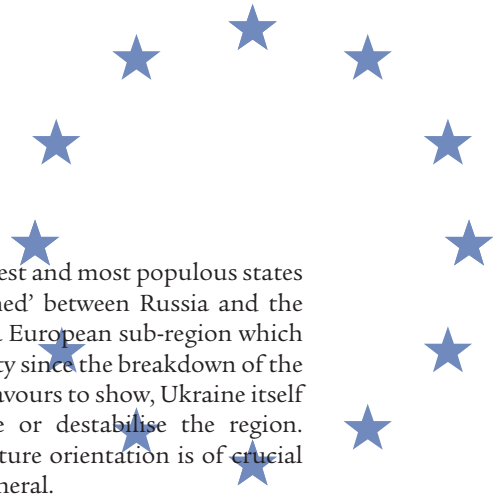

Where is Ukraine going? One of the largest and most populous states on the continent of Europe, 'sandwiched' between Russia and the EU, Ukraine is located in the centre of a European sub-region which has been characterised by great instability since the breakdown of the Soviet Union. As this *Chaillot Paper* endeavours to show, Ukraine itself has great potential to either stabilise or destabilise the region. Therefore, the question of Ukraine's future orientation is of crucial importance for European security in general.

The aftermath of the parliamentary elections on 30 September 2007 and the renewal of a coalition between the 'Orange Forces' in December seems to be an opportune time to reflect on this question. After a long period characterised by ambivalent policies vacillating between Russia and the Western community of states, a democratic upheaval swept away the corrupt regime of President Kuchma, and Ukraine embarked on a course towards Euro-Atlantic integration after the 2004 Orange Revolution. However, the post-revolutionary transformation did not go smoothly, with the new political leadership quickly becoming bogged down in domestic infighting. Internal crises and power struggles left the country practically without leadership between March and August 2006 and again between April and September/December 2007.

This *Chaillot Paper*, edited by Sabine Fischer, brings together four perspectives on Ukrainian domestic politics and foreign policy. The first two chapters' investigation into the causes of recent domestic crises and the role of single groups of actors (principally the Ukrainian oligarchs) provides an insight into the domestic intricacies of a country as complex as Ukraine. The third chapter takes stock of Ukraine's relations with the EU three years after both sides declared swift *rapprochement* and the far-reaching Europeanisation of Ukraine to be their common goal, when the European Neighbourhood Action Plan was signed after the Orange Revolution. The final chapter focuses on how relations with Russia and its CIS neighbours remain a crucial dimension of Ukraine's often ambivalent foreign policy, and examines the extent to which Ukraine has become, or has the potential to become, a force for stability in the region.

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