

SUMMARY

OF THE REPORT

“INTEGRATION WITHIN ASSOCIATION:
DYNAMICS OF THE EU-UKRAINE AGREEMENT IMPLEMENTATION”

THE FOURTH EDITION, EXTENDED

For more than seven years, relations between Ukraine and the EU have been governed by the Association Agreement (AA), the most ambitious international agreement Ukraine has ever concluded.

The Association Agreement was signed in 2014 and ratified by the Verkhovna Rada and the European Parliament at the same time. Selected AA provisions began provisionally applied on November 1 2014, while the provisions of Deep and Comprehensive Free Trade Area (DCFTA) - from January 1, 2016 (although the opening of the EU market occurred earlier, namely in April 2014 based on autonomous trade preferences). On September 1, 2017, the AA came into force in full.

The Association Agreement is a vast, legally binding bilateral international agreement between Ukraine and the EU. The most specific commitments of the Parties were undertaken in the framework of the DCFTA and economic cooperation aiming at achieving Ukraine’s integration into the EU internal market. This part of the AA text can be tentatively divided into three types of arrangements:

- **“Direct action” arrangements**, the key element of which is tariff liberalisation - mutual opening of markets through the gradual abolition of duties (asymmetric, privileged for Ukraine by the EU) ;
- **“Prerequisite” arrangements**, the implementation of which requires Ukraine to fulfil certain obligations, after which there is an opportunity to make the decisions to deepen integration. That is true for most sectoral integration, where the removal of barriers to the activities of Ukrainian business in the EU market (and vice versa) provided implementation by Ukraine of norms and standards of the EU in these areas/sectors;
- **Arrangements, the implementation of which contributes to creating a level playing field in the market** to ensure fair competition between Ukrainian and European companies. That is done by gradual implementation by Ukraine of the rules and standards of the EU concerning the rights of consumers, intellectual property rights protection, rights of workers, environmental requirements, state aid and preventing monopolisation of markets. However, these arrangements do not provide for the decisions on deepening integration due to Ukraine’s fulfilment of its obligations.

In this way, an essential part of the arrangements (*quid pro quo*) in the framework of the AA is a unilateral regulatory approximation in exchange for economic integration. Ukraine is obliged to adopt and practically implement the *acquis* - legal norms, regulations and technical standards of the EU - in exchange for commitments of the EU to integrate Ukraine into the internal market of

the EU. In general, except for the European Economic Area and the candidate countries, the EU has never been so open to its internal market to third countries.

The EU's commitments on Ukraine's sectoral integration, which specify the areas for which the AA provides for additional decisions on Ukraine's integration, are presented in Table 1. In total, we are talking about 15 areas. Adopting these decisions should allow the Ukrainian business to operate in the EU market without additional permits, certificates, or licenses.

Table 1: Sectoral integration of Ukraine into the EU internal market under the AA provisions

| № | Area | Market | AA provisions | Method of integration to the EU market as foreseen in the AA | Timeframe for implementing Ukraine's obligations as in the AA, from the date of entry into force/start of the AA provisional application |
|---|-------------------------------------|---------------------|------------------------------------------|------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------|
| 1 | Technical barriers | Industrial products | Article 57 AA, Annex III | Conclusion of the Agreement on Conformity Assessment and Acceptance of Industrial Goods (ACAA) | Two years * (until 31.12.2017) |
| 2 | Sanitary and phytosanitary measures | Agro-food goods | Articles 64, 66 AA, Annexes IV, V, IX | Decision-making on recognition of equivalence in different sectors of agro-food products ** | 2021 *** |
| 3 | Customs procedures | All goods | St. 76.1 (c), 76.4 (b) AA, Annex XV | Joining the common transit system | One year (until 31.12.2016) |
| | | | St. 76.1 (k), 80 (i) AA | Mutual recognition of authorised economic operators (AEO) | Three years (until 31.12.2018) |
| 4 | Services | Financial | St. 4 (3) of Annex XVII, Appendix XVII-2 | Granting the internal market treatment | Six years (until 31.12.2021) |
| 5 | | Tele-communications | St. 4 (3) of Annex XVII, Appendix XVII-3 | Granting the internal market treatment | Four years (until 31.12.2019) |
| 6 | | Postal and courier | St. 4 (3) of Annex XVII, Appendix XVII-4 | Granting the internal market treatment | Two years (until 31.12.2017) |
| 7 | Transport services | Automotive | Article 136 AA, Annex XXXII (1) | Possibility of concluding a special agreement in the field of road transport **** | Seven years (until 30.10.2021) |
| 8 | | Railway | Article 136 AA, Annex XXXII (2) | Possibility of concluding a special agreement in the | Eight years (until 30.10.2022) |

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| | | | | field of railway transport **** | |
| 9 | | Inland water | Article 136 AA, Annex XXXII (5) | Possibility of concluding a special agreement in the field of inland water transport **** | Five years (until October 30, 2019) |
| 10 | | International maritime | St. 4 (3) of Annex XVII, Appendix XVII-5, Annex XXXII (4) | Granting the internal market treatment | Six years (until 31.12.2021) |
| 11 | | Aviation | Article 137 AA | Decisions under a separate Common Aviation Area Agreement (CAA) | Not specified***** |
| 12 | Government Procurement | Public procurement market | Article 154 v, Annex XXI | Opening access to the market in the amount determined by the provisions of the AA | Gradually, in five stages, within six months - eight years (until 31.12.2023) |
| 13 | Energy | Natural gas market | Annex XXVII | Not clearly defined in AA ***** | to 31.12.2019 |
| 14 | | Electricity market | Annex XXVII | Not clearly defined in AA ***** | 2021 |
| 15 | Education | Labor market | St. 432.b AA, Annex XLII | Mutual recognition of qualifications and competencies | Not specified |

* For fulfilling the obligations in the scope sufficient for the conclusion of the ACAA. For fulfilling it in the scope enough for extension of the ACAA coverage to all 27 sectors listed in the AA – 5 years

** Also, there is an option of approval of individual producers for exports to the EU without waiting for decisions on the equivalence of the whole relevant sector. In practice, Ukrainian producers are actively using this option

*** According to the Comprehensive Strategy for the Implementation of the AA Chapter on Sanitary and Phytosanitary Measures (Chapter 4 of the Title IV of the AA) that was approved by the AA joint bodies at the end of 2019 and became the content of Annex V to the AA

**** The AA text does not put implementation of regulatory approximation obligations as a precondition for the possible conclusion of this agreement

***** The EU-Ukraine Common Aviation Area (CAA) Agreement was initialled at the end of 2013 but has not yet been signed due to a dispute between the UK and Spain about the mention of Gibraltar Airport in the text of this agreement

***** Even the updated Annex XXVII does not contain a clear perspective for gaining internal market treatment. However, its implementation may lead to de facto integration of Ukraine into the EU gas market when transportation of gas from Russia to the EU through the territory of Ukraine is regulated by EU law (and, possibly, with the point of gas delivery shifted to the Eastern border of Ukraine)

***** Even the updated Annex XXVII does not contain a clear perspective for gaining internal market treatment. However, its implementation may lead to de facto integration of Ukraine into the EU electric energy market, with Ukraine joining the European ENTSO-E network

As of June 2021, Ukraine should have met its obligations in 7 of the 15 areas. That refers to technical barriers, customs procedures, telecommunications, postal and courier services, inland water transport, the natural gas market and the first three stages of public procurement. In addition, by the end of 2021, commitments on sanitary and phytosanitary measures, financial services, road transport, international maritime transport and the electricity market were to be met.

Thus, as of mid-2021, one could already expect the formation of preconditions for the adoption of EU decisions on Ukraine's integration into its internal market, which relate to:

- Conclusion of the Agreement on Conformity Assessment and Acceptance of Industrial Products (ACAA);
- Recognition of the equivalence of certification systems at least for one type of agro-good products;
- Integration into the European Common Transit System;
- Mutual recognition of autonomous economic operators;
- The "internal market treatment" for postal and courier services;
- The "internal market treatment" for telecommunication services;
- The beginning of consultations on the possibility of concluding a special agreement in the field of inland water transport; and
- The third stage of opening the public procurement market.

However, not everything went as planned. To date, actual progress in economic integration into the EU market has been made in only two areas. First, a decision was made to recognise the equivalence of seed certification systems. Secondly, Ukraine has been de facto integrating into the EU gas market through the establishment of a separate independent operator of Ukraine's gas transmission system, agreements on cooperation between Ukraine's gas transmission network operators and neighbouring EU member states, and the signing of a gas transportation agreement between Naftogaz and Gazprom based on EU rules.

Ukraine also gained partial access to the public procurement market under the WTO Agreement on Government Procurement, but this took place outside the AA.

In many areas, Ukraine has been lagging in the implementation process. At the same time, where Ukraine has made significant progress, there is no verification and official confirmation of the implementation by the EU. That creates risks because the partners evaluate the same events differently, and therefore their next steps are based on different assumptions.

By separate areas, the dynamics for 2020 - the first half of 2021 is as follows:

Technical barriers to trade: In October 2020, a preliminary EU expert assessment mission was launched to evaluate the state of harmonisation of Ukrainian legislation with the EU *acquis* as part of the overall assessment of Ukraine's readiness to conclude an Agreement on Conformity Assessment and Acceptance of Industrial Products (ACAA). The results of this assessment mission, presented in May 2021, indicate a high level of legislative harmonisation, which, however, is not

entirely sufficient and requires further work. During the second half of 2021, an assessment of the implementation of legislation and the effectiveness of the quality infrastructure is expected to begin.

Sanitary and phytosanitary measures: At the end of 2020, the EU recognised the equivalence of the control and certification system of cereal seeds in Ukraine, the first achievement of integration within the AA. While legal harmonisation progresses steadily, the Ukrainian producers of animal products actively used the possibility of individual verification of production for export to the EU.

Customs: Since the legislative breakthrough in 2019, when the long-awaited new legislation was finally adopted in line with Ukraine's AA obligations, the main task is its implementation. Ukraine has started granting an authorised economic operator (AEO) status, and one company has already received it. However, the incomplete secondary legislation limits the benefits of using this status. Mutual recognition can be obtained after the AEO system has been in place in the country for some time. The application of the computer system NCTS, which ensures the implementation of the common transit system, is also underway. As of June 2021, this system operates in the national mode in parallel with the standard one, and in about one and a half years, Ukraine is expected to join the pan-European system.

Financial services: At the beginning of 2020, the Strategy for the Development of the Financial Sector of Ukraine until 2025 was approved. It, in particular, provides for the implementation of the critical provisions of EU legislation required to obtain an internal market regime with the EU. However, this perspective remains unclear, given the changes in EU regulation that have taken place since the conclusion of the AA negotiations. Therefore, an important task is to update Annex XVII to the AA and create an institutional mechanism that would allow the implementation of the functions of European Supervisory Authorities in Ukraine, which is a necessary prerequisite, according to the new EU regulations, for obtaining an "internal market".

Telecommunications: In 2020, thanks to the EU expert mission, the "road map" for Ukraine's integration into the EU Digital Single Market, developed by Ukraine in 2018, was updated. The measures envisaged by the map form the basis for further development of digital regulation in Ukraine following EU recommendations. Furthermore, in early 2021, Ukraine and the EU adopted a work plan in electronic trust services to be implemented over the next two years.

Postal and courier services: Ukraine has not yet adopted a law to implement Directive 97/67 / EC provisions. The bill, which is currently before the parliament, needs to be finalised, as it does not fully comply with the said Directive.

Transport: The Common Aviation Area Agreement, initialled in 2013, remains unsigned, despite the completion of the Brexit procedure. In 2020, the law on water transport was finally adopted, which partially embeds the provisions of all six EU directives relating to this mode of transportation. However, no breakthrough has occurred in other transport sectors: several draft key laws on rail, sea and road transport are still pending in parliament.

Public Procurement: In 2020, a new version of the Law on Public Procurement came into force, approximating Ukrainian legislation to EU directives according to the requirements of the second (out of five) stage of the AA Indicative Schedule in public procurement. At the same time, the EU and Ukraine have not yet agreed on the formal completion of the first stage. In addition, in 2020, a bill, which introduces localisation requirements for selected public procurement and thus does not correspond to the content of Ukraine's obligations under the AA, was registered in the Verkhovna Rada.

Energy: As already mentioned, Ukraine has achieved a significant level of integration in the EU natural gas market. Based on 2020 results, the Energy Community assessed the implementation status of European legislation in the gas market in Ukraine as “almost complete” (84%). At the same time, the European Green Deal also includes changes in EU legislation on the gas market, which creates new challenges for Ukraine. Joining the ENTSO-E network is the main European integration task that remained on the agenda in the electricity market. In May 2021, the President signed a law allowing Ukrenergo to be certified as a European-style OSP, bringing Ukraine one step closer to the integration goal, but much remains to be done.

Education: To obtain mutual recognition of qualifications and competencies, Ukraine has committed itself to implement the Recommendations of the European Parliament and the Council on the establishment of a European qualifications system based on the principle of lifelong learning. In June 2020, the government approved a new version of the National Qualifications Framework in line with European qualifications. However, a significant part of the tasks related to creating a qualification system, particularly the adoption of the necessary legislation, is delayed.

Thus, Ukraine has been fulfilling its obligations, although with delays. As a result, the question of EU decisions on Ukraine’s integration into the EU internal market in the relevant sectors, as provided by the AA, will increasingly arise. However, given the existing preconditions, in 2021, we can expect only one decision related to the economic integration - the signing of the Common Aviation Area Agreement.

At the same time, given the continued active implementation of Ukraine’s commitments and the presence of political will on the part of the EU, by 2023, we can expect progress in sectoral integration within the AA on:

- Mutual access to public procurement markets, with at least several stages of the Indicative Plan completed;
- Ukraine’s accession to the pan-European common transit system;
- Connection to the ENTSO-E network;
- Conclusion of the Agreement on mutual recognition of electronic trust services between Ukraine and the EU;
- Conclusion of the ACAA Agreement;
- Further recognition of the equivalence of certification systems for agricultural products; and
- Mutual recognition of authorised economic operators.

In parallel with realising the opportunities already provided in the Agreement, AA modernisation should occur.

The need to update the AA Annexes is evident as the EU legislation has evolved significantly since the negotiations between Ukraine and the EU on the AA (2011). Already at the meeting of the Association Council in December 2018, the Parties agreed to begin work on updating the Annexes to the Association Agreement to take into account the new legal realities of the EU. Annex XXVII on energy was the first to be updated in 2019. In addition, proposals for updating the content of Annex XVII-3 on telecommunications services have been developed. There is also a need to update Annex XVII-2 on financial services and most other annexes to the AA.

The revision of Annex I-A in terms of tariff quotas for poultry meat has set a precedent that will stimulate a meaningful revision (further liberalisation) of all other existing tariff quotas of the DCFTA. After all, since the end of the AA negotiations, there have also been significant changes in Ukraine's economy, which require the renewal of the AA, primarily in the tariff part of the DCFTA.

The Association Council that met on February 11, 2021, declared the intention of both sides to hold the comprehensive overview of the Association Agreement at the next Ukraine - EU summit and begin consultations on possible further liberalisation of trade under the DCFTA.

Thus, to ensure Ukraine's integration into the EU internal market as one of the primary objectives of the Agreement, the parties should work to ensure parallel on sectoral integration under existing agreements and the Agreement's modernisation.

The critical tasks for Ukraine are to continue the harmonisation of legislation within the framework of the obligations of the Association Agreement and its implementation, taking into account:

- The need to consult with EU representatives regarding the compliance of draft regulations with the *acquis* before the adoption of these acts;
- The need for further verification of compliance of changes with EU norms and practices;
- The need for dynamic adaptation to changes in EU legislation.

At the same time, it is essential to strengthening the EU's commitments related to regular verification of Ukraine's progress, especially in sectors where further integration involves a separate EU decision based on Ukraine's assessment of compliance with its legislation and effective implementation.

Sectorwise, the EU should decide on its readiness to conclude agreements with Ukraine in the fields of road, rail and inland waterway transport. The AA allows for the possibility of concluding such special agreements to ensure coordinated development and progressive liberalisation of transportation between the Parties. However, according to the text of the AA, this is an opportunity, not an obligation. So far, the relevant issues remain the subject of bilateral negotiations between Ukraine and (neighbouring) EU member states.

Analysing the opportunities for deepening economic integration within the AA, we should not forget about global changes in EU policy, which will also determine relations with Ukraine. At the end of 2019, the EU announced a policy of the European Green Deal, the strategic goal of which is to make Europe climate-neutral by 2050. The Green Deal covers most of the issues of sectoral cooperation between Ukraine and the EU, where Ukraine's economic integration into the EU market is envisaged, particularly energy, transport, technical regulation and sanitary and phytosanitary measures, public procurement and financial services. Without considering the Green Deal, effective AA modernisation and the achievement of sectoral integration are impossible.