



# Ukraine: Current Issues and U.S. Policy

**Steven Woehrel**  
Specialist in European Affairs

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## Summary

Since Viktor Yanukovich defeated Prime Minister Yuliya Tymoshenko to win Ukraine's presidency in 2010, many observers have expressed concern about Ukraine's democratic development, including the government's use of the courts to neutralize opposition leaders, including Tymoshenko, who was sentenced to a seven-year prison term in 2011. These actions have led to serious doubts about whether parliamentary elections scheduled for October 28, 2012, will meet international standards.

The global economic crisis hit Ukraine hard. Ukraine's real Gross Domestic Product (GDP) fell by an estimated 15% in 2009. The economy began to recover in 2010, and GDP increased by 4.7% in 2011, due in part to a surge in demand for Ukrainian steel exports. However, living standards for many Ukrainians remain low, leading to a rapid drop in Yanukovich's popularity when compared to the period soon after his inauguration. Expected slow growth in Western Europe will likely result in slower growth in 2012 for Ukraine as well.

President Yanukovich has pursued closer ties with Russia, especially in the economic sphere. A major focus of his policy has been to seek reduced prices for natural gas supplies from Moscow. In April 2010, he agreed to extend the lease of the Russian Black Sea Fleet in Ukraine for 25 years in exchange for a reduction in gas prices. However, the impact of the deal on gas prices has been less than anticipated, as oil prices (on which Ukraine's gas price is calculated) have soared due to unrest in the Middle East. As a result, Ukraine has sought additional gas price cuts from Moscow, so far without success. Ukraine has so far fended off Russian pressure to sell it control of its gas pipeline system and join Russia-led political and economic integration structures.

Yanukovich has said that EU integration is a key priority for Ukraine, but EU criticism of what it views as the politically motivated conviction and imprisonment of Tymoshenko and others has called into question whether a long-awaited association agreement with the EU (including a free trade agreement) will be signed and enter into force. Yanukovich has made clear that his country is not seeking NATO membership, but will continue cooperation with NATO, including the holding of joint military exercises.

The Obama Administration has worked to "reset" relations with Russia, but has warned that it will not accept any country's assertion of a sphere of influence, a reminder of U.S. support for Ukraine's sovereignty. The Administration has not publicly expressed concern about what some observers view as the pro-Russian tilt of Ukraine's foreign policy under Yanukovich. The Administration has focused on helping Ukraine rid itself of its supplies of highly enriched uranium, assisting Ukraine with the clean-up of the Chernobyl nuclear site, and diversifying Ukraine's sources of energy, including advice on developing Ukraine's shale gas reserves. Administration officials have expressed concerns about regression in Ukraine's democratic development since Yanukovich took power, including in such areas as media freedoms and selective prosecution of the government's political opponents.

Several pieces of legislation have been introduced in the 112<sup>th</sup> Congress calling for Tymoshenko and other victims of politically motivated prosecutions to be released from prison. Two of them, S.Res. 466 and H.Res. 730, call for sanctions against Ukrainian leaders responsible for selective prosecutions.

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## Background

Ukraine, comparable in size and population to France, is a large, important, European state. The fact that it occupies the sensitive position between Russia and NATO member states Poland, Slovakia, Hungary, and Romania adds to its geostrategic significance. Many Russian politicians, as well as ordinary citizens, have never been fully reconciled to Ukraine's independence from the Soviet Union in 1991, and feel that the country belongs in Russia's political and economic orbit. The U.S. and European view (particularly in Central and Eastern Europe) is that a strong, independent Ukraine is an important part of building a Europe whole, free, and at peace.

From the mid-1990s until 2004, Ukraine's political scene was dominated by President Leonid Kuchma and the oligarchic "clans" (groups of powerful politicians and businessmen, mainly based in eastern and southern Ukraine) that supported him. Kuchma was elected president in 1994, and re-elected in 1999. He could not run for a third term under the Ukrainian constitution. His rule was characterized by fitful economic reform (albeit with solid economic growth in later years), widespread corruption, and a deteriorating human rights record.

Ukraine's 2004 presidential elections were marred by electoral fraud, which triggered massive street protests. The oligarchs chose Prime Minister Viktor Yanukovich as their candidate to succeed Kuchma as president. The chief opposition candidate, former Prime Minister Viktor Yushchenko, was a pro-reform, pro-Western figure. After the November 21 runoff vote, Ukraine's Central Election Commission proclaimed Yanukovich the winner. Yushchenko's supporters charged that massive fraud had been committed. Hundreds of thousands of Ukrainians took to the streets, in what came to be known as the "Orange Revolution," after Yushchenko's chosen campaign color. They blockaded government offices in Kyiv and appealed to the Ukrainian Supreme Court to invalidate the vote. The court did so and set a repeat runoff vote. Yushchenko won the December 26 re-vote, with 51.99% of the vote to Yanukovich's 44.19%.

The "Orange Revolution" sparked a good deal of interest in Congress and elsewhere. Some hoped that Ukraine could finally embark on a path of comprehensive reforms and Euro-Atlantic integration after years of half-measures and false starts. However, subsequent events led to disillusionment among Orange Revolution supporters, both in Ukraine and abroad. President Yushchenko soon fell into squabbling with Yuliya Tymoshenko, his main backer during the Orange Revolution and his first prime minister, over policy and over mutual allegations of corruption, slowing progress on reforms.

In 2006, Yushchenko reluctantly reappointed his 2004 presidential election opponent Viktor Yanukovich as prime minister, after Yanukovich's Party of Regions won the most seats in parliamentary elections that year. Political conflict between Yushchenko and Yanukovich soon ensued, leading to early parliamentary elections in September 2007. The Party of Regions remained the largest party in the new legislature, but the Yuliya Tymoshenko Bloc and Yushchenko's Our Ukraine-People's Defense group won enough seats to form a new government. After lengthy negotiations, President Yushchenko nominated Tymoshenko as his candidate for prime minister. The parliament approved Tymoshenko as prime minister on December 18, 2007, with 226 votes, the barest of majorities in the 450-seat assembly.

Over the next two years, Ukraine's government again lurched from one political crisis to another. Perhaps the key problem was the familiar one of tensions between Tymoshenko and President Yushchenko. In addition to policy differences and intense personal enmity and distrust between

the two leaders, the conflict was also due to jockeying for power in advance of upcoming presidential elections, in which both were to be candidates. As Ukrainian leaders engaged in this three-sided political battle, an overwhelming majority of Ukrainians grew disgusted with the Ukrainian political class, according to opinion polls. Observers say that this is in part due to the fact that Ukrainian leaders continued to squabble despite the global economic crisis, which inflicted severe blows on Ukraine's economy.

Ukraine held presidential elections on January 17, 2010. As expected, Viktor Yanukovich came in first, winning 35.32% of the vote. Yuliya Tymoshenko, doing somewhat better than some pre-election polls indicated, won 25.05%. Serhei Tihipko, a former prime minister whose support was strongest in pro-Russian eastern Ukraine, won 13.05%. Former parliament speaker Arseniy Yatsenyuk won 6.96%. Incumbent President Yushchenko did very poorly, winning a mere 5.45%. Other candidates split the rest of the vote. The results set up a second round runoff vote between Yanukovich and Tymoshenko on February 7. Yanukovich won 48.98% of the vote, beating Tymoshenko, who won 45.47%. The results showed a sharp regional split, with Yanukovich winning in Russian-speaking eastern and southern Ukraine, while Tymoshenko prevailed in central and western Ukraine, where Ukrainian nationalism is stronger. However, Yanukovich's overwhelming margins in the east (particularly in his home base, the Donetsk and Luhansk regions) more than offset Tymoshenko's modest victories in some western areas.

International monitors praised the conduct of the election. Joao Soares of Portugal, head of the observer team from the Organization for Security and Cooperation in Europe, said the February 7 vote was an "impressive display of democratic elections." In a possible hint to Tymoshenko, he added that it was "now time for the country's political leaders to listen to the people's verdict and make sure that the transition of power is peaceful and constructive."<sup>1</sup> Exit polls by independent groups did not show a significant departure from the announced results. Tymoshenko charged that Yanukovich's supporters had engaged in massive fraud, but that she would not call her supporters out into the streets to challenge the result. Analysts suggested that this was because a disillusioned public would not turn out for mass demonstrations as they had in 2004.

On March 11, 2010, the Ukrainian parliament approved Yanukovich's choice for the post of prime minister, Mykola Azarov. Azarov has been a loyal associate of Yanukovich for many years. He served as first deputy prime minister and finance minister during Yanukovich's two terms as prime minister. The government is supported by the Party of Regions, the Communist Party, and the centrist and opportunistic Lytvyn Bloc. However, in order to secure a majority, additional support from deputies of the former ruling coalition was required. As has happened after previous presidential elections, the new leader was able to gain that support. Opposition leaders charged that those who switched did so because they were bribed or threatened with government retaliation against their businesses if they did not comply. The opposition also said that the defections from a party faction were unconstitutional. However, the Ukrainian Constitutional Court later ruled that the method of the government's formation was legal. President Yanukovich's formal powers were further boosted in October 2010, when the Constitutional Court invalidated constitutional amendments adopted during the Orange Revolution that had ceded some of the president's power over the government to the parliament.

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<sup>1</sup> The reports of the International Election Observation Mission can be found at <http://www.osce.org/odihr/>.

## Current Political Situation

President Yanukovich and his supporters have portrayed themselves as a team of professionals engaged in the practical work of governing, as opposed to the unproductive squabbling of the Yushchenko period. The opposition charges that the government has not achieved significant results while in office, except for engaging in massive corruption and favoring the business interests of its oligarchic backers. They have noted that the Yanukovich family is rapidly acquiring assets, forming an oligarchic group of its own. After a brief “honeymoon” period after the presidential election, the Yanukovich administration dropped sharply in public opinion polls (as its predecessors did).

Ukraine’s government has been strongly criticized over its human rights record. Ukrainian journalists and international groups such as Freedom House and Reporters without Borders have charged that the government pressures the media to engage in self-censorship. Private media owners have reportedly been threatened with harm to their businesses if their outlets do not moderate their criticism of the government. Journalists groups have complained that physical assaults on journalists have gone unpunished.

U.S. and EU officials have expressed concern that opposition leaders have been targeted for selective prosecution. In the most prominent case, in October 2011 Tymoshenko was convicted of abuse of power arising out of her role in signing a natural gas supply agreement with Russia and sentenced to seven years in prison. In August 2012, Ukraine’s Supreme Court upheld the conviction. Tymoshenko is currently awaiting another trial on charges of embezzlement, fraud, and tax evasion while she headed an energy company in the 1990s. Due to serious back pain she was suffering, Tymoshenko was transferred first to a prison hospital, and then, after she complained of mistreatment and inadequate care, to another hospital outside the prison.

In another apparent case of selective prosecution, in February 2012 former Interior Minister Yuri Lutsenko was convicted on charges of abuse of office, fraud, and embezzlement, and sentenced to four years in prison. In all, U.S. Ambassador to the OSCE Ian Kelly said after Lutsenko’s conviction, 13 former senior officials from the Tymoshenko-led government, including 4 cabinet ministers, 5 deputy ministers, 2 agency heads, 1 governor, and the head of the state gas monopoly, had been charged with alleged crimes arising from their time in office.

### Key Contenders in Ukraine’s Parliamentary Elections

**Party of Regions:** The main party of the ruling regime. By far the largest party in outgoing Ukrainian parliament, and likely in the next one as well, it draws its support from eastern Ukraine, where suspicion of Ukrainian nationalism is high and support for close ties with Russia is strong. It defends the economic interests of powerful oligarchic business groups.

**Fatherland:** The largest opposition party, founded by imprisoned opposition leader Yuliya Tymoshenko. In order to boost the opposition’s chances, Fatherland’s party list for the parliamentary election includes figures from other opposition groups. This united opposition slate is running on a populist, anti-corruption platform. It will likely draw its support from western and central Ukraine, where Ukrainian nationalism is strongest.

**Communist Party:** The Communist Party has been overtaken by the Party of Regions in its eastern Ukraine strongholds and has a largely elderly electorate. It opposes market economics and favors strong ties to Russia. The Communists could attract some votes from those in eastern Ukraine who are disenchanted with the Party of Regions, with which, however, it is allied in the current government.

**Ukrainian Democratic Alliance for Reform (UDAR):** Founded by heavyweight boxing champion Vitali Klitchko (the acronym “UDAR” means “punch” in Ukrainian), UDAR is relying chiefly on the personal popularity of Klitchko. Its platform, while expressing opposition to regime corruption, has been criticized for lacking in specifics. Its party list is heterogeneous, including former supporters of Yushchenko and Tymoshenko, as well as opportunistic figures who have switched sides in the past when it suited their personal interests.

Given this record, the United States and the European Union are concerned about whether October 28, 2012, parliamentary elections will meet international standards. To its credit, the Ukrainian government has welcomed an election observation mission from the Organization for Security and Cooperation in Europe to monitor the vote.

According to Ukraine's electoral law, half of the seats in the parliament will be determined by proportional representation by a country-wide party list, with a minimum of 5% of the vote needed to receive seats. The other half of the seats will be decided by races in individual districts. In August 2012, the Ukrainian Central Election Commission struck Tymoshenko and Lutsenko from the united opposition's party list, due to their criminal convictions.

The opposition's prospects may be hampered by a lack of complete unity. Fatherland (Tymoshenko's party), Front for Change (led by former presidential candidate Arseniy Yatsenyuk) and a few smaller parties have formed a joint list for the proportional vote, and are selecting only one opposition candidate to run in the individual districts. They are also coordinating informally in single member districts in western Ukraine with Freedom, an extreme Ukrainian nationalist group. However, other parties, such as UDAR (Punch), led by heavyweight boxing champion Vitaly Klitschko, have not joined Fatherland and its allies, and have submitted their own candidates, possibly splitting the opposition vote. Moreover, other, unaffiliated figures could also split the anti-regime vote in individual districts.

If past elections are any guide, the Party of Regions will do very well in its eastern Ukraine base, as well as the largely Russified south, while the opposition will do well in less populous but nationalist western Ukraine and in central Ukraine as well. A language law signed by Yanukovich in August 2012 that gives the Russian language a greater official status may intensify this regional split. The opposition will be likely to do better in the party list vote than in many of the individual districts, where the regime can most easily deploy government resources to help its favored candidates before the vote and pressure even genuinely independent figures to support the government after the election.

Judging by polling data so far and the actions taken by the Party of Regions to tilt the playing field in its favor, it will likely be difficult for the opposition to attain its objective of winning a majority. However, it is possible that the opposition could reduce the regime's majority, dealing a blow to its already faltering prestige. Barring massive electoral fraud, it is likely that the opposition will at least be able to prevent the regime from getting the 300 seats needed in the 450-seat parliament to reshape this constitution according to its own wishes.

Even if the regime does not engage in electoral fraud during the vote or afterward (perhaps an optimistic assumption), it is likely that the United States' and EU's assessment of the vote will still be quite critical, above all due to the government's use of the courts to decapitate the opposition before the vote. Other issues currently raised by the opposition during the campaign, such as intimidation of independent media, bias in government-controlled broadcast outlets, and use of government resources to help pro-regime candidates, will also likely figure in U.S. and EU assessments.

## **Current Economic Situation**

Until the global economic crisis, Ukraine was experiencing substantial economic growth, with GDP increasing by an average of 7.5% between 2000 and 2007. The growth was fueled mainly by

consumption, including an import boom fed by heavy domestic and foreign borrowing. This was reflected in a widening trade deficit and current account deficit. Ukraine's growth was also due to strong demand for products of the country's large steel and chemicals industries. Despite this growth, Ukraine remains much poorer than other European countries. In 2011, its GDP per capita in purchasing power parity terms was only 21% of that of the EU and only 43% of Russia's. In 2010 its foreign direct investment (FDI) per capita was \$979, less than half of that in Russia and about a quarter of Poland's FDI per capita. Foreign companies often cite such issues as rampant corruption and serious shortcomings in the rule of law (including a weak judiciary) as key stumbling blocks to foreign investment.

Due to the unsustainable basis of its growth and the lack of confidence caused by its squabbling political leadership, Ukraine was hit very hard by the global economic crisis. Ukraine's real Gross Domestic Product fell by 15.1% in 2009. The economy soon rebounded, however. Real GDP rose by 4.2% in 2010, according to the Economist Intelligence Unit, and by 5.2% in 2011. Ukraine's recovery has been assisted by a sharp increase in demand for steel, which has spurred exports. Real GDP growth slowed to 2.5% in the first half of 2012 on a year-on-year basis, due to a downturn in Europe.

Ukraine's currency, the *hryvnya*, was devastated by the crisis, dropping from 5.05 to the US dollar at the end of 2007 to 7.7 at the end of 2008. In mid-2012, it was still nearly 8 *hryvnya* to the dollar. This development has been devastating for Ukrainian banks as well as for many Ukrainian savers, as many deposits and loans were denominated in foreign currencies before the financial crisis.

There have been concerns about the transparency of the privatization process under the Yanukovich administration. In 2011, Ukrtelecom, the state-owned telecommunications firm, was sold to Epic, an Austrian financial firm reputed to have close ties with Ukrainian officials and businessmen. Foreign investors in the agriculture sector expressed anger at Ukraine's limitation of grain export licenses, which appeared to be granted preferentially to companies with close ties to government officials. Observers believe that the natural gas sector privatization currently underway will also lead to control of regional gas supply infrastructure by powerful oligarchs close to the government.

In July 2010, the International Monetary Fund approved a \$15.15 billion standby loan for Ukraine to support its reform efforts. Two tranches of the loan were disbursed, but the IMF has declined to release additional tranches, due to Ukraine's refusal to increase energy prices for domestic consumers, which would be highly unpopular in Ukraine. Heavy government spending in the run-up to the parliamentary election will also likely be viewed with disapproval by the IMF. Ukraine has received loans from Russia and China to try to make up for the suspension of the IMF loan. Ukraine has also raised large additional loans on the Eurobond market.<sup>2</sup>

## Ukraine's Foreign Policy

Since achieving independence in 1991, conflict between Ukraine's political forces has led its foreign policy to appear incoherent, as the contending forces pulled it in pro-Western or pro-Russia directions or simply neglected foreign policy as less important than domestic political

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<sup>2</sup> Economist Intelligence Unit Country Report: Ukraine, August 2012.



combat and the division of the spoils of victory. Before the election of Yushchenko as president in 2005, Ukrainian leaders gave lip service to joining NATO and the European Union, but did little to meet the standards set by these organizations. Ukrainian leaders also promised closer ties with Russia in exchange for Russian energy at subsidized prices, but balked at implementing agreements with Russia that would seriously compromise Ukraine's sovereignty, such as ceding control over Ukraine's energy infrastructure to Moscow.

President Yushchenko tried to break with this pattern, and accelerate Ukraine's integration into the global economy and Euro-Atlantic institutions. Ukraine achieved one key foreign policy goal in 2008, when it joined the World Trade Organization (WTO). However, progress toward eventual membership in the European Union and NATO was limited and relations with Russia were troubled.

President Yanukovich's foreign policy appears to resemble a return to that of the pre-Yushchenko period, but with a stronger tilt toward Russia. Yanukovich has broken with previous Ukrainian presidents by clearly rejecting NATO membership for Ukraine. He continues to express support for EU integration for Ukraine, but the genuineness of his commitment to the reforms needed to reach this goal is open to question. He has improved ties with Russia, but has so far tactfully evaded Russia's most ambitious demands for economic and military integration.

## **NATO**

Ukraine currently has an "Intensified Dialogue" with NATO. President Yushchenko sought a Membership Action Plan (MAP), a key stepping-stone to joining the alliance. The MAP gives detailed guidance on what a country needs to do to qualify for membership. NATO declined to offer Ukraine a MAP at the April 2008 NATO summit in Bucharest, despite strong support from the United States and almost all Central European NATO members. Germany and France played the leading role in blocking the effort. They raised questions about Ukraine's qualifications for a MAP and also expressed concerns that granting a MAP to Ukraine would hurt relations with Russia. In a move that surprised many observers, the summit communiqué also contained an unqualified statement that Ukraine (and Georgia) "will become members of NATO," without specifying when that might happen.

European NATO countries that have opposed a MAP for Ukraine appear to fear that it would result in a sharp deterioration in relations with Moscow and perhaps even being embroiled in a military conflict with Russia in the future. In addition, European critics of Ukraine's NATO membership candidacy point out that opinion polls have repeatedly shown that a large majority of Ukrainians oppose NATO membership. In what appeared to be an attempt to skirt the sensitive membership candidacy issue, in December 2008 NATO foreign ministers agreed to work with Ukraine on "annual national programs" within the framework of the existing NATO-Ukraine Commission, which assists Ukraine's defense reform efforts.

In 2010, President Yanukovich dropped the MAP aspirations of his predecessor, a move that pleased Russia. He said that Ukraine would continue cooperating with NATO in defense reform and other areas, but without seeking membership in the alliance. Ukraine has continued to participate in joint exercises with the United States and other NATO countries. Russia has been irked by continuing political consultations between NATO and Ukraine, including on issues affecting Russia, such as the Black Sea Fleet. Ukraine has not contributed substantial numbers of troops to Afghanistan, at least in part due to bad public memories of the Soviet occupation of Afghanistan in the 1980s, but has supported a provincial reconstruction team. According to the

website of the NATO-led ISAF peacekeeping force, Ukraine had 23 soldiers in Afghanistan in August 2012. Also as of August 2012, Ukraine deployed 134 troops to KFOR, the NATO-led peacekeeping force in Kosovo. In September 2012, Ukraine confirmed that it will participate in NATO-led anti-piracy operations off Somalia.

## **European Union**

Ukraine seeks eventual EU membership. Most EU countries have been cool to Ukraine's possible membership, perhaps because of the huge burden a large, poor country like Ukraine could place on already-strained EU coffers. Indeed, EU officials have tried to dissuade Ukraine from even raising the issue. However, Poland and the Baltic states have advocated Ukraine's eventual membership in the EU, in part because they see a stable, secure Ukraine as a bulwark against Russia. Nevertheless, even the most optimistic supporters of Ukraine's EU membership acknowledge that it could be many years before Kyiv is ready to join, but believe that formal EU recognition of Ukraine's eligibility could speed the reform process in Ukraine.

Ukraine currently has a Partnership and Cooperation Agreement (PCA) with the EU, as well as a Ukraine-EU Action Plan within the context of the EU's European Neighborhood policy. The agreements are aimed at providing aid and advice to assist Ukraine's political and economic transition and to promote closer ties with the EU. In 2009, the EU launched the Eastern Partnership program within the context of their European Neighborhood policy, which also includes non-European countries. The EU claims that the regional approach taken by the Partnership (which includes Belarus, Moldova, Georgia, Armenia, and Azerbaijan) improves EU cooperation with these countries.

The EU has budgeted €470 million (\$682 million) in aid for reforms in Ukraine for 2011-2013.<sup>3</sup> The assistance covers such areas as energy cooperation, strengthening border controls, bolstering the judiciary and the rule of law, and addressing environmental concerns.

The EU and Ukraine have initialed an Association Agreement. The agreement, which does not contain a perspective of future membership, includes a free trade accord and will allow for deeper cooperation between the EU and Ukraine in a wide variety of fields. However, EU officials have made clear that the signing of the agreement, let alone its ratification and entry into force, will not occur until after the October 28, 2012, Ukrainian parliamentary elections, when the EU will make an assessment of the state of democracy and the rule of law in Ukraine.

## **Russia**

Ukraine's closest, yet most difficult and complex, relationship is with Russia. President Putin strongly backed Yanukovich's fraudulent "victory" during the 2004 presidential election campaign and reacted angrily to the success of the Orange Revolution. Russian observers with close ties to the Kremlin charged that the Orange Revolution was in fact a plot engineered by the United States and other Western countries. Relations during the Yushchenko presidency were rocky. Russia was irked by Yushchenko's efforts to support greater democratization in the region;

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<sup>3</sup> "See March 2011 EU press release at <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/11/250&format=HTML&aged=0&language=EN&guiLanguage=en>.

impose tighter border controls on Transnistria, a pro-Moscow, separatist enclave within neighboring Moldova; and forge closer links with Georgia.

Ethnic Russians make up 17.3% of Ukraine's population, according to the 2001 Ukrainian census. They are concentrated in the southern and eastern parts of the country. They form a majority in the Crimea (a peninsula in the Black Sea in southern Ukraine), where they make up 58.3% of the population. In the Crimean city of Sevastopol, the home base of the Russian Black Sea Fleet, 71.6% of the population are Russians. In addition, ethnic Ukrainians in the east and south also tend to be Russian-speaking, are suspicious of Ukrainian nationalism, and support close ties with Russia. Russian officials have often tried to play on these regional and ethnic ties, not always successfully.

One of President Yanukovich's top foreign policy priorities has been to improve relations with Russia. In April 2010, Russia and Ukraine agreed to extend the stay of the Russian Black Sea Fleet in Crimea until 2042, from the original withdrawal date of 2017. In exchange, Russia agreed to provide Ukraine with discounted prices for natural gas supplies for 10 years, a benefit that the two sides estimated as worth \$40 billion. Russian companies, with Russian government support, have also stepped up efforts to buy key industrial assets in Ukraine since Yanukovich has come to power. While they have achieved some successes, they have also faced opposition from Ukrainian oligarchs who desire to maintain control of major companies.

However, some of Russia's boldest proposals for improving ties with Ukraine appear to have gone further than Kyiv can support. Yanukovich continues to stress Ukraine's neutral, "non-bloc" status. He has said Ukraine will not join Moscow's counterpart to NATO, the Collective Security Treaty Organization. Russia is pressing Ukraine to join its customs union with Belarus and Kazakhstan. Ukraine has rejected these overtures, saying the customs union is not compatible with the agreements Ukraine signed with other countries before it joined the World Trade Organization. The EU has also warned that it would not be compatible with the EU-Ukraine free trade agreement that is part of the Association Agreement. In September 2012, Ukraine joined a Russian-led Commonwealth of Independent States free trade area.

## **Energy Issues**

The most severe crises in Russian-Ukrainian relations have occurred over energy. Ukraine is heavily dependent on Russia for its energy supplies. About 80% of its oil and natural gas consumption comes from Russia. However, Ukraine's vulnerability to Russian pressure has been mitigated by the fact that the main oil and natural gas pipelines to Central and Western Europe transit its territory. Well over two-thirds of Russia's gas exports have passed through Ukraine in recent years. Ukraine rivals Germany as Gazprom's largest gas consumer. Until the Yushchenko presidency, Russian firms supplied energy to Ukraine at prices far below market rates. Energy sales have been conducted by non-transparent intermediary companies, offering the elites of both countries opportunities to profit. Russia's efforts to increase gas prices for Ukraine to market levels provoked a crisis in 2006 that resulted in cutoff of Russian gas to Western Europe for several days in January 2006. A second gas crisis occurred in January 2009, resulting in a gas cutoff of nearly three weeks.

Russia has sought control of Ukraine's natural gas pipelines and storage facilities. Its efforts have been unsuccessful so far, due to Kyiv's refusal to cede control of one of its key economic assets. This fact, as well as the 2006 and 2009 gas cutoffs, has led Russia and some European countries to plan and build pipelines that would bypass Ukraine. Gazprom is developing gas pipelines

under the Baltic Sea (called Nord Stream) and through the Balkans (called South Stream) to Western Europe. Nord Stream made its first deliveries of gas in 2011, while South Stream is planned to start construction in late 2012, with first deliveries projected for 2015. Gazprom is also planning to increase supplies to Western Europe through the Belarusian pipeline system, over which it gained full control in 2011. Ukraine's reduced share of gas transport to Europe could give Russia more leverage to demand that Ukraine sell it control of its gas pipeline system at a lower price that it otherwise could. Russia could also feel it would have a freer hand to put greater pressure on Ukraine on other issues, including political ones. Key Western European countries could feel they have less of a stake in Ukraine's future, if they, like Russia, were no longer dependent on Ukrainian gas transport infrastructure.

Yanukovich, who is supported by oligarchs who control gas imports and own energy-hungry steel and chemicals industries, has stressed the need to secure lower natural gas prices from Russia. He has sharply criticized the gas agreement between Russia and Ukraine signed by Tymoshenko in 2009, saying that the gas was far too expensive for Ukraine. The April 2010 Black Sea Fleet agreement was one step Yanukovich has taken to try to secure cheaper gas supplies. However, the impact of the deal on gas prices has been less than anticipated, as oil prices (on which Ukraine's gas price is calculated) soared due to unrest in the Middle East.

Russia continues to pressure Ukraine to make further concessions if it wants further gas price cuts. Russia and Ukraine have agreed that Ukraine can pay for its gas in Russian rubles rather than in dollars. Russian banks have provided loans to Ukraine to pay for gas at current prices, perhaps providing Russia with additional leverage with Kyiv. Moscow has tried to persuade Ukraine to join a customs union with Russia, Belarus, and Kazakhstan by offering it cheaper gas if it does so, so far without success. Russia has also advocated the merger of Gazprom with Ukraine's state-controlled gas firm Naftohaz, which would amount to a Russian takeover of the Ukrainian company, due to the former's much larger size. Yanukovich has rejected this project, but has offered Russia part-ownership of Ukraine's gas pipeline system in exchange for guaranteed gas volumes for Ukrainian gas pipelines and access to Russian gas and oil deposits. According to this plan, EU companies would also participate in a new company that would control the gas transit system.

Given Russia's unwillingness to renegotiate the terms of the current gas supply agreement, Ukraine has sharply reduced its import of gas from Russia in 2012. Under the terms of Ukraine's "take-or-pay" contract with Gazprom, Ukraine is obliged to pay for all of the contracted gas, whether it takes it or not, although Russia has refrained from trying to enforce this provision at present. Ukraine has intensified efforts to find alternative sources of supply of energy, including greater use of coal, boosting domestic gas production, and securing supplies of liquefied natural gas from other countries.

## **U.S. Policy**

In a call to Viktor Yanukovich on February 11, 2010, to congratulate him on his victory in the Ukrainian presidential election, President Obama touched on the main themes of U.S. policy toward Ukraine. He noted the "strategic partnership between the United States and Ukraine is based on shared interests and values. These include expanding democracy and prosperity,

protecting security and territorial integrity, strengthening the rule of law, promoting non-proliferation, and supporting reform in Ukraine's economic and energy sectors."<sup>4</sup>

Yanukovich's rejection of NATO membership and his move toward closer ties with Russia (as shown, for example, in the 2010 agreement to extend the stay of the Russian Black Sea Fleet in Crimea) did not provoke public criticism from the Obama Administration. The Administration has instead focused on improving cooperation in such fields as nuclear non-proliferation and energy. However, U.S. officials have expressed increasing concern about backsliding in Ukraine's democratic development.

After a meeting on the eve of the Nuclear Security Summit in Washington in April 2010, President Obama and President Yanukovich agreed that Ukraine would rid itself of the entire stock of highly enriched uranium (HEU) from its soil by the time of the next Nuclear Security Summit in March 2012. The United States agreed to help Ukraine to develop its nuclear research capabilities and diversify its sources of fuel supply for its nuclear reactors. The United States also pledged to continue to cooperate with Ukraine on nuclear safety issues, including the cleanup of the Chernobyl nuclear reactor site. In total, the United States has contributed almost \$240 million to Chernobyl cleanup efforts. At an international pledging conference for Chernobyl in April 2011, the United States pledged another \$123 million.<sup>5</sup>

The two countries are cooperating on energy issues as well. U.S. officials have repeatedly stressed that Ukraine's security depends on diversifying its energy supplies and increasing energy efficiency. Yanukovich has placed more emphasis recently on "energy independence" for Ukraine after repeatedly failing to secure a natural gas price break from Russia. In February 2011, the United States and Ukraine signed a memorandum of understanding on a U.S. Geological Survey effort to help Ukraine explore and develop its reserves of unconventional natural gas. Other U.S. aid programs are aimed at helping Ukraine improve its energy efficiency. In August 2012, the U.S. Trade and Development Agency agreed to fund a feasibility study on restarting production at long-idled, low-yield hydrocarbon deposits in Ukraine.

In October 2011, the White House press secretary issued a statement saying the United States was "deeply disappointed" with Tymoshenko's conviction and sentencing in a "politically motivated prosecution." The statement said that the trial and other incidents raised "serious concerns" about the government's commitment to democracy and the rule of law. The statement called on Ukraine to release Tymoshenko and other opposition figures so that they can take part in the October 2012 parliamentary election. In a brief meeting with President Yanukovich at the March 2012 Nuclear Security Summit, President Obama praised Ukraine for removing all of the highly enriched uranium from its territory. President Obama stressed that Ukraine should hold free, fair, and transparent parliamentary elections in October, and expressed concerns about selective prosecutions of the political opposition.

In August 2012, a State Department spokesman said the United States was "disappointed" by the Ukrainian Supreme Court's rejection of Tymoshenko's appeal of her conviction, and reiterated concerns about the selective prosecution of government opponents. The Administration also

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<sup>4</sup> Press release from the White House website at <http://www.whitehouse.gov/the-press-office/readout-presidents-call-with-president-elect-yanukovich-ukraine>.

<sup>5</sup> U.S. Participation in the Kyiv Summit and the Chornobyl Pledging Conference: Fact Sheet, April 19, 2011, from the State Department website at <http://www.state.gov/r/pa/prs/ps/2011/04/161228.htm>.

criticized Lutsenko's conviction on additional charges in August, and the intimidation of independent media.

## **Congressional Response**

### **U.S. Aid to Ukraine**

According to the USAID "Greenbook" website, the United States obligated \$3.5 billion in aid to Ukraine from FY1990 to FY2010. According to the FY2012 Congressional Budget Presentation for Foreign Operations, in FY2011, the United States provided \$123.243 million in aid to Ukraine. In FY2012, Ukraine is slated to receive \$113.878 million.

On December 23, the President signed the Consolidated Appropriations Act, 2012 (P.L. 112-74), which contained foreign operations funding. The conference report directs the Secretary of the Treasury to keep the appropriations committees informed on the issues of export quotas, allocation of grain licenses, VAT tax refunds, and repression of fundamental rights in Ukraine, including due process of law and freedom of expression and association. The conferees also expressed support for forest management programs and programs to fight tuberculosis and HIV/AIDS in Ukraine.

The Administration requested \$104.407 million in aid for Ukraine for FY2013. Of this amount, \$53.957 million is allocated to the Economic Support Fund (ESF) account, \$27.2 million from the State Department Global Health Programs account, \$7.9 million from the AID Global Health Program account, \$7 million in Foreign Military Financing, \$1.9 million in the IMET military training and education account, \$4.1 million in the International Narcotics Control and Law Enforcement account, and \$2.35 million in the Nonproliferation, Antiterrorism, Demining and Related Programs account.

A significant portion of U.S. aid to Ukraine in the ESF account for FY2013 is dedicated to improving the safety of the Chernobyl nuclear facility, including finishing the construction of the containment structure over the damaged reactor and securing and storing spent nuclear fuel. Other ESF programs are aimed at improving governance and increasing the accountability and effectiveness of the justice system. Global Health funding will help Ukraine fight its HIV/AIDS crisis, which is the most severe in the region. Security assistance for Ukraine is aimed at helping Ukraine's defense reform efforts, improving operability with U.S. and NATO forces, and taking steps to boost Ukraine's military capabilities. U.S. assistance has helped Ukraine destroy its stock of SCUD short-range missiles and make progress toward the elimination of its stock of propellant for SS-24 ICBMs.

The committee report (H.Rept. 112-494) to H.R. 5857, FY2013 the State-Foreign Operations appropriations bill, expresses the committee's concern about "recent declines in democratic governance [in Ukraine], particularly the abuse of power to create unfair conditions for political competition, and encourages close monitoring by the Department of State of upcoming national elections."

### **Other Legislation**

Legislation on Ukraine has been introduced in the 112<sup>th</sup> Congress. On January 26, 2011, Representative Kaptur introduced H.Res. 66, which supports the establishment of a staff

exchange program between the House of Representatives and the Verkhovna Rada, Ukraine's parliament. On April 14, 2011, Senator Lugar and Senator Kerry introduced S.Res. 153, which recognizes the 25<sup>th</sup> anniversary of the Chernobyl nuclear accident. The resolution was adopted by unanimous consent on May 9, 2011.

On September 15, 2011, Representative Sander Levin introduced H.Res. 401, which expresses support for Ukraine on the 20<sup>th</sup> anniversary of its independence. The resolution also notes concerns about the Tymoshenko case and other problems with Ukraine's democratic development. On October 13, 2011, Representative Kaptur introduced H.Res. 435, which condemns the persecution of Tymoshenko, former Interior Minister Yuri Lutsenko, and other political prisoners.

On March 22, 2012, Representative Turner introduced H.R. 4243, the NATO Enhancement Act of 2012. The bill includes reauthorization of programs to facilitate the transition to NATO membership for eligible countries. However, it makes clear that the fact that Ukraine is no longer seeking membership "shall not inhibit security cooperation in terms of interoperability, training, reform, joint exercises, and bilateral exchanges with nations previously designated as eligible to receive security assistance under this Act." A Senate companion bill, S. 2177, introduced by Senator Lugar, contains the same provisions.

In May 2012, Senator Inhofe introduced S.Res. 466. The resolution condemns the imprisonment of Tymoshenko as politically motivated and calls for her release. Until she is released, S.Res. 466 calls on the Organization for Security and Cooperation in Europe to not allow Ukraine to assume the chairmanship of the organization in 2013; urges the State Department to withdraw the U.S. Ambassador to Ukraine and suspend embassy operations and initiate a visa ban against President Yanukovich and others responsible for Ms. Tymoshenko's imprisonment; and calls on NATO to suspend all cooperation agreements with Ukraine.

In July 2012, Representative Christopher Smith introduced H.Res. 730, which calls on Ukrainian authorities to release Tymoshenko and other victims of selective justice, and to hold free and fair parliamentary elections in October 2012. The resolution calls for the United States to deny visas to Ukrainian officials "involved in serious human rights abuses, anti-democratic actions, or corruption that undermines or injures democratic institutions in Ukraine, including officials responsible for and participating in the selective prosecution and persecution of political opponents."

## **Author Contact Information**

Steven Woehrel  
Specialist in European Affairs  
swoehrel@crs.loc.gov, 7-2291