

**Russia-EU common energy
space – how to create it best:
New Bilateral Russia-EU
Partnership Agreement? Export
of EU “acquis communautaire”?
Energy Charter Treaty!**

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Common energy space demands common rules – what options for common rules in energy between Russia & EU?

- 1) Export of EU *acquis communautaire* ?
- 2) New bilateral Russia-EU treaty – “based on the Energy Charter principles” ?
- 3) Energy Charter Treaty !

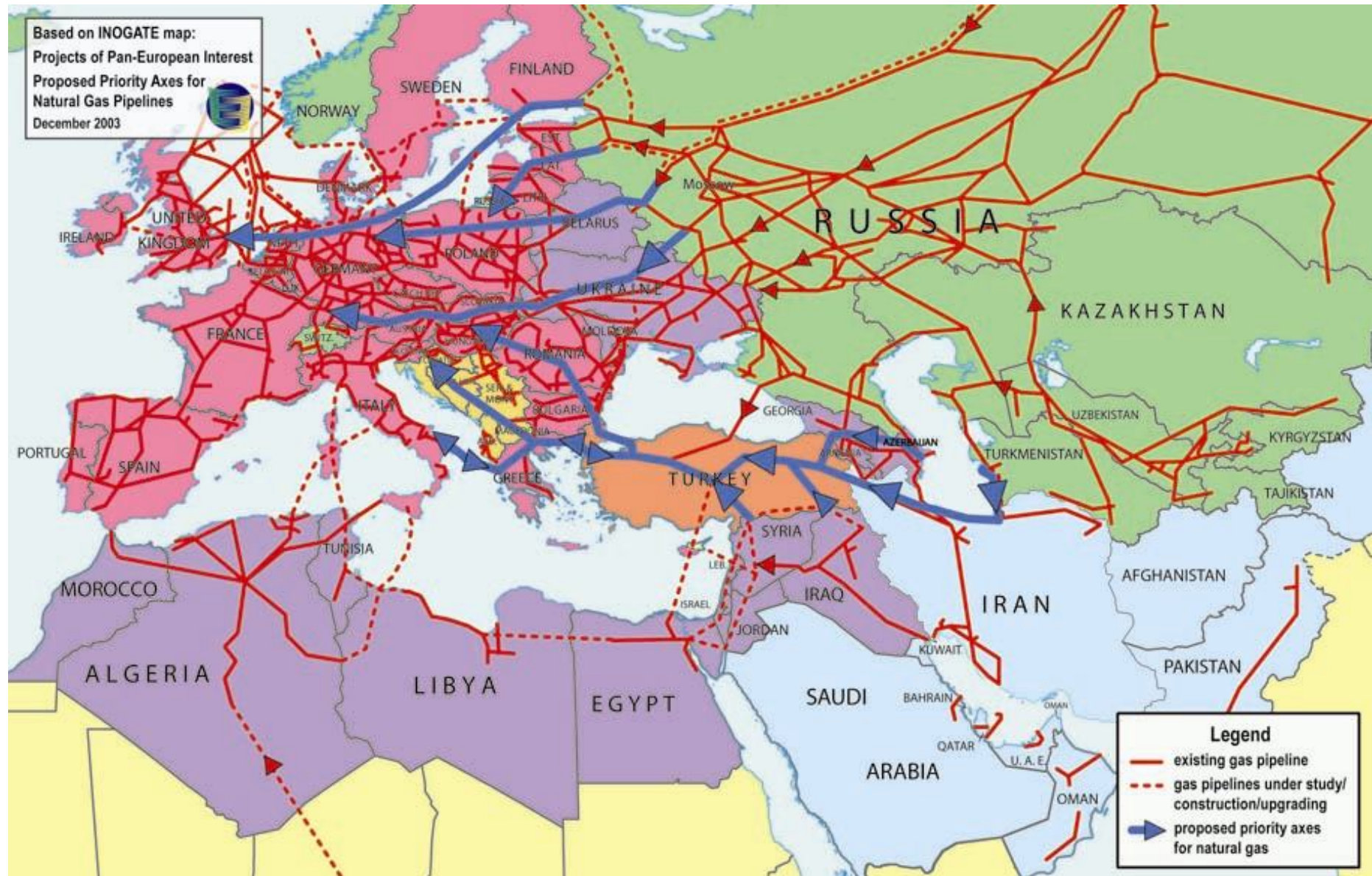
Option 1: Export of “acquis communautaire”

- EU’s preference: for EU, harmonization of EU legislation with legal systems of thirds states means basically application of EU legislation within these third states, incl. in energy => “export of acquis”
- EU tries to expand geographical area of implementation of acquis in energy:
 - EU enlargement (EU15=>EU25=>EU27=>EU27+?)
 - EU-SEE Energy Community Treaty
 - EU Neighborhood Policy
 - EU has even initially included Russia in this Policy => strong negative respond from Khristenko to Lamoureux,

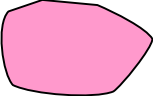
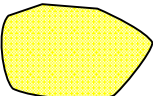
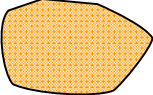
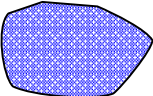

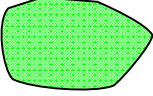
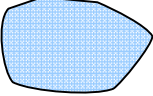
but

- EU acquis does not (and will not !) cover all segments of energy (gas) value chains destined for EU and originated from Russia & other key non-EU producers (Central Asian states, Iran, etc.)

Common rules of the game in Eurasian energy & export of EU's acquis



Common rules of the game in Eurasian energy & export of EU's acquis ? (legend)

Zone	States within the zone	Description
	EU Members: 27 EU countries	EU legislation, including the energy legislation, is fully applicable
	Energy Community EU-SEE Countries: Croatia, Serbia, Montenegro, Croatia, Bosnia, FYROM (Macedonia), Albania, UNMIK (Kosova); other Energy Community members are already EU members	Only EU legislation on internal electricity and gas markets is applicable
	EU Candidate Countries: Turkey (Croatia is already an Energy Community member so applying the EU energy market acquis)	Still in the process of alignment to the EU legislation but full compliance not likely before membership
	EU Neighbourhood Policy Countries: CIS (Armenia, Azerbaijan, Belarus, Georgia, Moldova, Ukraine) and Northern Africa (Algeria, Egypt, Israel, Jordan, Lebanon, Libya, Morocco, the Palestinian Authority, Syria, Tunisia)	Enhanced energy cooperation based on National Action Plans with Ukraine and Moldova (as well as with Israel, Jordan, Morocco, the Palestinian Authority and Tunisia); partial application of EU energy policies and legislation may be possible in the future
	EU-Russia Strategic Partnership: EU & Russia	Based on shared principles and objectives; applicability of the EU legislation in Russia is out of question
	ECT member-states: 51 states of Europe & Asia	ECT is fully applicable within the EU as minimum standard; EU went further in liberalizing its internal energy market, BUT whether EU can demand that other ECT member-states follow same model and speed of developing their domestic markets?
	ECT observer-states: 20 states of Europe, Asia (e.g. Middle East, South-, SE- & NE-Asia), Africa, North & Latin America	Shared ECT aims & principles; did not take ECT legally binding rules; not ready to take more liberal rules of EU Acquis

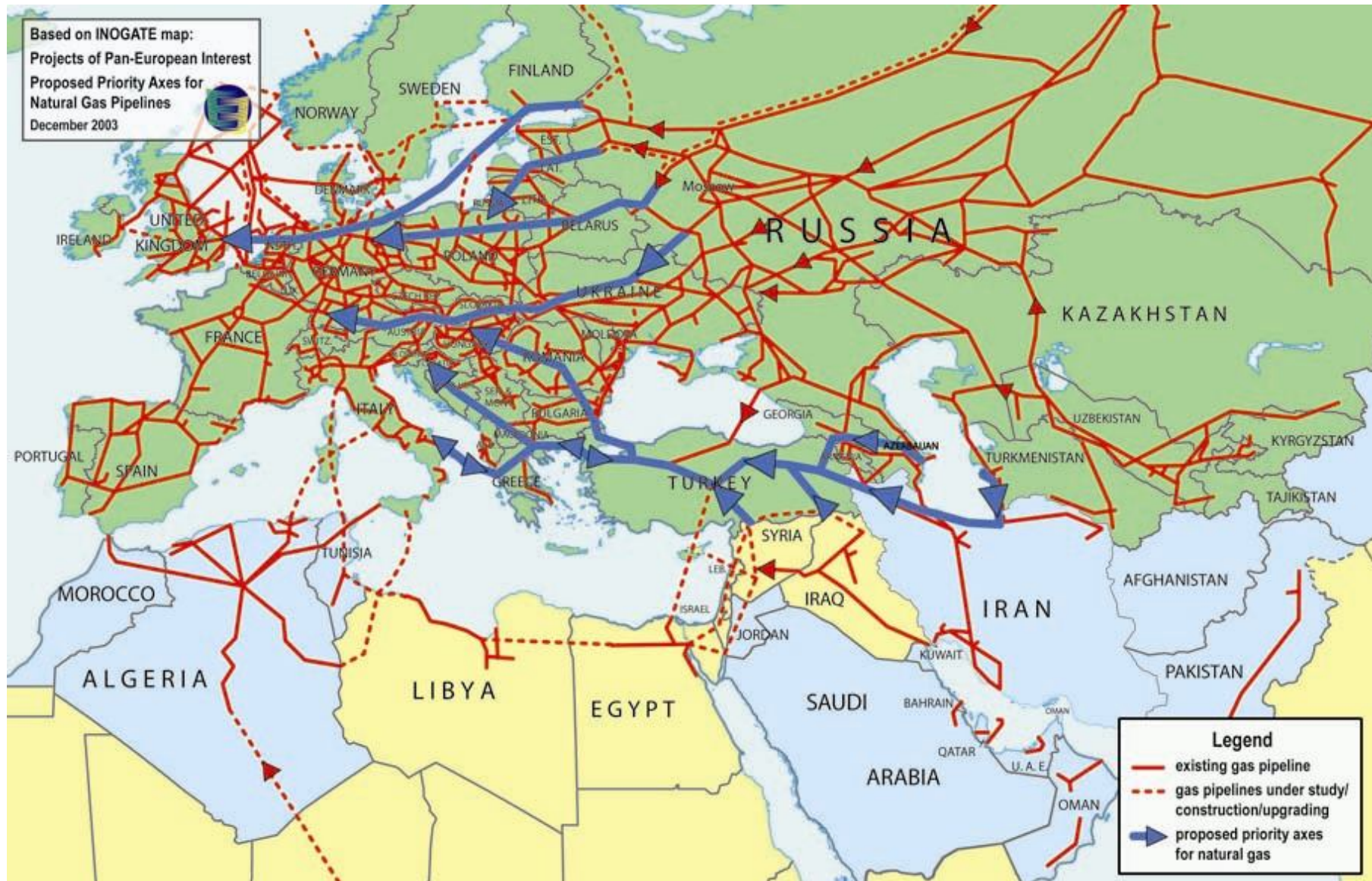
Option 2: New bilateral Russia-EU treaty – “based on the Energy Charter principles”

- Russia’s compromise proposal – some supporters in EU, *but*
- Any bilateral Russia-EU Treaty (PA) does not cover transit states between Russia & EU,
- If it based on “Energy Charter principles”:
 - What does this mean operationally? Different wording of ECT provisions in new PA? => if so, possibility for two standards (under new PA & under ECT) of (i) implementation of “provisions based on ECT principles” & (ii) of their interpretation in different arbitrations => instead of diminishing legal risks, this would increase such risks & the cost of capital for Russian and EU investors in energy projects of mutual interest,
 - To negotiate today new Russia-EU legally-binding Treaty (27+1+1 CPs) is much more difficult task than it was in early 1990’s with PCA & ECT negotiations (then - window of political opportunities, not now) => (3 open issues between Russia & EU in draft Energy Charter Transit Protocol took 6+ years already) => when this new broader Treaty can be finalized and ratified ? => risk of failure of new negotiations

Option 3: Energy Charter Treaty as a legal background of Russia-EU common energy space

- ECT (incl. members & observers) covers all major current & future energy (gas) value chains to EU => minimum standard of common rules in a broader area than just Russia-EU space
- Optimal solution: Russia-EU PA energy chapter = ECT is a legal background of Russia-EU common energy space
- ECT (in force since 1998) is already a common legal background within 51 Eurasian states, incl. Russia & EU:
 - EU: ratified by all EU member-states & by EU => ECT is already an integral part of the EU acquis,
 - Russia: signed & applied on provisional basis (ECT Art.45) => Russia still to ratify ECT => this is crucial if ECT to become common legal background of Russia-EU common energy space

Common rules of the game in Eurasian energy & expansion of ECT



Russia ECT ratification: what obstacles?

- **Political concerns**

- Natural reaction on external political pressure on Russia to ratify ECT without considering Russia's concerns (like "Russia *must* ratify ECT" – f.i. Barroso et al prior to 2006 G-8 St.Petersburg Summit)
- Based on misinterpretations of ECT from both sides =>
 - part of Russian politicians, opposing ECT, just did not read ECT (f.i., concerns as if ECT requests mandatory TPA, etc.), *but*
 - Russian politicians reacts mostly not to the ECT provisions, but to their (mostly questionable or incorrect) interpretations by EU officials echoed by international press (like "ECT opens access to Gazprom transportation system at low domestic tariffs", etc.)

- **Concerns as "negotiating tool"**

- To possess something to give up later in search of compromise
- All general concerns regarding what is *not* present in the ECT (like "ECT does not address problems of Turkish & Danish straits", etc.)

- **Valid & substantiated economic concerns**

- 2001 Parliamentary Hearings: Russia will return to ECT ratification question after all her valid concerns are adequately addressed => two issues in regard to transit (ECT Art.7) => to be addressed in Transit Protocol => no ECT ratification without TP (Khristenko) => open issues in TP itself preventing its finalization

Russia's ECT ratification & TP: how to proceed?

- **Option 1:** Russia first ratify ECT, afterwards Energy Charter community finalize & ratify TP => demand of EU, impossible for Russia
- **Option 2:** first finalize & ratify TP (with full consideration of valid Russia's concerns), afterwards Russia returns to ECT ratification issue => impossible by ECT rules (no state can join Energy Charter Protocol if not first ratified ECT)
- **Option 3** = the only workable compromise: Russia will ratify ECT & TP simultaneously => ECT community need to concentrate on practical ways of solving this problem

ECT & TP: 2 + 3 = 5 open issues on transit

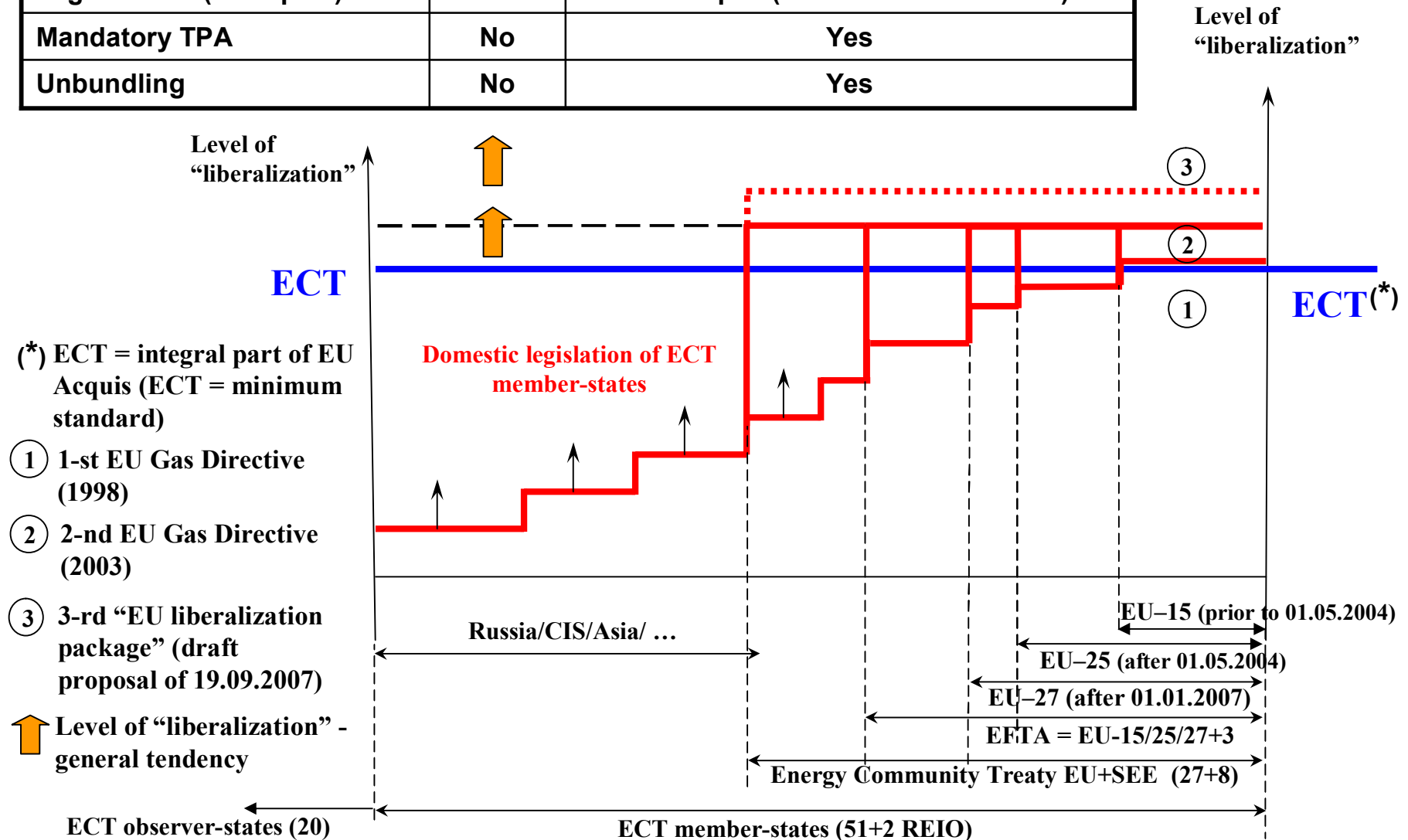
- 2 open issues in ECT (Art.7) for Russia:
 - Transit vs. domestic tariffs (ECT Art.7.3)
 - Conciliatory procedure (ECT Art.7.6-7.7)
- 3 open issues in draft TP for Russia & EU:
 - Auctions & cost-reflectiveness of transit tariffs (TP Art.10) => new article on congestion management (TP Art.10bis)
 - Problem of contractual mismatch (long-term access to transportation capacities for long-term supply contracts within unbundled energy systems) (TP Art.8)
 - Implementation of Transit Protocol within EU => EU proposal in TP Art.20/“REIO clause”: transit = if energy flow crosses whole EU territory and not territory of its individual member-states => key issue of disagreements between Russia & EU = internal EU issue (correlation between ECT and acquis within EU) => a key to ECT ratification by Russia is in EU hands
- Technical solutions to all issues (except REIO clause) agreed in principle informally at multilateral level; way forward on REIO clause agreed multilaterally with major input from Russia & EU (October 2008 TTG Group meeting)

Key EU problems regarding ECT

- EU ratified ECT in two capacities: (a) each EU member-state and (b) EU as a whole (as REIO) => internal EU problems (“transit” according to ECT & TP/REIO clause, dispute settlement within EU, etc.)
- Increasing gap between level of liberalization of (a) internal energy market(s) within EU [First 1996/98 => Second 2003 => Third 2009 (?) EU Directives] and (b) ECT as a minimum standard for broader Eurasian community => different ECT vs EU acquis approaches (NTPA vs MTPA, unbundling, etc.) =>
 - ECT as an instrument of protection of non-EU and EU companies against “excessive” liberalization of internal EU energy space ?
- EU as ECT CP: ECT = international treaty, EU acquis = domestic legislation for EU => ECT to dominate over EU acquis =>
 - companies from EU member-states can litigate against EU (f.i. against Third liberalization package) in international arbitration courts outside EU (ICSID, UNCITRAL, SCC) based on ECT provisions => f.i. “ownership unbundling = expropriation” [EU gas company] => ECT Art.13 (on investment protection)
- Whether EU would really like to have ECT as a legal background of Russia-EU common energy space?

ECT & EU acquis: “minimum standard” within evolving Eurasian common energy space vs. more “liberalized” model

Legal norms (examples)	ECT	EU Acquis (2-nd EU Gas Directive)
Mandatory TPA	No	Yes
Unbundling	No	Yes



Option 3 (ECT-based): how to proceed

- Finalize & sign Transit Protocol, incl. to cover Russia's substantiated concerns on transit both in TP and in ECT,
- Address other substantiated Russia's concerns re ECT of multilateral character (closed list to be presented by Russia to ECT community),
- Russia simultaneously ratify ECT & TP,
- Russia-EU PA energy chapter: "ECT is the legal basis of Russia-EU common energy space"; PA energy chapter entering into force linked to Russia's ECT & TP ratification,
- After all ECT members ratify ECT (today: 46 of 51) => further development of ECT based on current policy debate (Ad Hoc Strategy Group discussions aimed at 2009 Energy Charter Policy Review – ECT Art.34.7) on new challenges & risks of energy markets developments and how to most effectively address them by further improvement & expansion of ECT