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Towards a new community energy policy?

In the energy political conditions of the 21st century, Europe, too, faces new challenges. Adapting to these conditions, solving today's problems is impossible by using yesterday's answers; new and more efficient solutions must be found. The 25 isolated national energy policies are no longer suitable for the solution of problems; a better coordinated, community-level energy policy is required.

SECURITY AND COMPETITIVENESS

Global demand for energy is increasing. By 2030, global energy demand and CO_2 emissions are expected to rise by some 60 per cent. Our climate is getting warmer. (As revealed by surveys, the average temperature on Earth has risen by 0.6 degrees Celsius and, unless further preventive measures are taken, there may be an increase of between 1.4 and 5.8 degrees by the end of the century.) Oil and gas prices are increasing (in the EU, they have doubled in the past two years). The energy import dependency of the EU is growing, with energy being imported mostly from politically risky regions. The EU depends on energy imports for 50 per cent of its current consumption, which, unless energy can be made more competitive, could reach 70 per cent in the next 20 to 30 years. Energy reserves are concentrated in a few countries. Half of the EU's gas demand comes from three countries (Russia, Algeria and Norway). In the next 25 years, some 80 per cent of gas consumption will be covered from imports.

By today, security of supply in Europe has become multi-dimensional and jeopardized in several aspects, being characterized by an external dependency on gas supplies from Russia and oil supplies from the Middle East, terrorist threats to energy establishments, as well as the ageing of European oil refineries and power stations as a consequence of low investments in the past two decades.

Both the expectations regarding security of supply and the requirements of the EU Emissions Trading Scheme can be met through major investment policies. The volume of the necessary investments and the weight of the problem are indicated by the fact that, according to EU estimations, investments of around EUR 1 trillion will be needed over the next 20 years to meet the expected energy demand and to replace ageing infrastructure. All of these must be implemented by keeping up competitiveness. The energy market of the EU is not yet competitive today; an internal energy market has not been developed. It is only a fully liberalized market that can create the condi-

tions for minimizing losses, fighting rising prices and efficiently joining the fight against climatic change. Without a fully liberalized market, consumers cannot enjoy the benefits of a competitive market like low prices or the security of supply. It is essential to interconnect the national energy markets, which are mostly still isolated today.

The acknowledgement of the above was reflected by the informal summit of Heads of State and Government at Hampton Court in October 2005, where chairman of the summit, British Prime Minister *Tony Blair,* tabled a proposal[1]. It was here that the Commission was invited to lay down the basis for a common energy political approach.

THE CHARACTERISTICS OF THE COMMUNITY ENERGY POLICY BEFORE HAMPTON COURT

The development of the Common European Energy Policy goes back to the establishment of the European Coal and Steel Community and the European Atomic Energy Community. Both of these were later incorporated into the Treaties that formed the legal basis for the European Union, yet energy policy as such is not part of the Treaty. The Union lacks a common energy policy even today, which decreases the EU's negotiating weight in international energy affairs. The awareness of a structural vulnerability related to energy has been present in the Community since the very beginning of European integration.

The Treaty establishing the European Coal and Steel Community, signed in Paris in 1951, ruled under its objectives, with reference to goods specified in the Treaty, the elimination, as between Member States, of any import or export duties or quantitative restrictions as well as any discriminatory regulations regarding producers, customers or consumers, with special regard to prices, delivery conditions and transportation charges.

The Treaty establishing the European Atomic Energy Community, signed in Rome in 1957, was aimed at facilitating the cooperation of Member States in research and the dissemination of technical information, the use and development of nuclear energy, the application of security standards as well as in the field of health protection.

Chapter 2 of the Second Article of the Rome Treaty rules on the elimination, as between Member States, of quantitative restrictions and of all other measures having equivalent effect. Article 37 rules on state monopolies of a commercial character, which are highly significant from the point of view of the energy market as well. Member States must ensure that public undertakings and undertakings with exclusive or special rights (which latter include electricity-industrial and natural gas industrial companies, irrespective of whether they are public, or privately owned) do not impose quantitative restrictions or any other measures of equivalent effect on exports and imports. In addition, Member States are obliged to adjust state monopolies of a commercial character so as to ensure that when the transitional period has ended, no discrimination regarding the conditions under which goods are procured and marketed exists between the nations of the Member States.

Under the regulations of the Rome Treaty on undertakings, an important rule regarding the energy sector is that undertakings entrusted with the operation of services of general economic interest are also subject to competition rules (insofar as the application of such rules does not hinder the performance of the particular tasks assigned to them).

Common commercial policy affects the energy sector in a way that, under Article 115, commercial political measures of a national nature are allowed only at times of economic difficulties.

Under Article 129 enacted by the Maastricht Treaty, signed in 1992, the Community, with the aim of facilitating a market without internal frontiers as well as economic and social cohesion, shall contribute to the establishment and development of trans-European networks in the areas of transport, telecommunications and energy infrastructures.

From the moment of its establishment, the Coal and Steel Community aimed higher than establishing a mere cooperation of energy sectors: it was the creation of a united Europe that its founding fathers had in vision. Being based on the cooperation of the coal and steel industries, both critical in the industry of the region, the Community determined economic development, as well as the rate of growth. Under the original plans, the cooperation was to include other branches in addition to coal and steel. Thus, it was through these treaties that the construction of the European Union began, but it was only from the 1990's, by initiating certain legislation on energy, that the European Commission paved the way for the establishment of a Common Energy Policy.

According to the Constitutional Treaty (III. 256), under ratification, the objectives of the energy policy of the European Union are to ensure the operation of the energy market and the security of supply of the Union, encourage energy efficiency and energy saving, as well as promote the development of new forms of energy. As it is underlined in the chapter referred to above, the Community Energy Policy shall respect the right of Member States to freely decide on the choice of their energy mix.

Today, Common Energy Policy can be identified as part of the Union's economic policy based on integration and deregulation, which is expected to contribute to the development of a single market as well as the creation of social cohesion. Within the general objectives, the energy policy must harmonize the aspects of security of supply (including the efficiency of energy supply), competitiveness and environmental protection. In the effort for creating a Common Energy Policy, there is an emphasis on the correlation between sustainable energy use and climatic change. Within the framework of the latter, limiting energy consumption and diversifying energy sources are the major goals.

THE COURSE OF DEVELOPMENT OF ENERGY POLICY

Although there was significant progress in European integration between 1957 and 1972, this was not apparent in energetic cooperation. A drawback to the formation of a common energy policy was that there were few areas where the interests of Member States in fact coincided. As regards the problem of Member States security of supply, this in itself was not a strong enough driving force making a common energy policy necessary. The latter was proved by the fact that the explosion of oil prices in the 1970's and the difficulties in energy supply did not advance the cause of a community energy policy. It was the Commission that made the initiatives for the formation of a common energy policy from the late 1980's onwards, which was related to the rebirth of the European Union: the Single European Document (1987) and Maastricht (1993). The processes were determined by the strengthening of supranationality, which typically left the field of energy unaffected. The fact that there were still some changes maturing in the community energy policy was due to activities unfolding in other fields related to energy. In the first place, it was the policy aiming at the formation of an internal market, in which competition policy had a major role, which fostered the community energy policy. The vision of an internal energy market for the Union was to a great extent affected by the efforts enforced

within OECD at that time, which had urged more liberal solutions in the energy sector for a long time.

In the second place, the Community created a firm environmental policy. By the early 1990's, the environmental policy had undergone two substantial changes: unlike energy policy, it was incorporated into the EC Treaty (following the Single European Document), and the horizontal feature of the industry also became apparent. Since then, the increasing weight of environmental policy within the community policies has been a major challenge to energy policy.

In the third place, the development of the community energy policy was also related to foreign political considerations, as the Union started to play an increasingly active role in international, world political affairs. Economic relations established with certain third countries (from the Middle East, North Africa, CIS) were meant to strengthen the Union's security of supply, complementing the efforts of the Member States for more efficient energy use, so to say.

Yet, the energy issue was not genuinely represented either in the Maastricht, or in the Amsterdam Treaty. The Union had no vision of a common energy policy, either. Under these circumstances, the Commission had a considerably wide scope for action when working out the directive proposals determining energy policy. These include two important directives[2] ensuring the free movement of electricity and natural gas across the borders of Member States, which, despite the resistance of Member States, argued for more open markets, also setting out the timetable and procedures of market liberalization.

The liberalization of energy markets and the implementation of efforts aimed at increasing security of supply are adversely affected by the unsatisfactory conditions of the energy transit and storage infrastructure. Today, connections between Member States are restricted to bilateral relations, which is a major obstacle to the formation of an integrated European energy market. At the moment, the internal energy market of the Union is a collection of national markets, where cross-border trade is restricted, security of supply is low and competition is limited. Every new connection would increase the security of supply and have advantages for across Europe as a whole. Without the further development of the trans-European energy network, the internal energy market is unable to fulfill its function and its operational breakdowns distort competition. This is why the Union urges developments interconnecting Member States, ensuring the further liberalization of the energy market, as well as working out a regulatory framework facilitating investments in the industry, which is also pressing because of the internal energy market integration of new Member States[3].

The revision of the Lisbon strategy made it clear that, without further increasing energy efficiency, it was impossible to increase the competitiveness of the Union. The Green Paper on Energy Efficiency[4] says that, by changing consumer habits and by the application of energy efficient technologies, energy consumption could be cost-efficiently reduced by 20 per cent by 2020. According to preliminary calculations, that would release some EUR 60 billion per year (which equals the annual energy consumption of Germany and Finland together).

The Union has made advance not only in the fields of market liberalization and environment protection (the objectives set with regard to the use of renewable energy sources) but has also taken several important initiatives in high-priority fields of energy policy like energy efficiency and the promotion of new energy technologies[5]. The proposals were made by the Commission without an actual mandate, relying only on the “good intention” and common sense of Member States.

In late 2005, the Commission made a report on the almost five years' experience of the operation of the competition market, assessing the achievements made in the establishment of the electricity and gas markets, before the energy market was to be fully opened up to all consumers on July 1, 2007.[6] The Commission established that competition was not yet implemented at the European energy markets and that the major obstacles to the unfolding of competition were market concentration, verticality, the lack of market integration, the lack of transparency and problems related to pricing. The gas and electricity markets were highly concentrated – although to different extents in various countries – so undertakings with a dominant position were able to exercise market influence. Power stations, using the capacity at their disposal, were able to influence prices, too. The findings also confirmed that the separation of network and sales activities was insufficient, which was an obstacle to the operation of the wholesale market. This, in turn, made the entrance of new market players impossible. System-connection capacities, the key elements of integration, were insufficient and thus prevented consumers from access to alternatives to national suppliers. The lack of price transparency furthermore added to the lack of confidence of industrial and retail consumers[7].

In compliance with the decision made at Hampton Court, the Community launched common thinking on the basic principles of the Community Energy Policy and the specification of areas where action was imperative. The need for the formulation of a more integrated energy policy was made more pressing by the Russian-Ukrainian gas dispute, which cast the light upon the common energy security policy, or rather, on the lack of such policy. Difficulties of supply highlighted the contradiction that, while there was community legislation for the regulation of energy markets, the security of energy supply was "only" national competence, i.e. the Union lacked a community policy for security of supply. At the same time, the establishment of a single, European-level liberalized energy market (electricity, gas) means that any gas or electrical energy supply disorders in individual countries or a region of the Union would spread to other Member States despite the fact that the latter have taken the necessary measures for the security of their supply at the national level. The currently ruling principle that Member States are to provide for the security of their supply individually thus cannot be followed in the long run. This principle is not in compliance with the objective of the establishment of a single natural gas and electricity market free of restrictions.

In the debate on working out the New Energy Policy, new Member States of the Union, which are most exposed to unilateral dependence, including Hungary, urged common security of supply measures in the fields of natural gas and electricity supply, similar to those earlier implemented in the case of crude oil products[8]. Beyond this, the diversification of energy sources and transportation routes, as well as the improvement of energy efficiency were also considered important.

France suggested that all Member States should have analyses on mid-term perspectives for energy demand and supply, which should be summarized by the Commission with the aim of establishing the investment in production, transport and storage required for making the demand-supply balance, determining quotas for greenhouse gas emissions. It urged that the Union should have a common vision for long-term energy supply shared by all Member States. France also recommended measures to facilitate the operation of the single gas and electricity markets (harmonizing the competence of European regulators, improving the cooperation of energy supply networks). For the diversification of energy supply and the improvement of security of supply, it empha-

sized the importance of facilitating and speeding up the development of TEN-E networks. For the efficient solution of mid- and long-term difficulties in gas supply, it urged the further development and amendment of Directive 2004/67/EC[9]. Ensuring the transparency of the European oil market, France suggested regular reports on European oil stocks. It drew attention to the significance of using nuclear energy in the creation of safe energy supply for the Union and in the combat against climatic change. It urged that, in research and development, priority should be given to new energy technologies and that the Union should favor the development of "clean energy" technologies also in its relations with third countries, emphasizing the advantages of the Kyoto agreement.

Considering the basic principles of the energy policy, *Germany* emphasized the priority of completing the liberalization of the internal energy market, for which it was essential to implement the common rules on the establishment of the internal energy market and to improve the coordination of cross-border energy trade at the regional level. Germany maintained that, in the creation of security of supply, it was energy efficiency that had a critical role, followed by the optimal utilization of national energy resources. It was the task of Member States to ensure sufficient gas stocks, necessary for covering the national demand in case of crisis. Germany urged the efficient and transparent implementation of the existing legislation, considering this sufficient for the advance towards a more communal energy policy.

During the debate, the opinion that the energy policy needed a supportive foreign policy became increasingly clear. Considering that Russia played a key role in the energy supply of the Union, the Union should give priority to Russia in the series of various dialogs, making Russia conscious of its responsibility for the security of supply of the Community[10]. Regional energetic cooperation in the internal market was a further element of the community energy policy, Member States mentioned. Within the framework of the latter, they emphasized the need to ensure that the Energy Treaty with Southern Europe take effect in 2006[11], suggested extending membership to the Ukraine and Norway and urged an agreement of a similar nature with countries of the Caspian-basin, rich in energy sources, as well as with Moldavia. It was necessary, furthermore, to diversify energy sources and supply routes and to establish the suitable network infrastructure, including such for the transit of liquefied gas. As Poland pointed out, the Union needed, in addition to its critical East-West infrastructure, the establishment of a North-South axis, too. Member States agreed that, within the framework of the Community Energy Policy, a solidarity mechanism serving the solution of supply crises was to be established.

Member States emphasized the importance of passing an ambitious Action Plan, meant to further improve energy efficiency, in the year 2006 and the revision of the EU Emissions Trading Scheme in the same year. Considering the aspects of European competitiveness, the latter revision was to cover all energy intensive industries.[12]

Despite the different approaches and emphases, there was wide consensus among Member States that action at the European level was imperative. Since the establishment of the Community, there had never been such a strong demand for the formulation of an integrated energy policy, yet, countries of a critical weight regarding the essence of the issue had a careful approach[13]. Especially the old Member States of the Union shared the view that the formation of the community energy policy could only be started after the establishment of the internal energy market by mid-2007. There

were only a few countries (Belgium, France and Lithuania) that formulated a demand for a genuinely new and ambitious European Energy Policy, underlining that Europe should speak with a single voice in foreign policy, since only so could its voice be heard in the world.

Proposals of the Green Paper

Concurrently with the activity of the work group on energy of the Council, the Commission completed their activity in the field, publishing the Green Paper[14] on March 8, 2006, with the following political proposals.

The Green Paper identifies the goals of the common European energy policy in ensuring sustainability, competitiveness and security of supply. In terms of geographical places, this means Kyoto, Lisbon and Moscow, i.e. the Kyoto Protocols for the mitigation of the effects of global warming, the Lisbon strategy ensuring higher competitiveness for the EU as well as Moscow, playing a key role in the energy supply of the Union.

The Green Paper identifies six areas where measures and action are necessary so that the Union is able to successfully meet the energy challenges of the 21st century.

❶ Plans for completing the internal electricity and gas markets and for increasing their efficiency, including establishing a European Energy Regulator and ensuring the better coordination of access to networks.

Since the connection of networks necessary for the single market is impossible without increasing physical capacity, the interconnection plan, which encourages the establishment of cross-border gas and electricity capacity at several places, is of primary importance. The importance of unbundling production, distribution and service activities as the basic condition for ensuring efficient market competition is also highlighted. The significant energy development requirements of the future make it necessary to create the conditions for new investment in the energy infrastructure. A better coordinated cooperation is required between regulatory and competition organs so that competitiveness can be improved.

❷ A stronger cooperation between Member Sates based on the principle of solidarity for a secure energy supply, including revising the EU stance on emergency oil and gas stocks as well as the possibility of new legislation on gas stocks. The Green Paper says that Member States must improve their cooperation to make sure that the information on the status of community oil stocks can be made public more regularly and in a more transparent way. The Green Paper also includes a proposal on the establishment of a European Energy Supply Observatory, the headquarters of which Budapest has also aspired to host.

❸ The strategic revision of the energy policy of the Union, while respecting various national energy political decisions, as well as making analyses serving as the basis for sustainable, more efficient and more diverse energy mix and energy goals, which could also serve as the framework for working out the national energy strategies. The strategic analysis would cover the examination of the advantages and drawbacks of all sources of energy. The latter is all the more necessary because Member States make their own choices on the energy mix they wish to use, but their choices have an impact on the energy security of their neighbors and, inevitably, on the Union as a whole.

❹ An integrated approach to tackle the problem of climatic change, based on an Action Plan on energy efficiency, as well as the preparation of a new Road Map for the further utilization of renewable energy sources, including the targets to 2020. The Green Paper plans to ensure the 20 per cent reduction in energy consumption, targeted for 2020, by campaigns promoting energy saving, financial means foster-

ing energy efficiency investments, as well as better information on the capacity of energy consuming equipment.

❺ For the promotion of innovation, the EU needs a strategic energy technology plan that would eliminate parallelism in national technological and research policies and, by establishing joint technological initiatives/enterprises, it would ensure that European industries become world leaders in the market of new energy technologies. Regarding the latter, a more strategic financing of energy-related research is advisable. In the field of technological development, the Commission assigns an important role to the recently proposed European Technological Center.

❻ A consistent external energy policy, to be implemented at the levels of both the Community and the Member States, speaking with a single voice, serves the efficient solution of the energy challenges that Europe faces. To this end the Commission urges identifying infrastructure priorities for the Union's security of supply and preparing a pan-European energy community treaty. With regard to the critical role of Russia in the energy supply of the Union, the Green Paper underlines the need for the establishment of a new energy partnership. A genuine partnership would mean security and accountability to both partners. There is a need for Russia's ratification of the Energy Charter Treaty and the completion of the negotiations on the Transit Protocol. The Green Paper proposes the establishment of a new Community mechanism enabling Member States to take rapid and coordinated action in external energy supply situations or in the case of unexpected supply disruptions. For the diversification of sources and purchase routes, closer cooperation is urged with energy exporter countries outside the Union (Russia, OPEC countries). Proposals of the Green Paper also include the construction of new pipelines and liquefied gas terminals serving the improvement of security of supply.

The Green Paper identified the key areas that could serve as the backbone for future energy policy. Yet, the proposals did not fully meet the expectations of Member States regarding the common energy policy. The proposal of the Commission fell short of the expectations of Central and Eastern European countries, most dependent on energy imports, especially in laying down the basis for an EU-level supply solidarity. The majority of Member States did not endorse the confirmation of the mechanisms related to stocks and reserves. The European Energy Security Treaty, proposed by Poland, and a plan for the coordination of gas storage, strongly supported by new Member States, were also rejected.

The Green Paper was confirmed at the European Council (EC) of March 27, 2006.

OLD NEW ENERGY POLICY?

At the European Council, Member States agreed that there was a need to work out a common European energy strategy and thus there was agreement in principle on institutionalizing the Common Energy Policy. The most important requirement regarding the new European energy policy is that it should have a well balanced approach in meeting the security of supply, competitiveness and environmental sustainability objectives. The main prerequisite for this is that the Union should increase activities improving security of supply.

A new aspect in the consideration of the community energy policy is that the problem of supply security is in the heart of the issue. Member States first of all agreed on the external aspects of security of supply. They emphasized the need to enhance energy-related foreign policy, deepen the existing energy partnerships, diversify energy sources and supply routes and take joint operative measures, based on solidarity, for the management of situations

of crisis, while also respecting the principle of subsidiarity. The question of the internal security of supply is clearly independent from the issue of external security of supply. While external relations create the need for better coordinated action at the EU level, Member States, with reference to internal security of supply, underlined that meeting their national demand was the primary responsibility of Member States.

The formation of the energy policy and the choice of the energy mix will continue to be issues dealt with at the national level. Considerations on the use of nuclear energy are also within national authority. The Commission will take initiatives related to the energy policy observing the principle of better regulation, i.e. its authority will not change or grow as compared to earlier: no authority will be withdrawn from Member States.

In addition to making security of supply the highest priority issue, the summit insisted on bringing the two other objectives, i.e. competitiveness and sustainability closer to the heart of the policy, too. Prerequisites for the unfolding of competitiveness are the development and completion of the internal market, which latter require the full, efficient and transparent implementation of the European Council directives 2003/53/EC and 2003/54/EC, in force, on the common regulations for the establishment of the internal market. The full liberalisation of the internal electricity and gas markets by mid-2007 has remained a key objective. An important element in establishing the internal market is the development and facilitation of regional markets. The proposal of the Green Paper on setting up a European Energy Regulator authority was not supported by all Member States. There was no unanimous support for prospective institutional developments like the establishment of a European Network Center and an Energy Supply Observatory, either. Instead, Member States opined that, using the institutions available, it was easier to improve cooperation to achieve higher efficiency. There was no intention to create a European super bureaucracy; instead, the role of national energy regulation authorities should be made stronger and their cooperation should be fostered.

As regards the aspect of environmental sustainability, the EC once again confirmed existing policies and basic principles related to the community energy policy. On the basis of the measures already implemented by Member States, the Action Plan on Energy Efficiency estimates 20 per cent energy saving capacity in the EU by 2020. Considering meeting the targets for 2010, the European Commission plans to raise the share of renewable energies within all energy consumption by 15 per cent until 2015, and the percentage of biofuel is to be raised to 8 per cent of petrol and diesel fuel. (The earlier target for 2010 was 5.75% per cent.) The implementation of an action plan on biomass passed in December last year serves loosening energy import dependence. It was also confirmed that, for the improvement of energy efficiency, the reduction of emission and the development of sustainable technologies, sufficient financial sources were to be allocated for energy-related R&D.

Beyond the earlier endorsed general principles serving the facilitation of energy political targets, the EC also identified more particular, foreseeable and indicative measures, which were not novel, either, as they had earlier been passed by the Member States. These primarily included the implementation of plans and policies related to energy efficiency (working out an action plan on energy efficiency by mid-2006) and of the action plan on biomass aimed at the reduction of harmful substance emission and the diversification of energy sources. Infrastructural projects necessary for the establishment of the internal energy market of the Union and of regional markets, as well as for the diversification of sup-

ply, must be accelerated. So as to facilitate the energy political targets of the Union, a more efficient energy dialog is required with Russia. The summit identified the ratification of the Energy Charter and the Transit Protocol by Russia, during the Russian chairmanship of G8 countries, as one of the targets.

Considering the above, can we speak of the formation of a new energy policy and what stage has the common thinking of Member States on a better coordinated energy policy come to?

Both the creation of the Green Paper and the Conclusions endorsed at the European summit in March may be considered as significant turns in the history of the common energy policy, yet, there were no uniform commitments made for a new community energy policy. A genuinely new European energy policy would require changing the legal basis of the cooperation and, in the mid- and long run, it would also presuppose divided authority between Member States and the Commission. By keeping the current status quo, only a more integrated cooperation in the field of energy can be spoken of, which is certainly not little. Even if the legal basis is left unchanged, however, there is a need for a better integration of the energy-related sectoral policies. Yet there should not be very high expectations of the efficiency of such integration because the energy policy meeting the aspects of competitiveness and environmental protection, launched 10 years ago, and the implementation of the targeted integration of these branches have borne little fruit since then.

The document regarded as the basis of a new energy policy, the Green Paper, and the Conclusions endorsed at the summit do not contain more, either, than a few, earlier agreed upon general principles on security of supply and competitiveness. Only small steps have been made towards the formation of a Common European Energy Policy. There are novelties only in two respects.

The most important novelty is that Member States have made a commitment for the formation of an authentic, energy-related, single foreign policy, referred to as the external policy for energy. Member States thus decided that a single EU policy was required, only considering the relations of energy affairs with foreign relations[15]. (In other words, Member States, analyzing the cooperation of the past forty years, did not regard it as necessary to make conclusions from the experience and lay down the basis for a genuinely new energy policy beyond the generally formulated basic principles.)

The other novelty is that once a year a high-level discussion is to be held on the energy strategy of Europe. To facilitate this, the Commission will make a strategic analysis on the energy situation by the end of 2006 for the first time, and every year later on, which will determine the mid- and long-term energy political objectives of the Community and identify the areas where action must be taken. It is in this process that the problems of European interest that require measures to be taken can be identified.

It was not determined in practice which areas were the cornerstones of the Community energy political policy. Its basis, the Green Paper, discusses almost all questions without identifying the priority areas of the Union's energy policy. Although improving the security of supply is the top priority of the European energy policy, neither the Green Paper, nor the Conclusions passed at the EC session focus really on improving energy efficiency, which is the most important means of increasing energy efficiency. Not to mention that the Union, in shortage of heating fuel, is able to influence energy consumption from the side of demand only[16].

Apart from the above two issues, no uniform commitments were made. The action plan on energy efficiency, for instance, does not include an actual commitment with regard to the 20 per

cent energy saving, failing to identify indicative targets for Member States. The same holds for renewable energy sources, regarding which no commitments were made, either. The new policy is not ambitious enough with respect to global warming. Furthermore, it fails to take a stance on the use of nuclear energy, even though it is well-known that the use of nuclear energy would be a solution for the secure energy supply of Europe[17] and could also significantly contribute to the reduction of harmful substance emission[18].

Although the strategic document addresses many issues, it fails to offer actual roadmaps. The most significant deficiency probably is that the Green Paper focuses little attention on potential long-term problems. It is not clear, either, how competition rules will be applied at the energy market in an environment where only target numbers will be identified, the application of best practices will be set as examples, or action plans will be made for renewable energy use and energy efficiency. What if the targets set cannot be met in a cost efficient way? The document does not say what means the Community will apply in order to solve the conflict.

One thing that is certain is that a more integrated energy policy can unfold in two directions. One is the external policy for energy, the formation of which is determined by significant energy producing and consuming, as well as transporting countries gradually becoming important players of the internal gas and energy market of the Community. The other direction of the policy in formation is related to the creation of a more open market, making greater competition possible.

Foreign policy

The Commission and High Representative of foreign- and security policy of the Union prepared a common paper on an external policy to serve Europe's energy policy, identifying the basic principles determining the security of the external energy supply of the Union[19] and formulating practical targets as well. It focuses primarily on the two critical pillars of the security of supply, namely the good functioning of markets and the diversification of energy sources and supply routes.

The most important condition for secure energy supply is the existence of well functioning markets, which require physical, as well as legal infrastructure. To this, the Union is able to contribute by expending its own energy market, forming a common regulatory space with neighboring countries, where uniform commercial, transit and environmental rules are applicable. In the focus of the EU external policy for energy is a strategic partnership to be formed with key energy producing and consuming countries. Regarding bilateral relations, the EU-Russian dialog is of special significance. Considering this, the Strategy urges Turkey's and the Ukraine's joining the Energy Community. Since well functioning markets demand further liberalization, in this, the Union must strive for reciprocity and the application of market rules (competition, transparency and non- discrimination). The Strategy makes it clear that the growing number of bilateral agreements signed by major consumer countries increases the supply risks of the energy system. The Union therefore encourages its partners, especially major consumer countries, to ensure their supply by multilateral agreements. A genuinely functioning energy market requires the implementation of the Energy Charter Treaty, which means that key signatory countries – including Russia and the United States – should ratify it.

Both a well operating market and diversification make the modernization and development of energy infrastructure necessary. The Strategy draws attention to the fact that infrastructural development is necessary not only in

energy producing but also in transit countries. Within the framework of the energy partnerships formed with energy producing countries of key significance, the EU must support the modernization of energy production. From the point of view of diversification increasing the security of supply, new gas pipeline projects affecting North-Africa, the Middle East and the Caspian region, are of high significance. From the Hungarian viewpoint, it is important that the document include the construction of new LNG-terminals for the transportation of Caspian oil to the Union. The plan of new pipelines assigns a central role to Turkey, where the gas pipeline from the Caucasian and Caspian regions to the Union would transit, skirting both Russia and Iran.

The external political strategy encourages the streamlining of multilateral relations into the energy policy of the Union, with special regard to the forums of G8 as well as of G8+5 countries, the latter bringing together producer and consumer countries. So as to increase security of supply, a more powerful coordination is necessary with IEA. It is set out in the Strategy that the energy political issues of the Union form an integral part of the system of multilateral trade in future, to which WTO rules are also applicable. The Strategy underlines that the Union should have suitable means for the early warning and management of energy supply risks. There are plans in place to establish a Network of Energy Correspondents and an Energy Supply Observatory, the latter being strongly supported by Hungary.

Internal Energy Market

A basic obstacle to opening markets is that national markets are ruled by energy producing companies in monopoly. Member States, on the other hand, are convinced that the security of energy – as part of national security – is too important to rely on the market. This conviction was one of the reasons why European governments "produced" their national champions. They are convinced that it is the existence of these quasi monopolies that guarantees secure energy supply[20]. The success of the liberalization ensuring the competitiveness of the EU energy market will also depend on the ability to persuade Member States to loosen the protection of their national energy companies.

In EU legislation it is highly probable that, depending on the inquiry of the Competition Directorate, the Commission will make a new legislative proposal (referred to as the Third Energy Market Liberalization Package), the aim of which would be to force out the separation of activities and ensure the independence of national regulatory authorities.

THE COMMISSION'S NEW PROPOSAL PACKAGE[21]

Almost one year after the publication of the Green Paper, the Commission – analyzing the conclusions of the social debate, the sectoral inquiry and the strategic review to be soon completed – tabled an integrated proposal package. Unlike earlier documents, the Package seems to offer an outline of the cornerstones on the basis of which the Union wishes to reduce its import dependence with the proclaimed intention to lead a new industrial revolution. The comprehensive set of measures presented on January 10, 2007, serves to limit climatic change, increase energy security in the Union and improve the competitiveness of the Community but determines the EU energy policy in relation with climatic change basically. The Union maintains that the greatest challenge that humanity faces is the fight against the consequences of climatic change. The average temperature rising by 5 degrees C and endangering the health of humans, the increas-

ingly frequent droughts and floods, the rising sea level and the decreasing productivity of land in southeast Europe all have cost-increasing economic consequences. The main pillar of the new energy policy is therefore the European commitment that the EU must reduce greenhouse gas emissions, caused by energy consumption, by 20 per cent by 2020. The package proposes unilateral reduction, irrespective of the fact whether or not major countries of emission, including the United States of America, follow the example. According to the target of the Package, CO_2 emission in the Union will be reduced by 60–80 per cent by 2050.

Beyond concrete visions and ideas on the future energy policy, another characteristic of the new Package is that it basically takes stock of the internal opportunities and sources of the Community. In the new Energy Package, there is great emphasis on accelerating the switch to the use of low carbon energy technologies, which also means an increase in the financial sources spent on the research on low carbon technologies. In 2006–2013, the Union will increase annual expenditure on energy research by at least 50 per cent. Within the framework of the change for low carbon energy technologies, the proposal identifies obligatory target numbers with respect to greenhouse gas emissions and renewable energy sources, which latter will have a share of 20 per cent in the energy mix of the EU by 2020. In addition to renewable energy sources, the use of biofuel is also to increase and must represent at least 10 per cent of vehicle fuels by 2020. At the heart of the Commission's proposal is the improvement of energy efficiency, within the framework of which the entire primary energy use is to be reduced by 20 per cent by 2020. The proposal urges the speedy introduction of low consumption vehicles of transport, as well as the improvement of energy efficiency in buildings in the Union. As regards the use of nuclear energy, the Commission leaves the decision to Member States. Member States should also decide in what ways, considering their national potentials, they are able to best attain the general targets on renewable energies. The Commission dropped their earlier proposal according to which the production of electrical energy from renewable energy sources should have been increased to 21 per cent by 2010. At the same time, Brussels asks Member States for National Action Plans in which the particular targets and target numbers of all renewable energy sectors are to be determined. The third high priority area of the Package is a proposal on the establishment on an internal energy market, based on an earlier inquiry. It is an indictment against major energy companies and governments who are responsible for the failure of liberalization[22]. An inquiry of the Competition Directorate of last November into the energy industry revealed serious problems related to competition in the gas and electricity sectors. It was highlighted that, even though June 1, 2007, was the target date of full market liberalization, both European consumers and the economy were unable to fully benefit from the advantages of opening up European energy markets like lower prices and higher level services. This is the case because a European energy market has failed to be developed; what is more, no mention can be made of the establishment of regional markets, either. The reason is the anti-competition network distribution practices of integrated "energy giants", which divert infrastructure investments. As a consequence, connecting capacities are missing, which limits cross-border transactions. Most national markets are still controlled by the major national energy companies, which have no interest in the entrance of new players into the market. In the January package, the Commission therefore proposed that, for the establishment of a genuinely functioning internal energy market, further measures – ensuring

the unbundling of production and distribution – are necessary. Under the original directive on the liberalization of the electricity and gas markets (2003/54; 2003/55), transmission networks must be legally separated from energy production and sales. In their January proposal, the Commission went even further, saying that only full ownership unbundling ensured fair market access[23]. This means that vertically integrated energy giants, which are also the owners of energy networks, must be divided up and separated into their units. This is the condition enabling new market players to have free access to networks on equal conditions so that competition ensuring a fall in prices may unfold.

For the operation of the internal energy market the Package underlines that the interconnection of the energy infrastructure in the Union should be improved to reach at least 10 per cent.

The three pillars of energy policy are supported by an authentic external policy for energy, through which the EU wishes to diversify and widen importing opportunities so as to improve the security and sustainability of energy supply. The top priority is initiating negotiations and urging a speedy agreement with Russia on the new Strategic Partnership. Strengthening EU relations with Central Asia, the Caspian and the Black Sea regions serves the diversification of energy sources and supply routes. Within the framework of the external policy for energy, bilateral dialogs with the United States, China, India and Brazil are aimed at the reduction of greenhouse gas emission and the increase of the use of renewable energy sources. A further target is the potential extension of the Agreement with Southeast Europe to Norway, Turkey, the Ukraine and Moldova. Strengthening energy relations with Algeria, Egypt and other energy producing countries of the Maghreb–Mashrek regions has also remained an objective. There is also a high priority new initiative, which is the establishment of a comprehensive African-European partnership, which, along with the partnership formed with Russia, may be considered one of the top priorities for the Union.

Debates, decision

The new proposals on energy and climatic change were discussed by various EU organs, after which the EC confirmed the integrated energy and climatic change policy of the Union in March 2006.

In the debates following the publication of the package, the stances of Member States varied mainly on the objectives of the Commission on energy efficiency and the use of renewable energy sources and its proposal regarding liberalization.

As regards long-term target numbers, the question arose whether they should be binding or, similar to the current regulations on renewable energy sources, only of an indicative nature. Another question is what the target should be. Against the 10 per cent proposed by the Commission, which is also endorsed by the majority of Member States, the Presidency suggests that the share of biofuels in transport-related fuel consumption should be determined at 12.5 per cent by 2020. At the Energy Council meeting on February 15, 2007, and that of the EC on March 9, 2007, departmental ministers and heads of government and state endorsed the obligatory increase of the share of biofuel in overall transport-related petrol and diesel consumption to 10 per cent by 2020. At the same time, they rejected setting binding target numbers for the use of renewable energy sources at the Community level. With respect to the use of renewable energy sources, the agreement was made that their share within the overall energy consumption of the Union should be increased to 20 per cent by 2020. On

the basis of this generally formulated target, it would be up to Member States to set their "differentiated national targets" considering their national potentials and opportunities. Target numbers were to be set with reference to the specific branches of renewable energy sources (cooling, heating and the production of electricity from renewables). The EC gave a mandate to the Commission to submit, later this year, a new and comprehensive draft directive on renewable energy sources, also including regulations on the general national targets of Member States, as well as rules on the sectoral targets of national action plans. A major deficiency of the package is that it lacks a European stance on nuclear energy, on which no position was formulated at the level of Heads of Government and State, either. Even though French president *Mr. Chirac* argued forcefully in favor of nuclear energy which, he said, should be officially acknowledged by the EU as a clean energy source alongside with wind- and other green energy, Member States remained divided on the issue.

It was the proposal on the establishment of the internal energy market that aroused the biggest dispute. Countries opposing the Commission's proposal, namely Germany and France[24] argued that, instead of the predicted fall in prices, liberalization had raised energy prices in 2004–2006 and that energy giants were not to be blamed for the imperfect functioning of the market. On the contrary: thanks to their stronger position, it was them who guaranteed security of supply during price negotiations with Russia, it was maintained. Facing the resistance[25] of the two major founding countries, the Commission offered another alternative to ownership unbundling as a solution of the situation: setting up an Independent System Operator to operate and supervise the networks owned by energy giants.

In the issue of the liberalization of the energy market, energy ministers practically sided with Germany and France, i.e. more radical liberation measures can only take place after the existing legislation has been fully translated by all Member States not only literally but also in spirit. The Energy Council invited the Commission to foster the unbundling of energy production and trade, as well as network activities. The Commission should furthermore ensure that new market players could have free access to the suppliers' infrastructure on equal conditions. In relation with the issue, the EC did not confirm the original proposal of the Commission, either, that was to oblige energy giants to unbundle production activities and the distributional network. Instead, it was pointed out in the Council Conclusions[26], using a firm tone regarding the issue, that there was a need to efficiently separate producer and commercial, as well as network operational activities, to strengthen the independence of national energy regulating authorities and harmonize their activities. The EC gave a mandate to the Commission to present a legislative proposal later this year (in summer-autumn) for the efficient separation of activities as an alternative to full ownership unbundling. The Commission expects the proposal to loosen the monopoly of national energy industrial companies having a dominant position at national energy markets.

At the EC, Heads of State and Government confirmed that, by 2020, greenhouse gas emissions would be reduced by 20 per cent compared with 1990 levels, which was an independent commitment by the Union. The Union would raise its commitment to 30 per cent if industrially developed major emission countries, including the United States, made a similar commitment, or if dynamically developing countries also committed themselves to contributing to the reduction to the necessary extent. A comprehensive energy Action Plan for the period of 2007–2009, on measures for the operation of the internal market, the

strengthening of the security of supply and the increase of energy efficiency, with deadlines included, was also adopted.

COMMUNITY ENERGY POLICY AFTER THE PACKAGE

The adoption of the Green Paper was borne by the realization that the problems that Europe was facing, i.e. the security of supply, the fight against climatic change and the network investments necessary for the establishment of an internal market demanded an energy policy at the Community level. While the January Package was another step in the formation of the Community Energy Policy, it gave imperfect answers in relation with the tasks outlined in the Green Paper, although it did offer more detailed and more particular suggestions regarding some energy political objectives.

The Package is based on the recognition that climatic change and energy policy require an integrated approach, since energy production and consumption are the major sources of greenhouse gas emission. Yet, this authoritative document fails to outline an integrated, long-term Community energy strategy, which Europe is very much in need of. It was no wonder that, after the publication of the Package, it was remarked that the Union had actually given up on working out a community energy policy and focused on the combat against climatic change and the reduction of greenhouse gas emission instead. The proposal does not contradict earlier suggestions and matches the triple energy political goals identified in the Green Paper. It does not, however, have a balanced approach towards sustainable, competitive and secure energy supply, giving high priority to sustainable energy supply. It is no doubt that, in the increase of efficiency and the application of renewable energy sources, the Union has significant achievements, further reserves and comparative advantages. It is also indisputable that sustainable energy production significantly increases the security of supply, yet, however successfully target numbers are met, this fails to counterbalance or solve Europe's imported energy dependence. Europe must make a decision on its energy future. It must prepare for a new phase in energy dependence characterized by greater harmony between the reform of the internal market and the external challenges to the Union. All this underlines the necessity for working out a coherent security of supply strategy. The same is supported by a new proposal of the Commission for the liberalization of the internal market, based on the assumption that liberalization in itself would guarantee the security of energy supply in Europe. The implementation of liberalization does certainly have significant energy security advantages, simply because the single European energy market is more protected from the consequences of supply disruptions. (In the case of supply disruptions, supplementary sources are easier to distribute in this bigger market than within a national economic framework.) Since the liberalized energy market exists mostly on paper and in regulations so far, its establishment may take longer time and require the creation of additional physical infrastructure and information system.

Even the establishment of a liberalized market will be no solution to the problems of energy import dependence on Russia and the consequences of climatic change, however. Another problem is that the negotiating position of companies deteriorates by ownership unbundling. The Commission proposal will thus have a result contrary to its intentions: forcing out competition in the short run by all means is inconsistent with guaranteeing long-term security of supply[27].

The January Package not only fails to outline a coherent security of supply strategy but it lacks the outline of an integrated energy policy, too, with all sides of the policy coordinated.

The problem of the security of supply in itself would, however, make such a policy necessary. Further arguments for such a policy are: the issue of establishing European-level networks, tasks related to the interconnection of national systems and the combat against climatic change. Although, regarding the latter, the Package did provide target numbers for its proposals (reducing harmful substance emission by 20 per cent and, in the case of developed industrialized countries, by 30 per cent), the question arises whether such commitments make sense, since the problems of climatic change are of a global nature and do not stop at the borders of Europe. Another question is if the further forceful unilateral reduction of CO_2 emission by the Union makes sense under conditions when major polluting countries (developed industrial and dynamically developing Asian countries) do not reduce their emission at a similar rate. In this case, the competitiveness of the European industry in the global competition is likely to fall without producing actual advantages for the environment.

THE ROLE OF RUSSIA IN ESTABLISHING SECURITY OF SUPPLY FOR THE UNION

The gas supply of the Union is basically ensured by Russia and North Africa, while there are additional supplies from the Middle East via Turkey, as well as liquefied gas coming from Nigeria. However, the import share of these latter is estimated not to rise above 10 per cent by 2030, while the share of Russia and CIS is to increase from the 28 per cent in the year 2000 to 54 per cent.

The EU and Russia are two great European powers with global ambitions, which are becoming increasingly closer neighbors with a growing number of issues of mutual interest and worries. All this presupposes a regulated system of relations. The EU would like to have a friendly and predictable Russia both in politics and in fields of concrete cooperation like the energy industry. Russia, on the other hand, would like to increase its presence in Europe without adopting the prolific legislation of the Union. When choosing the framework of cooperation, Russia decided against the path followed by CIS states and did not form its relations within the framework of what is referred to as the "European neighborhood policy". Russia decided for partnership, wanting to be an equal partner in the cooperation. Russia did not form its relations with the developed part of Europe with the perspective of joining the Union and did not set out to adopt Community legislation. Their relations and cooperation are determined by the opposition of the energy superpower Russia and the de facto world power Europe lacking any geopolitical means. Russia intentionally uses its energy relations also as a tool for political supremacy, while the Union lacks actual diplomatic or military power. Realizing the latter, the Union forms common regulatory spaces with third countries (Partnership and Cooperation Agreements), in which the legislation of the Union and the third country in question are gradually shifted closer. For the time being, it is in this policy where the Union has found the opportunity of regulating and influencing the conditions which finally determine gas supply to the Union[28].

Russia and the EU are significant partners in energetic cooperation. During the decades, interdependence has developed between them, which is to further increase in future. Russia is highly dependent on the European markets and the dependence of the Union on Russian gas supplies is also significant. Russian pipelines have been constructed in the direction of the Member States of the Union and the EU is one of the best profiting markets for Russian gas. More than 60 per cent of Russian export revenues come from energy trade. Raw materials sold to the Union contribute to the foreign

exchange revenues of the Russian budget by 40 per cent. One fourth of the gas and oil demand of the Union (EU-25) comes from Russia, which share is to grow in the next 20–30 years. According to estimations, 70 per cent of the energy demand of the Union will be covered from imports by 2030. Russia wants to remain Europe's key energy supplier also in the first third of the 21st century, for which the conditions are given considering its huge stocks. The shortage of national capital necessary for exploitation is a problem, however. As exploitation goes further east, transportation to the Union gets increasingly expensive. The need to cover growing import demand urges Russia to allow foreign investors to have a greater share in production and development. Dependence involves risks on both sides. For the Union, import dependence is a problem primarily because markets are not permeable. On the other hand, the security of the European market is important for Russia, too, since here it is able to sell gas with higher profits compared to other markets[29].

The EU wishes to reduce the risks of energy supply by what are referred to as Partnership and Cooperation Agreements signed with the governments of energy producing and transporting countries. Among these, the agreement with Russia[30] is of special significance and aims at the establishment of a stable investment environment and closer cooperation between energy companies. Through the cooperation, the EU also contributes to the liberalization and increasing transparency of the Russian economic management. Russia, however, is still reluctant to shift its legislation towards that of the Union.

A new stage of the EU–Russia dialog was the Paris summit in October 2000, where the two sides signed an Energy Partnership Agreement. Surpassing their former cooperation, which had basically been restricted to producer-consumer relations, they acknowledged the interdependence and complementarity of their energy sectors. The two sides manifested their common intention to foster the stability of the energy market on the European continent. Russia showed readiness to work for the long-term security of energy supply for the Union, while the Union agreed to provide technical assistance for the production and transportation investments in the energy sector. The cooperation focuses on four areas, which are investment, trade, infrastructure and energy efficiency. Within the framework of the joint energy efficiency initiative, partners strive to ensure that all phases of exploitation and end use are energy-saving[31]. The dialog also extends to the planned ratification of the Energy Charter by Russia.

Unlike the system of world trade based on WTO rules, in energy trade there are no common rules worked out and agreed upon by producer and consumer countries. Under such conditions, relations with energy producing countries like Russia, are based on contractual agreements, which create a stable framework for trade and investments. The Russian-Ukrainian dispute on gas prices in January 2006 and the "business" dispute with Belarus on transit duties related to oil transportation[32] a year later, even though they were disputes between the former Soviet Union and former member states thereof, highlighted the political risks of energy dependence, frightening EU governments, too. The disputes drew attention to at least two factors endangering security of supply. One is the lack of regulations governing the energy relations of energy producer, supplier and consumer countries and the other is the need for infrastructural investment in Russia.

ENERGY CHARTER

Formally, both Russia and the EU committed themselves to applying the Energy Charter Treaty[33] in the energy sector. In practice, how-

ever, there has been no political agreement on the extent of the commitments regarding the implementation of the Treaty. The Treaty was signed by 51 countries plus the European Community. So far, it has been ratified by 46 countries, including the Member States of the EU. Russia has signed but, until today, has not ratified the Treaty, the only legally binding multilateral agreement regulating energy trade, investment and transit, and applies it on a temporary basis at the moment.

The two agreements, i.e. ECT and the protocol on energy transit known as the Transit Protocol together create the multilateral regulatory framework for energy transit via Eurasia.

The Transit Protocol sets out legally binding regulations on cross-border investments. Under the regulations, the states must guarantee the free transit of energy supply through their territory; may not impose unjustified delays or transit restrictions and must apply non-discriminatory pricing. Energy transit charges are to be set on an objective basis; they must be justifiable and non-discriminatory.

The debate between Russia and the Union has been going on for several years; negotiations at the expert level are under way. There are two particular problems in which the harmonization of stances is in progress. One is Article 8, which would oblige Gazprom to make its pipelines accessible for third parties such as the Ukraine, Turkmenistan and the EU[34]. The other, Article 20, is what is referred to as the Clause on regional integration, which sets obligations for the Union. Under this, the Community must make its internal energy distribution network accessible for suppliers from third countries, under the same conditions as those given to EU suppliers.

The negotiations on the Transit Protocol are still under way at the moment. Since the end of 2005, there have been discussions on a new proposal under which the most important rights enacted in the Transit Protocol would be extended to pipelines within the Union through the application of a benchmark mechanism. Although the advance of the negotiations made EU authorities optimistic, contrary to their expectations, the Charter Treaty was not ratified at the EU-Russian Energy Conference in October 2006. It may take several years more for the Russian government to give its approval for ratification[35] because it wishes to grant itself the widest possible room for action at the market of carbon hydrogenes, in order to facilitate its modernization goals and supremacy efforts. For the time being, it is not ready to give up its sovereignty in the field of energy, which is the basis for its supremacy policy. It has no direct interest in shifting its regulations towards EU law; it is not in Russia's interest, either, to become part of the common European political and economic region. Russia's rejection of the EU legislation on the energy market and the EU's urging Russia's shift by all means make it more difficult for both sides to approach interests and look for a compromise. WTO membership will be of help in solving the problem.

In winter 2005–2006, there were disruptions in the gas supply of several Member States of the Union because some of the gas due to arrive from Russia under the treaty was missing. A similar situation developed also in the case of Russian industrial suppliers[36]. The weather in January 2006 drew attention to a factor endangering the security of supply to the EU, the vulnerability of the Russian energy system and the limits of capacities, which, in the case of bad weather, would have caused supply problems even without political disputes. For the lack of necessary investments, Russia is unable to meet either national or EU demands[37].

The pipelines, the infrastructure are outdated, unsafe and in need of development. The investments of the 1990's resulting in above 9% growth were basically directed at the gas and oil

exploitation industries, while infrastructural investments failed to take place. In the 1980's-1990's, even the investments necessary for keeping up production were unimplemented. Several high pressure pipelines are over 30 years old and, due to the extraordinary operational (climatic and geographical) conditions, are in a bad state. The renovation of pipelines would cost billions of euros. In the year 2004, 70 bn of the 171 bn cubic meters of gas that Russia was due to deliver filtered off in the air and Russia had to pump it back so as to meet its treaty obligations. According to estimations, investments worth some USD 90 bn will be required in the next 25 years to keep up the current level of gas production in Russia, which the country will be able to finance only by involving foreign, first of all European investors.

The effort to strengthen the security of supply of the EU launched a series of conflicting approach attempts between the Union and Russia. In the process, the Union, urging direct access to pipelines in Russia, called for the ratification of the Energy Charter Treaty by Russia and, in relation with the Community Energy Policy in formation, it underlined the diversification of energy sources and routes, which was a source of misunderstanding for Russia. Even though the proposal was motivated not by the wish to maximize self supply and minimize dependence but by the wish to reduce the risks related to dependence. The Union's emphasizing the establishment of a genuinely functioning internal gas and electricity market in the Union also bore uncertainty for representatives of Russian business circles and political decision makers since, due to the imperfect functioning of the market, it cannot be established today what rules will be applied at this market and in what ways they will affect Russia. The energy market of the Union is, contrary to the officially declared policy of the EU urging liberalization, still a closed market today, where new entrants face difficulties. The liberalized market of the Union will have to be actually functioning so as to become an attractive example for external suppliers.

While the Union, in the course of events, reminded key energy exporter countries, including Russia, to apply the international agreements and rules in the energy sector, its Member States made efforts to protect their national energy giants referred to as "national champions" from cross-border acquisitions, trying to avoid competition. When informed of the acquisition of shares in Centrica[38] by Gazprom, Great Britain held out the prospect of reconsidering the Acquisition Act of 2003, which made government intervention possible only when national security interests were endangered. The confrontation, i.e. the contradictory management of the security of supply continued when Gazprom warned the Union against restricting the expansive transactions of the state gas company in Europe if it needed Russian gas supplies also in the future. The visit of President *Putin* to China later on gave rise to fears in Europe that Russian supplies might give priority to Asia over Europe.

So as to make the situation clear, the *Barroso-Piebalgs-Bertenstein* letter was issued, declaring the common stance of the Union (the Commission, the Energy Commissioner and the Austrian presidency), which, as a part of the wished for community energy policy, could be regarded as the first instance of single foreign political action. The letter practically discusses almost all issues that have been sources of dispute for the two sides.

The letter acknowledges long-term contracts as justified since they facilitate investments made to satisfy future demands. Under EU competition rules, contracts that foster new investments or have other advantages are given preferential treatment.

It is pointed out in the letter that the diversification of sources and routes underlined by the EU Energy Commissioner does not mean

that the Union wants to restrict supplies of Gazprom to the European market. By the growing demand for energy, the two sides stay in the state of mutually advantageous interdependence and the transparency expected from both sides must contribute to the further deepening of mutual interdependence and trust.

The letter assures that there will be no discrimination against the giant Gazprom, which fears that the EU wants to impose restrictions on its efforts to become a global energy company[39]. Its monopoly will be considered, however. The rules that apply for Gazprom are the same as those applicable for European competitors. It is pointed out in the letter, at the same time, that EU competition rules give preference to contracts that offer new investments or other permanent advantages. The letter emphasizes that Russia has always been a reliable partner and will remain an important partner for the Union in the future as well.

It is furthermore underlined in the letter that the EU assigns great significance to the ratification of the Energy Charter and the Transit Protocol because it is these mechanisms that lay down the basis for the long-term operation of the broadly interpreted European market, including the rights of transit countries and the access to pipelines by third parties. Moscow has not yet agreed to take the commitments involved in the ratification upon itself because that would put an end to the monopoly of Gazprom.

In addition to acknowledging long-term contracts as justified, the letter underlines the importance of transparency, which must ultimately lead to ending the monopoly of Gazprom.

At the various energy forums, a growing need for establishing a truly functioning strategic partnership between the Union and Russia was defined. The main reason for this was not the fact that the Russian Strategic Partnership Agreement signed in 1997 was to expire in 2007[40], but the fact that since the conclusion of the agreement there had been significant changes both in the development of the post-Soviet era and in the Union through the admission of new Member States. Beyond these, the agreement currently in force could not become a solid basis for cooperation between the two sides, which is also proven by the fact that, not long after the conclusion of the agreement, the two sides felt the need for strengthening and extending the EU-Russian bilateral cooperation[41]. In relation with the energy policy of the Union, the question of energetic cooperation has been on the agenda since January 2006. From the point of view of the energy future of the Union, it is especially important that long-term cooperation should have a solid contractual basis. The revision of the agreement in force and the preparation of the contractual basis for the post-2007 cooperation have speeded up. In the latter, the Union wishes to achieve that the comprehensive agreement should have an ambitious energy chapter that is in accordance with the main principles of the Energy Charter Treaty. Negotiations are at a deadlock at the moment. The Commission makes efforts for the solution of the Russian-Polish dispute caused by the Russian import ban on Polish meat and vegetable products, which blocks the resumption of negotiations.

There are signs that, after Russian's accession to WTO, trade relations with the Union will widen and economic integration will deepen. After the preparation and the first discussion (EC) on the external policy for energy, the Commission was invited to work out the potential elements of future partnership. The energy issue is likely to be a priority and in the new agreement, the Union wishes to include the basic principles of the Energy Charter Treaty ensuring reciprocity, transparency and non-discrimination.

Considering the critical remarks voiced especially frequently since January 2006, the

new cooperation must become a widened strategic partnership made richer both in content and commitments, in which mutually advantageous interdependence and reciprocity (with regard to the access to markets, infrastructure and investments) are reflected. Cooperation profitable to both sides must be formed.

There is a need for a genuine energy dialog between the EU and Russia. A basic condition for an efficient energy dialog with the EU is that Russia should form its strategy for the sector. It has to establish the necessary legal background, pass the new act on the exploitation of the deep underground, another act on foreign investors in strategic sectors and an act on product division. It needs to have a detailed strategy on the development of the Russian gas industry. First of all, however, it has to solve the structural transformation of natural monopolies. The Russian side believes that Kazakhstan, Turkmenistan and Azerbaijan should also be involved in the dialog.

The renewed strategic partnership between the EU and Russia must be based on long-term strategic relations characterized by mutual advantages, reciprocity and complementarity.

What interests can form the basis of a partnership agreement based on energetic cooperation?

Through the partnership, the EU wishes to increase its security of supply, because of which it wishes to guarantee direct access for European investors to Russian energy sources and markets. As regards the interests of the other side, Russia also wants to acquire a share in the European energy distribution systems and asks for the same conditions for Russian companies at the EU market that are granted to companies of the Union. So as to meet the growing energy demand of Europe, Russia has to move to increasingly difficult and complicated exploitation conditions, which requires well developed technology, capital and expertise available in the Community. Thus, it is the most critical and important areas of Russian development that may come into question within the framework of reciprocity on this side, too.

Complementarity can be made use of also in the adoption and application of energy saving technologies implemented by foreign companies, especially in the case of heating and the electricity networks. The energy thus saved can be released for European export. The Russian side believes that cooperation should not be narrowed down to stable energy transit, the share of technologies and to financial investments. In the Russian processing industry, there should be a move of energy-intensive industries based on the consideration that energy should be used where it is produced. It is in Russia's interest that raw material-intensive industries using modern, environmentally friendly technologies should be moved to the country[42]. If these industries are moved to Asia, the growing energy demand there will urge Russian energy producing companies to move their energy exports further east, from Europe to Asia.

WHICH WAY TO GO?

By the creation of the Green Paper and the Conclusions endorsed at the European summit in March 2006, there was a turn in the history of the Community Energy Policy. It would be too early to speak of the establishment of a new energy policy, however, since Member States made no uniform commitments for a new community energy policy. They did not regard it as necessary, by analyzing the cooperation of the past forty years, to make conclusions from the experience and lay down the basis for a genuinely new energy policy beyond the generally formulated basic principles. Member States did, however, start common thinking on a more

coordinated energy policy. A genuinely new European energy policy would require changing the legal basis of the cooperation and, in the mid- and long run, it would also presuppose divided authority between Member States and the Commission. Considering the legal basis of cooperation, the current status quo, a more integrated cooperation in the field of energy between Member States can be spoken of.

The document regarded as the basis of a new energy policy, the Green Paper, and the Conclusions endorsed at the summit do not offer more, either, than a few, earlier agreed upon general principles on the security of supply and competitiveness. There are novelties only in two respects.

The most important novelty is that Member States have made a commitment for the formation of an authentic, energy-related, single foreign policy, called external policy for energy. Member States thus decided that a single EU policy was required only considering the relations of energy affairs with foreign relations.

The other novelty is that once a year a high-level discussion is to be held on the energy strategy of Europe. To facilitate this, the Commission will make a strategic analysis on the energy situation by the end of 2006 for the first time, and every year later on, determining the mid- and long-term energy political objectives of the Community and identifying the areas where action must be taken. It is in this process that problems of European interest that require measures to be taken can be identified.

It was not determined in practice which areas should be the cornerstones of the Community energy policy. Its basis, the Green Paper, discusses almost all questions without identifying the priority areas of the Union's energy policy. Although improving the security of supply is the most important priority of the European energy policy, neither the Green Paper, nor the Conclusions passed at the EC focus really on improving energy efficiency, which is the most important means of increasing security of supply. Not to mention that the Union, in shortage of heating fuel, is able to influence energy consumption from the side of demand only.

Beyond the formation of the external policy for energy and the annual strategic revisions, no uniform commitments were made. Neither the Action Plan on Energy efficiency, nor the targets regarding renewable energy sources involve actual commitments for Member States. The new policy is not ambitious enough with respect to global warming. Furthermore, it fails to take a stance on the use of nuclear energy, even though the use of nuclear energy would be a solution for the secure energy supply of Europe and could also significantly contribute to the reduction of harmful substance emission. One more reason why the issue cannot be avoided is that, according to calculations, alternative energy technologies will not be mature enough before 2030 to be realistically taken into account in meeting energy demand. Until then, security of supply could be increased by the use of nuclear energy and the commitments involved in meeting the Kyoto objectives could also be met.

Although the strategic document addresses many issues, it fails to offer actual roadmaps. The most significant deficiency probably is that the Green Paper focuses little attention on potential long-term problems. It is not clear, either, how competition rules will be applied at the energy market in an environment where only target numbers will be identified, the application of best practices will be set as examples, or action plans will be made for renewable energy use and energy efficiency. What if the targets set cannot be met in a cost efficient way? The document does not say what means Community will apply in order to solve the conflict.

One thing that is certain at the moment is that a more integrated energy policy can unfold in two directions. One is the external policy for

energy, the formation of which is determined by significant energy producing and consuming, as well as transporting countries gradually becoming important players of the internal gas and energy market of the Community. The other direction of the policy in formation is related to the creation of a more open market, making greater competition possible.

A foreign policy serving European energy policy lays the emphasis on the two critical elements of external security of supply, i.e. on the good operation of markets and the diversification of energy sources and supply routes. It wishes to facilitate the creation of well operating markets by forming common regulatory spaces with the Union's neighboring countries where the same or similar commercial, transit and environmental regulations are applied as in the European Union.

At the heart of the EU's external policy for energy are the strategic partnerships to be established with key energy producer and consumer countries, of which the EU-Russian dialog is of special significance. The basis for the latter is the well-known fact that Russia and the EU are significant partners in energetic cooperation. The mutual interdependence that has formed during the decades is to grow in the future. At present, one fourth of the gas and oil demand of the Union (EU-25) comes from Russia and the raw materials sold to the Union contribute to the foreign exchange revenues of the Russian budget by 40 per cent. A major obstacle to bilateral relations is that there are no common rules on energy trade developed and endorsed by producer and consumer countries. Russia has signed but, to this day has not ratified the only legally binding multilateral agreement, the Energy Charter Treaty.

The considerations of the new European energy policy and the events of January 2006 drew attention to the need for a new and genuinely operating strategic partnership where the mutually beneficial interdependence and reciprocity (regarding the access to markets, infrastructure and developments) are implemented. Cooperation profitable to both sides is required. The complementary areas serving as the basis for cooperation (access to each other's markets, Russia's demand for developed technologies and financial investments) are available. For the establishment of a new partnership, both sides should get over the uncertainty that has been characterizing EU-Russian relations for a long time, i.e. that they have been unable to set clear, common objectives for long-term cooperation.

Considering the diversification improving the security of supply in the Union, the new gas pipeline projects through which energy supplies to the Union would come from North Africa, the Middle East and the Caspian region, are of special significance. The plan for the new gas pipelines assigns a central role to Turkey, where the pipeline conducting oil from the Caucasus and the Caspian region to Europe would transit, skirting both Russia and Iran.

The strategy makes it clear that the growing number of bilateral agreements signed by major consuming countries increases the supply risks of the energy system. The Union therefore encourages its partners, especially major consumer countries, to secure their energy supply by multilateral agreements. It is set out in the strategy that, in the future, energy political issues of the Union will constitute an integral part of the system of multilateral trade, to which WTO rules are applicable. An actually functioning energy market would presuppose the implementation of the Energy Charter Treaty, which means that key signatory countries, including Russia and the United States, should ratify it.

Since both a well functioning market and diversification presuppose a developed energetic infrastructure, further infrastructural development is necessary not only in energy producer but also in transit countries. Within

the framework of the energy partnerships formed with key energy producer countries, the Union must support the modernization of energy production.

The publication of the Package in January was a further step towards the establishment of a more coordinated energy policy. The comprehensive package of measures presented on January 10, 2007, serves to limit climatic change, increase energy security in the Union and improve the competitiveness of the Community but determines the EU energy policy basically in relation with climatic change. While the Green Paper fell short of expectations by failing to identify the cornerstones of the energy policy, the Package met this requirement to some extent, offering some concrete suggestions.

Another characteristic of the package is that it focuses primarily on areas where the Union has significant reserves, which are increasing efficiency, more intensively using renewable energy sources and establishing an internal market for energy. The package places special focus on the establishment of an actually functioning internal energy market, which requires further measures for the unbundling of production and distribution. It is maintained in the package that only full ownership unbundling assures fair market access. The external policy for energy is added to the above, which is significantly influenced by the diversification of energy sources and supply routes.

Regarding these targets, the Package offers more detailed and particular suggestions. It offers target numbers for the increase of energy efficiency and the wide use of renewable energy sources. It sets the concrete target that, by 2020, greenhouse gas emission from energy use should be reduced by 20 per cent. The target of increasing energy efficiency is concrete as well. The only question that may arise is whether it makes sense to offer target numbers and, if so, to what extent can the objectives set be considered realistic: are they supported by feasibility studies? Are the preconditions available to ensure that the setting of target numbers will actually lead to fostering investments? Through national action plans to be based on the EU targets, Member States do make commitments to meeting the targets.

At the same time, similar to the Green Paper, the Package does not make a stance in the issue of nuclear energy, either. Its main deficiency is probably that it focuses little attention on long-term problems. The Package is based on the recognition that climatic change and energy policy require an integrated approach, since energy production and consumption are the major sources of greenhouse gas emission.

While the integrated strategy on energy and climatic change gives special focus on sustainable energy supply, which increases the security of supply, it does not have a balanced approach towards the issue of sustainable, competitive and secure energy supply. A coherent strategy on the security of energy is missing from the proposals. It is indisputable that increasing efficiency and using renewable energy sources significantly increase the security of supply, yet, however successfully target numbers are met, this fails to counterbalance or solve Europe's imported energy dependence. Europe must make a decision on its energy future. It must prepare for a new phase in energy dependence characterized by greater harmony between the reform of the internal market and the external challenges to the Union. All this underlines the necessity for working out a coherent security of supply strategy. The same is supported by a new proposal of the Commission for the liberalization of the internal market, based on the assumption that liberalization in itself would guarantee the security of energy supply in Europe. The implementation of liberalization does certainly have significant energy security advantages, simply because the single European energy market is

more protected from the consequences of supply disruptions. (In the case of supply disorders, supplementary sources are easier to distribute in this bigger market than within a national economic framework.) Yet, even the establishment of a liberalized market will be no solution to the biggest problem in the Union's security of supply, i.e. the problem of energy import dependence on Russia, or the consequences of climatic change. Not to mention the problem that the negotiating position of companies deteriorates as a consequence of ownership unbundling. The Commission's intention to force out competition will thus conflict with its wish to guarantee long-term security of supply[43].

Beyond determining the energy supply strategy, the outline of a more integrated energy policy with all sides of the policy coordinated is missing. While the measures necessary for the actual functioning of an efficient internal market are mentioned, no common approach, no single voice is used with suppliers from outside the Union, which latter would be a precondition for a better coordinated policy.

For Europe, two pressing problems have still remained. The first is how energy supply can be made more secure despite the region's growing dependence on Russian gas import. In the debate aimed at decreasing dependence, it is underlined that the Union should take collective action in energetic issues. Practice proves, on the other hand, that Member States have given preference to their energy giants over the still non-existent coordinated energy policy. Still in 2006, Member States[44] signed bilateral long-term agreements with Russia, even though the demand for a better coordinated energy policy had been formulated by then. There are at least two factors that account for this[45]. The first one is that the trade of gas between Russia and the Union is based on market principles, long-term contractual agreements and authentic commitments. The latter is indicated by the fact that the agreements in question were signed by the Member States after the Russian-Ukrainian gas dispute, without hesitation. The other one is that the Union should manage the increasing energy dependence of Member States in an environment where an external policy for energy is missing and the institutional requirements for it are not available, either. Another cardinal issue is that there should be a radical change in the fight against climatic change. All these are basic issues that require a coordinated energy policy.

Notes

1 For a long time, Great Britain used to be an opponent of the Community Energy Policy. The first signs of change appeared during the debate on the Constitutional Treaty, when Britain raised no objections to energy policy being included in the Treaty. The change of attitude was due to the fact that the once net energy exporter had become a net energy importer.

2 Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC, and Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC, *Official Journal L 176 of 15. 07. 2003*

3 The European Parliament discusses the second reading of the guidelines of the EP and the Council for trans-European energy networks (Proposal for a decision of the European Parliament and of the Council laying down guidelines for trans-European energy networks and repealing Decision No. 96/391/EC and No. 1229/2003/EC (COM (2003) 742 final – not published in the Official Journal)

4 Commission Green Paper, 22 June, 2005 "Energy Efficiency or Doing More With Less", COM (2005) 265, not published in the Official Journal

[5] Directive 2001/77/EC of the European Parliament and of the Council of 27 September 2001 on the promotion of electricity from renewable energy sources in the internal electricity market, *Official Journal L 283 of 27. 10. 2001;* Directive 2002/91/EC of the European Parliament and of the Council of 16 December 2002 on the energy performance of buildings, *Official Journal L oo1 of 04. 01. 2003;* Directive 2004/8/EC of the European Parliament and of the Council of 11 February 2004 on the promotion of cogeneration based on a useful heat demand in the internal energy market and amending Directive 92/42/EEC, *Official Journal L 52 of 21. o2. 2004;* Directive 2005/32/EC of European Parliament and of the Council of July 2005 establishing a framework for the setting of ecodesign requirements for energy-using products and amending Council Directive 92/42/EEC and Directives 96/57/EC and 2000/55/EC of the European Parliament and of the Council; Directive 2006/32/EC of the European Parliament and of the Council of 5 April 2oo6 on energy end-use efficiency and energy services and repealing Council Directive 93/76/EEC, *Official Journal L 114, 27. 04. 2006*

[6] On November 16, 2005, the Commission opened a broad discussion on the preliminary statement of the Directorate General for Competition on the comprehensive inquiry into competition in the internal gas and electricity markets. The inquiry had been launched in June 2005 after industrial consumers had complained about constantly rising prices and the lack of competition.

[7] Regarding the long-term power purchase agreements, the report highlighted Poland, Hungary and the Czech and Slovak Republics. It established that, in Hungary, 67 per cent of the consumption was based on such contracts, which were to expire in 2015–2022 (in the case of Poland, the rate was 45 per cent and the date of expiry 2017).

[8] The Hungarian stance urged the creation of compulsory natural gas security stocks, compulsory heating fuel stocks, the introduction of regulations on power station capacity as well as the introduction of collective measures increasing supply and reducing consumption in case of shortage of supply.

[9] Council Directive 2004/67/EC of 26 April 2004 concerning measures to safeguard security of natural gas supply, *Official Journal L 127, 29. 4. 2004*

[10] Poland formulated the opposite stance: intending to loosen the energy dependence on Russia, it issued a *General Declaration on the European Energy Security Treaty,* initiating a voluntary cooperation between NATO and EU Member States based on the principle of political solidarity. The initiative was doubtful from the very beginning in that it suggested solving the energy security of Europe by leaving out Russia, the country basically covering European import, or even by going against its interests.

[11] The Treaty took effect on July 1, 2006

[12] Including transport, which had not been part of the system before

[13] Germany maintained, for instance, that a better application of the existing legislation was sufficient for ensuring the secure supply for Europe.

[14] Green Paper "Energy" – A European Strategy for Sustainable, Competitive and Secure Energy, *COM, 2006, 105 final*

[15] The EC invited the Commission to make their proposals.

[16] According to IEA-surveys, world energy consumption could be reduced by 10 per cent by 2030, utilizing the currently available means of energy efficiency. 40 per cent of the energy used in the EU is used for buildings, two thirds of this by private consumers. Energy saving light bulbs use only one fifth of the energy of normal light bulbs. In stand-by function, television sets and video recorders use only 10 per cent of the average household energy in the EU.

[17] More than half of the Member States do have firm views and plans on the use of nuclear energy.

[18] One more reason why the issue cannot be avoided is that, according to calculations, alternative energy technologies will not be mature enough before 2030 to be realistically taken into account in meeting energy demand. Until then, security of supply could be increased by the use of nuclear energy and the commitments involved in meeting the Kyoto objectives could also be met.

[19] The basic principles are
- in the partnership cooperation with third countries, facilitation of the transparency of energy relations; mutually beneficial, open and transparent regulation of energy investment and trade, free of discrimination;

- contribution to the development of producer and export capacities of energy producing countries, infrastructural development;
- creation of a favorable investment environment in countries outside the Union, ensuring access to energy sources;
- ensuring access to export pipelines;
- increasing the environmental security of energy infrastructure;
- promotion of energy efficiency and the use of renewable energy sources;
- the application of Kyoto mechanisms;
- the diversification of energy imports;
- working out an international agreement for supplying countries in favor of using nuclear energy with uranium concentrate;
- the creation of strategic stocks by cooperation with neighboring countries.

[20] In the problem of cross-border takeovers, the debate on the merger of Gaz de France and Suez or the Spanish Endesa and the German EoN shows how sensitive Member States are when some of their sovereignty is to be sacrificed in energy issues. Member States are most dedicated to the view that in industries of key significance such as the energy industry, national giants must be protected. This is also made possible by the Takeover Directive, since governments have been given wide authority to take protective measures against aggressive foreign takeover attempts.

[21] Commission proposes an integrated energy and climatic change package to cut emissions for the 21st Century.

[22] Alan Riley: The Coming of the Russian Gas Deficit, CEPS (Center for European Policy Studies), *Policy brief, October 2006*

[23] So as to force out full ownership unbundling, Article 86 (3) of the EC Treaty, as the only article, empowers the Commission to initiate direct legislation without the approval of the European Parliament or the Council. On the basis of this, Commissioner of Competition Sir Leon Brittan ordered Member States to open up their public utility markets, the most significant of which were the telecommunications markets. In the gas industry, the key step from the point of view of competition would be to unbundle the ownership of services and of networks. The operator of the network would attain profits only if they allowed access to the pipeline. The more gas is transited through the pipeline, the higher the profits will be, which means a consequent fall in prices for the end user.

[24] France's stance was shared by the Czech Republic, Austria and Hungary, while Ireland, Lithuania and Sweden announced a reservation against the Commission's proposal.

[25] During the debate, Germany, holding the EU presidency, underlined that it did not rule out further liberalization measures but all Member States should first of all implement the regulations of Directive 2003/54 on the internal energy market, i.e. the legal unbundling of production and distribution. Thus, further liberalization steps could be taken only after the full implementation of the existing legislation. Full ownership unbundling must be preceded by the establishment of an Independent System Operator, which would supervise the operation of networks owned by integrated energy giants. If the Independent System Operator was indeed set up and operating, there was no need for ownership unbundling. The German government, forcefully supporting its energy companies, opined in any case that competition should not be restricted to the issue of ownership unbundling. For the unfolding of genuine competition, a strong regulatory system, as well as suitable incentives to facilitate investments, were necessary.

[26] Council Conclusions, Brussels, 8/9 March, 2007

[27] Dieter Helm (*Europe's energy future: in the dark,* www.opendemocracy.net, *16-1-2007)* maintains that the demand for the full liberalization of the energy market seems to have come too late, since the high concentration of the energy sector was achieved with the Commission's approval.

[28] In the field of energy, this common regulatory space already includes Norway and southeast Europe and is to soon include the south Mediterranean.

[29] Riley

[30] Partnership and Cooperation Agreements (PCA's) between the EU and Russia, 1 December, 1997. Regarding their legal form, PCA's are treaties, which is the highest rank in international law, and, as regards their contents, they are binding for both sides. PCA's, which are what is referred to as mixed agreements, are signed by Member States and the Community with third countries outside the Union. The main reason for this is that they authorize the Community to lead political dialogs, for

which it has no competence otherwise. PCA's are ratified by the national parliaments of Member States. The commitments made within the framework of PCA's are more restricted than those involved in European Agreements. On the other hand, political dialog is more intensive and the summits held every two years are complemented by ministerial meetings. What characterizes the Agreements signed with Russia is that they have not been implemented most of the time.

[31] According to OECD calculations, Russia could increase its exports by 30 per cent if it managed to reduce energy use by 10 per cent. In: Russian electricity reform: Emerging challenges and opportunities International Energy Agency (IEA), *Paris, 2004*

[32] In early 2007, Russian authorities closed the pipeline transporting oil to the Union via Belarus. Russia was forced to do so after Belarus had siphoned off some 79 thousand tons of oil from the raw material destined for the Polish and German markets. The background of the "business" dispute between the two sides was that at the end of last year, Russia had doubled the price of gas sold to Belarus, which was still just one third of the price of gas sold to Hungary. In return, Belarus imposed a transit duty on Russia oil transported to Europe, which Moscow found unlawful.

[33] The Energy Charter Treaty is a framework agreement regulating international energy trade, transit and investments. It grants foreign investors the same rights as to national investors and makes non-discriminatory access to pipelines possible. It establishes a legal framework for long-term cooperation in the energy sector. It declares several principles with reference to the world energy market, with reference to trade, investment and transit. The legal framework covers questions of national sovereignty on technology transfer, competition, environmental aspects, companies engaged in public commerce and on natural resources. In the trade of energy materials and products, WTO rules are applicable to all signatories of the Treaty. The Treaty was signed in December 1994 and entered into force in April 1998

[34] It is unacceptable for Russia that Asian republics could have free access to the Russian transit pipeline because in that case they would be able to transport gas 50 per cent cheaper than Russia. Russia, on the other hand, expects net profits for allowing access to energy production and transit.

[35] Russian and European gas interdependence, Dominique Finon and Catherine Locatelli, *Chier de recherché, LEPII January 2007*

[36] According to the president-CEO of the electricity industrial giant, there were gas restrictions in power stations in June 2006

[37] According to calculations, there will be a continuous and growing deficit in Russian gas exploitation from 2010 onwards. IEA, Optimizing Russian Natural Gas: Reform and Climate Policy, 2006

[38] Centrica is the owner of the gas supplier British Gas and controls 20 percent of the gas market in Britain, while it also has interest outside Great Britain. Under the change, the government's approval is necessary for takeovers affecting important gas service companies. (Until 2015, Gazprom will supply some 20 per cent of Britain's gas demand.)

[39] which means that Gazprom wishes to be actively involved not only in gas- but also in oil and electricity supply.

[40] The agreement is automatically prolonged unless partners withdraw from it.

[41] The EU-Russian strategic documents on the future of bilateral relations were endorsed in 1999 and the Road Maps of the Four Common Spaces, for the further development of these "four common spaces" were signed in 2005

[42] A commentary by Viktor Invanter, director of the Research Institute of Economic Predictions of the Russian Academy of Sciences, in *RIA Novost, June 15, 2006*

[43] Dieter Helm *(Europe's energy future: in the dark,* www.opendemocracy.net, *16-1-2007)* maintains that the demand for the full liberalization of the energy market seems to have come too late, since the high concentration of the energy sector was brought about with the Commission's approval.

[44] In addition to the big Member States (Germany, France, Italy), the Danish DONG and the Austrian OMV also signed agreements for 20 years.

[45] Dominique Finon, Catherine Locatelli