



OCCASIONAL PAPER SERIES

# **THE COMMON ENERGY MARKET OF THE EURASIAN ECONOMIC UNION**

Implications for the European Union and the role of  
the Energy Charter Treaty (ECT)

**Kristina Zemskova**  
Energy Charter Secretariat  
2018

## **DISCLAIMER**

Information contained in this work has been obtained from sources believed to be reliable. However, neither the Energy Charter Secretariat nor the work's author guarantees the accuracy or completeness of any information published herein, and neither the Energy Charter Secretariat nor the work's author shall be responsible for any losses or damages arising from the use of this information or from any errors or omissions therein. This work is published on the understanding that the Energy Charter Secretariat and the work's author supply the information but do not attempt to render legal or other professional services.

This study is published without prejudice to the position of Contracting Parties/Signatories of the Energy Charter Treaty or to their rights or obligations under the Energy Charter Treaty or any other international investment agreement. The contents of this work are the author's sole responsibility. They do not necessarily represent the views of the Energy Charter Secretariat.

© Energy Charter Secretariat, 2018

Boulevard de la Woluwe, 46

B-1200, Brussels, Belgium

Reproduction of this work, save where otherwise stated, is authorised, provided the source is acknowledged. All rights otherwise reserved. All the information contained in this paper is up-to-date as of January 2018.

ISSN : 2593-5666

**The common energy market of the Eurasian Economic Union:**

**implications for the European Union and the role of the Energy Charter Treaty (ECT)<sup>1</sup>**

*Executive summary*

The Eurasian Economic Union (EAEU) is often compared to the project of the European Union (EU). While one of the most common comparisons is the institutional structure of the EAEU, another important point of resemblance when noting the development of the Eurasian integration is its energy component. Russia stresses the security of demand as one of the primary issues of its national security and energy plays an important role in the country's external relations, while for other EAEU members the security of supply makes an important part of their economic prosperity. Similar to the EU, where energy became one of the driving forces behind the European integration, the initiative of a common energy market can play its role in the process of Eurasian integration. If created, the EAEU energy market would be one of the largest energy markets in the world. Strategically located, it would comprise a population of about 182 million and represent resources-rich countries, which collectively possess 14.6 % of the world's oil and 17.3% of its natural gas production.

Although it is unclear how quickly this integrated market will emerge, any reform move would present the EU with a new policy dilemma in its wider-neighbourhood: the common Eurasian energy market could either build new bridges in the region or deepen the fragmentation of energy markets and therefore worsen the current state of affairs between the EU, the Eastern Partnership countries and Russia. This paper aims to explore the effects that the emerging common energy market will have on the EU and its Energy Community project. The paper will give a brief overview of how the common Eurasian energy market is being founded, of existing divergence of interests and market asymmetries of respective EAEU Member States, and point to possible implications for the EU. In conclusion, the paper will provide some recommendations for EU-EAEU relations in the energy sector, including the possible role that can be played by the Energy Charter in the context of EU-EAEU relations.

---

<sup>1</sup> All the information contained in this paper is up-to-date as of January 2018.

## ***Background***

Attempts to promote reintegration in post-Soviet space have been ongoing since the early 1990s. Among the earliest initiatives have been the creation of the Union State of Russia and Belarus and the GUUAM group (Georgia, Ukraine, Uzbekistan, Moldova) which was launched in 1997. There was also an endeavour to mitigate the consequences of the dissolution of the single Soviet electricity system by means of creating the Electric Power Council of the Commonwealth of Independent States (CIS) back in 1992.

Nevertheless, the more comprehensive initiative to reintegrate national energy markets was undertaken within the Eurasian Economic Community (EEC) of Russia, Belarus, Kazakhstan, Kyrgyzstan, Tajikistan launched in 2000. The EEC was the first organisation containing agreements on development of fuel balances and common information management system for the energy market of the member states. In 2011 Belarus, Kazakhstan and Russia created the Eurasian Customs Union (EACU) which in 2012 evolved as a Single Economic Space (SES) of three countries with 17 basic inter-governmental agreements covering electric power, gas, oil and petroleum products which identified common principles and approaches towards access to services of natural monopolies and pricing.

In 2014 Belarus, Kazakhstan and Russia signed the founding treaty and in 2015 the Eurasian Economic Union (the EAEU) was established. Later, in 2015, Armenia and Kyrgyzstan also joined. The Treaty establishing the EAEU for the first time introduced an initiative to deepen integration of the participating states in the field of energy cooperation and to create a common market of energy resources<sup>2</sup>.

The declared intention of the EAEU to create a common energy market presents somewhat of a novelty in terms of analysing the prospects of such initiative for countries of the region as well as potential implications on the EU's energy policy.

First of all, compared to the previous integration initiatives, the novelty of the EAEU is in conferring to the union an international legal personality, which sets the EAEU as an international organisation in an effort to be acknowledged by other international actors. Thus, the

---

<sup>2</sup> Treaty on the Eurasian Economic Union, Section XX

EAEU as both “the next, advanced stage of the integration in the post-Soviet space”<sup>3</sup> and a culmination of the previous multi-step integration become a reality not only for the countries involved, but also for the regional integration organisations, international actors and the European Union (the EU).

Secondly, the institutional design of the EAEU is often compared to the EU: in the words of the Minister of the integration of the Eurasian Economic Commission T. Valovaya, “the European model of integration and its basic principles were used as a model for the Eurasian integration”<sup>4</sup>. Energy security concerns also underpinned the process of the European integration and the EU has its roots tracing back to the European Coal and Steel Community and the European Atomic Energy Community in 1950s.

In addition, the initiative of creating the common Eurasian energy market and, as a part of it, a common electricity market, reflects the two leading global trends – regionalisation and liberalisation (unbundling) - as means to ensure the effectiveness of the sector and allow the countries to meet their energy needs more effectively<sup>5</sup>. Nevertheless, the creation of the common electricity market within the EAEU along with the same process within the EU Energy Community might lead to a competition between these two regional projects and its institutional frameworks, which, in its turn, might lead to fragmentation in the region both regarding market designs and geopolitics.

### *Concepts for energy markets in the EAEU’s Treaty*

The Treaty of the newly established EAEU is mainly of a political importance for the participating states and, particularly, for Russia and Kazakhstan, as the two leaders of the integration process, as, in spite of the declared in the preamble commitment of the states to the further development of the Eurasian economic integration, the document contains a relatively small number of new provisions compared to the previously signed agreements. The Treaty

---

<sup>3</sup> В. Путин, «Новый интеграционный проект для Евразии — будущее, которое рождается сегодня» (V.Putin, «The new integration project for Eurasia – the future is being born today»). Available at: <https://iz.ru/news/502761> (consulted 9.12.2017)

<sup>4</sup> Т.Валовая, «Мы очень хорошо друг друга дополняем» ( Т.Valovya, “We complement each other quite well”). Available at: <http://eurasian-studies.org/archives/3564> (consulted 9.12.2017)

<sup>5</sup> I. Kustova, “Regional Electricity Cooperation in the South Caucasus - Energy Charter” – p. 5.

consists of four parts, two of which – part two and three (76 articles out of 118) basically doubles the 2009 Treaty on the Custom Union and the 2011 Treaty on Single Economic Space<sup>6</sup>.

The first part of the Treaty confines the EAEU with an international legal personality as well as defines the decision-making process and the new bodies of the EAEU, which in fact have been already existing within the previous (the Customs Union, SES) blocs. The institutional structure of the union includes the Supreme Eurasian Economic Council, which meets on the level of the heads of member states (i.e. presidents), the Eurasian Intergovernmental Council consisting of the heads of governments (i.e. prime-ministers), the Eurasian Economic Commission as an executive body responsible for routine questions and the Court of the Eurasian Economic Union. Decisions which are fundamental to the functioning of the EAEU, including energy issues, are taken by the Council.

Principles of cooperation in the energy sector are defined by Section XX of the part three of the Treaty, while part four contains new transitional and final provisions. The parties declare their common intention to create the common electricity market by July 2019, and the common markets of gas, oil and petroleum products by July 2025<sup>7</sup>. Until the mentioned dates, the access to the services of natural monopoly entities in the electrical power sector, in the sphere of gas transportation and functioning of the common market of oil and petroleum products shall be determined by the respective protocols to the Treaty<sup>8</sup>. Other transitional provisions of the Treaty are also related to the movement of goods that in fact means finalization of the creation of the Customs Union<sup>9</sup>.

Thus, compared to the Customs Union Treaty and the Single economic space initiatives, one of the main distinguishing features of the EAEU are the provisions aimed at creation of the internal energy market and conferring the union with its international legal personality. The empowerment of the EAEU with a legal personality has been of crucial importance in promoting the vision of the Union as an international organization that other international bodies, such as

---

<sup>6</sup> А. Кнобель, “Евразийский экономический союз: перспективы развития и возможные препятствия”, Вопросы экономики, 2015 № pp.87-108 (A. Knobel “*Eurasian economic union: perspectives and problems*”, *Voprosy ekonomiki* 2015 № pp.87-108). Available at: [https://iep.ru/files/text/nauchnie\\_jurnali/knobel\\_vopreco\\_3-2015.pdf](https://iep.ru/files/text/nauchnie_jurnali/knobel_vopreco_3-2015.pdf) (consulted 9.12.2017)

<sup>7</sup> Treaty on the EAEU, Article 104.

<sup>8</sup> Treaty on the EAEU, Annexes XX-XXIII.

<sup>9</sup> A. Knobel, “*Eurasian economic union: perspectives and problems*”, p. 89.

the EU, will have to engage with on an inter-regional basis rather than with the individual countries, as was the case before.<sup>10</sup> The ambitiously promised creation of the common energy markets of electricity, gas, oil and oil products will require harmonization of legislation aimed at establishing comparable legal regulations in these spheres, and eliminating the numerous existing non-tariff barriers is instrumental in addressing abiding existing tensions within spheres of electricity, oil and gas between the member-states.

### *Conceptualization of the common markets*

According to Article 79<sup>11</sup> of the Treaty on the EAEU, the Members States are developing a long-term mutually beneficial cooperation in the energy sector, implementing a coordinated energy policy and carrying out a step by step building of the common market of energy resources (electricity, gas, oil and oil products) in order to ensure efficient use of the potential of fuel and energy complexes.

The energy sectors to a large extent determine dynamic of the development of national economies and their competitiveness on the world market. Thus, the main goals of forming the common energy markets are to ensure the stable supply of energy resources to the national markets of participating states, enhance their energy security (both of supply and demand) and to foster the countries' positions on the global energy markets<sup>12</sup>.

Among the general principles behind the gradual establishment of the common market for energy resources are market pricing, development of competition, elimination of all types of barriers to trade in energy resources, development of transport infrastructure, creation of environment favourable for attracting investments in energy sector, gradual harmonization of national rules and regulations related to operational dimension and business infrastructure.

For oil and oil products, the creation of common market is envisioned in three stages: development of the programs (2016-2017), realization of the programs' provisions (2018-2023)

---

<sup>10</sup> K. Wolczuk , R. Dragneva, *“The Eurasian Economic Union: Deals, Rules and the Exercise of Power”*, Chatham house, 2017. Available at: <https://www.chathamhouse.org/publication/eurasian-economic-union-deals-rules-and-exercise-power> (consulted 9.12.2017)

<sup>11</sup> Treaty on the EAEU, Article 79.

<sup>12</sup> Л. Шенец, *“Создание общих рынков энергетических ресурсов как главный фактор повышения энергетической безопасности Евразийского экономического союза”* (A. Shenec, *“The creation of common energy markets as the main factor of energy security of the EAEU”*), September 2017, Astana.

and entering into force of respective international treaties (prior to 2024). The Concept for Establishing of Common Market of oil and petroleum products was adopted on May 2016 and is aimed at promoting energy security of the member states and strengthening their positions on the world oil and petroleum products markets. The concept provides a set of common rules for trade in oil and oil products (such as elimination of tariff barriers and export duties), unification of norms and standards for oil and petroleum products, rules for equal access to the infrastructure and distribution of the transport system capacities. Export tariffs (export customs duties), however, remain subject to each country's national legislation though there are some plans to harmonize them<sup>13</sup>.

Nevertheless, the key questions in the concept such as the pricing mechanism and unification of technical standards have already created debates due to the Member States' divergent interests. Regarding the pricing method, the concept suggests application of market prices to oil and oil products. Russia has a market oil price aligned to the international oil prices, while its tax reform is supposed to gradually bring domestic oil prices in line with international pricing through increasing its mineral extraction tax<sup>14</sup>. Belarus and Kazakhstan<sup>15</sup> suggest lowering the price by excluding from pricing the expenses for purification and transportation of the oil and oil products<sup>16</sup>. In other words, Kazakhstan and Belarus seek to differentiate tariffs between exports and domestic deliveries, while Russia wants all tariffs to be the same for all types of shipments<sup>17</sup>. Harmonization of quality standards is favoured by Kazakhstan and Belarus, while Russia believes such approach unrealistic due to the fact that oil and oil products are streamed from a several field and would, in any case, lead to significant expenses<sup>18</sup>.

---

<sup>13</sup> “*Consultation non a Multilateral Framework Agreement on Transit: position of Kazakhstan*”, The Energy Charter Secretariat, Room document 2, Implementation Group Meeting, 14 September 2017.

<sup>14</sup> “Russia postpones scrapping oil export duties to 2022-2025”, Reuters, March 2017. Available at: <https://www.reuters.com/article/us-russia-oil-tax-exports/russia-postpones-scrapping-oil-export-duties-to-2022-2025-idUSKBN16K23F> (consulted 9.12.2017)

<sup>15</sup> “*Consultation non a Multilateral Framework Agreement on Transit: position of Kazakhstan*”, The Energy Charter Secretariat.

<sup>16</sup> А. Белокопытов, “Энергетическое сотрудничество государств ЕАЭС: предпосылки, тенденции, перспективы” (A. Belokopytov “Energy cooperation of the EAEU Member States: tendencies and perspectives”), Available at: [https://www.imemo.ru/files/File/ru/conf/2016/29042016/01\\_06\\_Belokopytov.pdf](https://www.imemo.ru/files/File/ru/conf/2016/29042016/01_06_Belokopytov.pdf) (consulted 9.12.2017)

<sup>17</sup> “*Consultation non a Multilateral Framework Agreement on Transit: position of Kazakhstan*”, The Energy Charter Secretariat.

<sup>18</sup> M. Pastukhova, K. Westphal, “*A common energy market in the Eurasian Economic Union: implications for the EU and relations with Russia*”, German Institute for International and Security affairs, February 2016. Available at:



Furthermore, besides the mentioned activities, the creation of fully functioning common market of oil and oil products will require more inclusive domestic reforms in the domain of privatization, competition, unbundling, tariff regulation and creation of an independent regulator.<sup>19</sup>

The same implementation timeline provided for the EAEU natural gas market. The respective Concept was approved and adopted by Council in 2016 and 2017 respectively. The Concept for the formation of the common gas market lists such measures as unification of norms and standards, unified pricing mechanism, the common set of rules for access to the infrastructure entities based on the territory of the member states.

However, though the agreement calls to eventually establish a common set of prices on a netback parity basis, neither details on timing nor specifics of the netback calculation have so far been officially agreed<sup>20</sup>. The same situation is with harmonization of standards, although this measure is listed as a priority. Another problem is the currently regulated by intergovernmental agreements destination clauses, meaning that the buyer does not have a right to resell the purchased cargo in another area except what is agreed in agreement: Russia persists that access should be available only for resell to other EAEU countries<sup>21</sup>. In addition, the current energy cooperation among the states is based on the existing bilateral agreements signed as from 2010 with the implementation dates up to 2040. Therefore, such agreements will need a revision according to the envisioned dates of the launch of the energy markets (2025).

To this day, the prospects for the creation of a common electricity market are the most realistic and advanced within the EAEU framework, putting the electricity market into the position of the key driver of integration<sup>22</sup>. As announced, the countries are planning to launch the market already by July 2019 with the implementation period defined as 2016-2018. The priority of

---

[https://www.swpberlin.org/fileadmin/contents/products/comments/2016C09\\_Pastukhova\\_wep.pdf](https://www.swpberlin.org/fileadmin/contents/products/comments/2016C09_Pastukhova_wep.pdf) (consulted 9.12.2017)

<sup>19</sup> M. Pastukhova, K. Westphal, “A common energy market in the Eurasian Economic Union: implications for the EU and relations with Russia”, German Institute for International and Security affairs, February 2016. Available at: [https://www.swpberlin.org/fileadmin/contents/products/comments/2016C09\\_Pastukhova\\_wep.pdf](https://www.swpberlin.org/fileadmin/contents/products/comments/2016C09_Pastukhova_wep.pdf) (consulted 9.12.2017)

<sup>20</sup> “Consultation non a Multilateral Framework Agreement on Transit: position of Kazakhstan”, The Energy Charter Secretariat.

<sup>21</sup> *Ibid.*

<sup>22</sup> Pastukhova, K. Westphal, “A common energy market in the Eurasian Economic Union: implications for the EU and relations with Russia”.

establishment and the greater degree of progress of the electricity market is attributed to the legacy of the Soviet electricity system with its numerous organizational and technical advantages.<sup>23</sup>

Several formation options were considered as a model for the EAEU electricity market. Among the considered options were such as to take the Russian wholesale electricity market as a model, or to create in Russia a regional electricity market similar to the ones of Kazakhstan and Belarus. Finally, the parties, due to market differences and unwillingness of Member States to restructure their local markets<sup>24</sup>, opted for the third way, which is based on the EU's model for continental electricity market and allows the formation of a common electricity market while preserving national markets<sup>25</sup>. The process is expected to be implemented in life in three major steps which are harmonization, unbundling and creation of a supranational independent regulator. Formation of the common electricity market will require relevant domestic reforms, but the process might take time as the starting points of the participating markets diverge significantly. Thus, the Belarus market is under full state control, while the Russian one is relatively liberalized and run by partially privatized companies. The market of Kazakhstan is similar to the Russian one but with a different pricing mechanism. Kyrgyzstan's electricity market is partially liberalized.

The creation of the common electric power market is supposed to improve reliability and efficiency of the electric systems, increase volumes of trade in electricity and energy security of states, increase the competitiveness of the market, meet the consumer demand for electric energy, increase pricing transparency and form the united pricing method. According to the already approved concept, the creation of the market will undergo in three stages: development and approval of the program (2015 – 2016), implementation (2016-2018), conclusion and entry into force (2018-2019). The envisioned market is to be based on principles of cooperation, gradual harmonization of the legislation, unhindered access to services of natural monopolies. The common market is supposed to solve the pricing issue and establish a unified pricing method, as well as to introduce a trading platform at the international level (the Council of the

---

<sup>23</sup> I. Kustova, “*Regional Electricity Cooperation in the South Caucasus - Energy Charter*”, the Energy Charter Secretariat, April 2016. Available at: <http://www.energycharter.org/what-we-do/knowledge-centre/occasional-papers/regional-electricity-cooperation-in-the-south-caucasus/> (consulted 9.12.2017)

<sup>24</sup> Pastukhova, K. Westphal, “*A common energy market in the Eurasian Economic Union: implications for the EU and relations with Russia*”.

<sup>25</sup> *Ibid.*

Common electricity market) designed to ensure coordination of the market and grant non-discriminatory access to national transmission grids. In spite of the position of Belarus, the negotiations on electricity market are the most advanced.

To sum up, it can be concluded that the most decisive issues still have to be negotiated by the parties and this process is expected to be cumbersome due to the different economic interests of the Member States. The strongest driver behind the negotiations remains to be Moscow.

### *The envisioned energy market and asymmetry of interests*

The envisioned energy market would be strategically located within Europe and Asia, encompassing a total population about 182 million people. The total oil production of the countries comprising the market would represent 14.6% of global production. The total gas production of the EAEU accounts for 18.4% of total global production (ranking second in the world) and power generation equating to 5.1% of global electric power production (ranking fourth in the world).<sup>26</sup> It is worth mentioning that these figures are mainly owed due to Russian membership of the EAEU, with Kazakhstan contributing 1.9% and 0.6% in gas and oil production respectively. Considerably small oil and gas reserves were discovered in Belarus while there are no such resources in Armenia<sup>27</sup>.

In 2015 EAEU Member States decided to increase their oil and gas extraction as well as electricity production. The Member States produced 614.4 million tons of oil (of which 306.5 million was exported to third countries), 679.3 billion cubic meters (bcm) of gas (173 bcm exported), and 1212.8 billion kWh of electric energy (19.7 billion kWh exported)<sup>28</sup>. The majority of energy produced in the EAEU is exported to third countries. Intra-bloc trade remains low and has even decreased in recent years.

One of the most striking and discussed features of the EAEU is an asymmetry of its energy markets and unevenness of the interests of the participating states. The EAEU's market is characterised by the domination of the redistributive motive over the creative one.<sup>29</sup> In other

---

<sup>26</sup> The EAEU's website. Available at: <http://www.eaeunion.org/?lang=en> (consulted 9.12.2017)

<sup>27</sup> *Ibid.*

<sup>28</sup> The Eurasian Economic Union Commission's website. Available at: <http://www.eurasiancommission.org/en/Pages/default.aspx> (consulted 9.12.2017)

<sup>29</sup> A. Knobel, "*Eurasian economic union: perspectives and problems*".

words, the transfer of oil and gas from Russia to other the EAEU's members is both a necessary redistribution mechanism and a condition for getting the potential positive economic effects inside the EAEU.<sup>30</sup> While forming the Customs Union in 2010, the participating states of Russia, Belarus and Kazakhstan created a common space for the circulation of goods within the union without internal tariffs, but agreed on applying a common external tariff. Notably, the countries had to agree on the application of Russia's external tariff level as a basis, which was much higher than the tariff levels of Belarus, Armenia, and Kazakhstan and could have affected their openness to global trade.<sup>31</sup> Regarding trade in energy, the participating states agreed on non-application in mutual trade of quantitative restrictions and export customs duties (taxes and fees) whereas the export tariffs for oil and petroleum products exported outside the union are decided by the Members States based on the bilateral treaties.<sup>32</sup> In other words, the Member-States do not pay an export tariff for the import of energy goods but impose such tariff when exporting (if allowed) them to third countries. In reality, this means an indirect subsidizing by Russia through selling gas and oil at prices below the world market ones.

While trade in oil and gas between resource-rich Russia and Kazakhstan is relatively low, the Belarus economy is heavily dependent on the access to the Russian hydrocarbons and - unlike the case with Kyrgyzstan and Armenia - Russia is Belarus's main trade partner accounting for 47% of all the trade. Belarus imports Russian crude oil (of which 45-50% were used for production of oil products to export) and natural gas (which were not directly re-exported) for the prices below the market ones, paying \$173 for 1000 cubic meters of gas (for comparison - \$250 for Armenia, \$430 for Ukraine)<sup>33</sup>. Taking into account that Belarus is exempt from paying an export tariff (30% of the price), Russian budget is losing approximately \$73 for 1000 cubic meters or \$9,5 million in total (\$8.5 for crude and \$1 for gas). Prior to 2013, Russian budget was receiving from Belarus compensation of \$4 billion for those 45-50% of oil exporting to the third countries, but, according to new rules, from 2015 the compensation has been cancelled<sup>34</sup>. Thus,

---

<sup>30</sup> A. Knobel, "*Eurasian economic union: perspectives and problems*".

<sup>31</sup> N. Popescu, "*Eurasian Union: the real, the imaginary and the likely*", European Union Institute for Security Studies., Chaillot Papers N° 132, September 2014 – p. 12.

<sup>32</sup> Treaty on the EAEU, Annex XXIII (3)

<sup>33</sup> A. Knobel, "*The price of the Union*", *Vedomosti*, 13 January 2014. Available at: <https://www.vedomosti.ru/newspaper/articles/2014/01/13/cena-tamozhennogo-soyuza> (consulted 9.12.2017)

<sup>34</sup> "*Belarus and the Eurasian Economic Union: The view from Minsk*", the European Council for Foreign Relations, January 2015. Available at:

the Russian transfer to Belarus economy is around \$10 milliard that corresponds to 15% of its GDP.<sup>35</sup>

Belarus is naturally interested in the current state of affairs with respect to low-cost and reliable supplies of Russian oil and gas. For this reason, Minsk, being 90% dependent on Russian gas for its electricity production<sup>36</sup>, insists on giving priority to the development of the common oil and gas markets, subverting the on-going negotiations on the launch of the electricity market. Russia-Belarus energy relations within the EAEU are based on the bargaining power, when Russia, being interested in the political strengthening of the union, at the annual negotiations allows Belarus to secure the favourable terms of energy imports to the detriment of its economic interests<sup>37</sup>, and Belarus has little choice but to rely on the economic support of its neighbour.

The situation with Armenia is somewhat similar: Yerevan's accession to the EAEU has reduced the gas import price from \$271 in 2014 to \$189 in 2015. This equates to \$82 that the Russian budget fails to receive from each 1000 cubic meters of gas exported<sup>38</sup>, or corresponds to 2% of Armenia's GDP<sup>39</sup>. For Armenia, which is highly dependent on Moscow for its energy security (Moscow deliver 75% of its energy requirements)<sup>40</sup>, the situation in the energy sector is similar to Belarus and the role of the economic carrot is played by reduced energy prices. Addition, Armenia is also in the Union due to geopolitical factors – Moscow shores up Yerevan's national security concerns in the South Caucasus.

Kyrgyzstan and Russia cooperate mainly in the sector of hydropower, but the latest hydropower deal between the countries was cancelled due to Russia's Inter RAO inability to fund the

---

[http://www.ecfr.eu/article/commentary\\_belarus\\_and\\_the\\_eurasian\\_economic\\_union\\_the\\_view\\_from\\_minsk](http://www.ecfr.eu/article/commentary_belarus_and_the_eurasian_economic_union_the_view_from_minsk) (consulted 9.12.2017)

<sup>35</sup> A. Knobel, "The price of the Union", *Vedomosti*.

<sup>36</sup> "The story that never ends. A new stage in the energy dispute between Russia and Belarus", OSW, May 2017. Available at: <https://www.osw.waw.pl/en/publikacje/osw-commentary/2017-05-17/story-never-ends-a-new-stage-energy-dispute-between-russia-and> (consulted 9.12.2017)

<sup>37</sup> A. Knobel, "Eurasian economic union: perspectives and problems".

<sup>38</sup> *Ibid.*

<sup>39</sup> "Кризис и налоговый маневр как испытание для ЕАЭС" ("Crisis and tax reform as a test for the EAEU"). Available at: <https://www.vedomosti.ru/newspaper/articles/2015/02/17/integratsiya-ispitanie-eaes#/galleries/140737492096660/fullscreen/1> (consulted 9.12.2017)

<sup>40</sup> T. Togt, F. Motesano, I. Kozak, "From completion to Compatibility Striking a Eurasian balance in EU-Russia relation", Clingendael, October 2015. Available at: <https://www.clingendael.org/publication/competition-compatibility-striking-eurasian-balance> (consulted 9.12.2017)

project<sup>41</sup>. Another field of cooperation is a gas sector (transfer of Kyrgyzgas system to the control of Gazprom). At the same, Kyrgyzstan's GDP is less than 3% of the EAEU total output while Russia accounts for 33% and 13% of its imports and export respectively. For that reason Kyrgyzstan is unable to pursue a more or less independent foreign policy. The main attraction of the EAEU Treaty for Kyrgyzstan is the labour provisions, as labour migration makes around 25% contribution to the country's GDP, while migrant workers from Kyrgyzstan represent the third largest group in Russia. In this light, the respective provisions of the Treaty such as free movement of workers, allowing for employment without employment permits and exemptions from an obligation to register for the first 30 days<sup>42</sup>, are of particular interest for Kyrgyzstan. Similar to the case of Armenia, Kyrgyzstan's choice for the EAEU lies in the combination of security reasons and Russian subsidies.

Such asymmetry has the potential to create obstacles for the single energy market due to the divergent interests between resources-rich Russia and Kazakhstan, on the one hand, and Armenia, Belarus, Kyrgyzstan on the other. At the same time, due to the complex connection between energy dependence and integration, the business of the countries are closely linked, with Russia's Gazprom having business links in all of the EAEU countries<sup>43</sup>.

### *Implications for the EU*

The creation of EAEU common energy market and common electricity market, as its most advanced component, will present the EU with a new set of policy dilemmas to deal with in the wider-European neighbourhood.

Besides the fact that the EU foundation treaties were devoted to energy issues and there were some initiatives within the gas and electricity sectors, the first comprehensive EU energy policy was presented only in 2006 and called for enhancing sustainability, competitiveness and security

---

<sup>41</sup> *Kyrgyzstan Revokes Hydropower Deal With Russia*, January 2017. RFERL. Available at <https://www.rferl.org/a/qishloq-ovozi-kyrgyzstan-energy-dreams/27499926.html> (consulted 9.12.2017)

<sup>42</sup> Treaty on the EAEU, Article 97.

<sup>43</sup> A. Wenger, R. Orttung, J. Perovic, *Russian Business Power: The Role of Russian Business in Foreign and Security Relations*, Routledge, 1 edition (October 16, 2006)

of supply<sup>44</sup>. Following the 2009 Treaty on Functioning of the European Union (the TFEU), the EU presented the provisions ensuring for completion of EU internal electricity market<sup>45</sup>, in 2011 the initiative for the completion of the internal electricity market was introduced by the European Council and in 2015 the concept of the Energy Union was suggested. With the aim to extend the EU's internal energy market rules and its principles to south-eastern Europe and the Black Sea region on the basis of a legally binding framework, in 2006 the EU Energy Community was established. As of July 2017, the Energy Community has ten members, the European Union and nine Contracting Parties, and three observers, one of which is Armenia. The signing states commit to implement key EU energy law, develop a regulatory framework and liberalize their energy markets in line with the Treaty acquis.

Thus, there is a potential conflict of interest between the two regional integration projects as they imply the creation of overlapping authorities and legislative frameworks<sup>46</sup>. Currently, Armenia is creating a common electricity market within the EAEU, while neighbouring Georgia is negotiating its accession to the EU Energy Community. It is noteworthy, that on the post-Soviet space the choices of the states, including those related to regional economic integration, are highly influenced by historical legacies and their security considerations, and any fruitful cooperation will require resolution of political and domestic issues<sup>47</sup>. This political complexity might be intensified by the mentioned integration dynamics in the region. In the current situation with the electricity markets, the regionalization, as the global trend of the recent decades might, on one hand, lead to liberalization and integration of the domestic markets. At the same time, such regional initiatives might contribute to the further fragmentation in market designs and negatively impact the EU Eastern Partnership policy.

Another option - and in the long-term a more beneficial one - would be a cooperation with the emerging EAEU on technical, operational and regulatory levels in spite of the existing political differences, the Western sanctions and the Ukrainian crisis issue. The EU - which generally

---

<sup>44</sup> EC Green Paper on A European Strategy for Sustainable, Competitive and Secure energy

<sup>45</sup> *"The Role of the Energy Charter Treaty in Fostering Regional Electricity Market Integration: Lessons Learnt from the EU and Implications for Northeast Asia"*, the Energy Charter Secretariat, 2015 – p. 58. Available at: <http://www.energycharter.org/what-we-do/investment/investment-thematic-reports/the-role-of-the-energy-charter-treaty-in-fostering-regional-electricity-market-integration-lessons-learnt-from-the-eu-and-implications-for-northeast-asia/> (consulted 9.12.2017)

<sup>46</sup> I. Kustova, *"Regional Electricity Cooperation in the South Caucasus - Energy Charter"* – p. 5.

<sup>47</sup> *Ibid.*

welcomes new regional integration initiatives - has been treating the EAEU with some animosity, regarding it as a predominantly geopolitical project as well as attempt by Russia to restore the Soviet Union's architectural design aimed at isolating the region from cooperation with the EU. At the same time, the officials from the EAEU's side have repeatedly expressed their interest in developing a constructive dialogue with the EU. The parties should be pragmatic and, noting the energy potential of the Eurasian region, should strive for such common partnerships that would serve their interests rather than become a subject of disagreements.<sup>48</sup> Taking into account the fact that the planned EAEU's energy market has been developing based on the WTO framework, this only increases the compatibility level of the EAEU and the EU to create a potential space for a pragmatic cooperation<sup>49</sup>. In addition, as was mentioned earlier, the model of the European continental electricity market was taken as a model for the EAEU common electricity market, which reminds us of the idea mentioned in Russian President Putin's thoughts on the common economic space "from Lisbon to Vladivostok" articulated back in 2010.<sup>50</sup>

### *The role of the Energy Charter Treaty (ECT)*

At the technical level, the Energy Charter Treaty, as a politically neutral and legally binding instrument, as well as inter-state process of energy dialogue, can provide a platform for cooperation and discussion between the EU and the EAEU. The Energy Charter, launched in 1990 as an opportunity for stable cooperation between Western and Eastern European countries, brings together 54 members, including the EU, its Member States and the countries of Eurasia. Russia, as a Signatory of the Treaty, applied it provisionally until 2009 but has never ratified it. The Energy Charter Treaty provides a legal framework for cooperation in the field of energy and covers such important aspects as investment protection, trade in energy, transit issues, energy efficiency, dispute resolution and other relevant areas.

One of the aims of establishing the common Eurasian energy market is to enhance participating's states positions on the global energy market that would require creation of an attractive

---

<sup>48</sup> E. Vinikurov, "The EAEU and the EU", Regnum, September 2016. Available at: <https://regnum.ru/news/2173129.html> (consulted 9.12.2017)

<sup>49</sup> *Ibid.*

<sup>50</sup> "Владимир Путин рассказал о перспективах сотрудничества России и Европы" ("V. Putin on Russia and Europe cooperation perspectives"), Rossiskay Gazeta, October 2011. Available at: <https://rg.ru/2010/11/26/putin.html> (consulted 9.12.2017)



investment climate in the countries. At the same time, energy business and energy projects are usually based on a long term approach and the respective investments require both a proper risk assessment and confidence of stakeholders. Therefore, from that perspective, the ECT allows the creation of legal framework that provides both for certainty and protection of investors (which includes provision of the definition of investments, equal treatment, expropriation, transfer of payments etc.) as well as interests of the host country.

Removal of barriers to trade of energy products and services is another vital element necessary for the creation of properly functioning and competitive energy market. The ECT provides for a stable, predictable and non-discriminatory regime for energy-related trade among the ECT contracting parties and has a legal framework based on GATT and WTO provisions. The ECT extends both benefits and obligations of WTO membership to the energy sector, which basically means that trade in the energy sector is treated as if all contracting parties were the members of the WTO<sup>51</sup>. This is particularly relevant for Belarus, which is not yet a WTO member<sup>52</sup>.

Transit of energy products among producing, importing and transit countries – which is exactly the case of the EAEU - is essential for the liberalization of trade in energy, and the ECT provides respective sets of rules to ensure discrimination-free transit. In addition, the ECT establishes two-sided dispute resolution mechanisms (state-to-state as well as investor-state arbitration) to ensure applicability and enforceability of its provisions. Above all, the advantage of the Energy Charter as a platform for the cooperation between the two regional projects is the ECT's respect for national sovereignty over energy resources and, therefore, its political neutrality.

Further, expansion of the ECT largely adopts a regional approach, endorsing regions comprised of certain groupings of states and de facto promoting regional cooperation and working with regional organizations<sup>53</sup>. This is particularly important from the perspective of the emerging EAEU electricity market. Thus, the Energy Charter with its technical expertise and experience in the region could play the role of an implementing agency which would take into account

---

<sup>51</sup> *“The Role of the Energy Charter Treaty in Fostering Regional Electricity Market Integration: Lessons Learnt from the EU and Implications for Northeast Asia”*, the Energy Charter Secretariat.

<sup>52</sup> *Belarus resumes WTO membership negotiations*, WTO. Available at: [https://www.wto.org/english/news\\_e/news17\\_e/acc\\_blr\\_24jan17\\_e.htm](https://www.wto.org/english/news_e/news17_e/acc_blr_24jan17_e.htm) (consulted 9.12.2017)

<sup>53</sup> *“The Role of the Energy Charter Treaty in Fostering Regional Electricity Market Integration: Lessons Learnt from the EU and Implications for Northeast Asia”*, the Energy Charter Secretariat.

specificity of the parties and contribute through regulatory frameworks to the development of inter-regional cooperation and achievements of the markets outcomes.

In view of the above, and to conclude, we draw the attention of the reader to the following recommendations:

- The EU should pay close attention to the regional developments within the evolving energy market of the EAEU.
- In order to avoid potential further fragmentation of regional markets which can result in competitive legal and institutional frameworks and affect the EU's Eastern Partnership policy, it is advisable to seek a dialogue and find appropriate ways for cooperation with the respective authorities of the EAEU, in spite of political disagreement between the EU and Russia over Ukraine and the imposition of Western sanctions on Moscow.
- Such dialogue could be developed through existing platforms such as the Energy Charter process. The majority of the Member States of both the EU and the EAEU are also members of the ECT.
- As has already been demonstrated above, on the technical level there are good opportunities for initiating cooperation with the EAEU in developing its common electricity market. From the long term perspective this could contribute to the compatibility and complementarity of both systems (in the EU and in the EAEU).
- The EAEU can also learn some lessons from the EU for developing its internal electricity market including EU regional experience in cross-border electricity trade and transit of electricity through transmission grids, attracting investments, market coupling.

## BIBLIOGRAPHY

### I PRIMARY SOURCES

#### 1. Official Documents

- The Energy Charter Treaty, Available at: <http://www.energycharter.org/process/energy-charter-treaty-1994/energy-charter-treaty/> (consulted 9.12.2017)
- EC Green Paper on A European Strategy for Sustainable, Competitive and Secure energy/ Brussels, 8.3.2006 COM(2006) 105 final. Available at: [http://europa.eu/documents/comm/green\\_papers/pdf/com2006\\_105\\_en.pdf](http://europa.eu/documents/comm/green_papers/pdf/com2006_105_en.pdf) (consulted 9.12.2017)
- “Consultation non a Multilateral Framework Agreement on Transit: position of Kazakhstan”, The Energy Charter Secretariat, Room document 2, Implementation Group Meeting, 14 September 2017.
- Treaty on the Eurasian Economic Union. Available at: [http://www.un.org/en/ga/sixth/70/docs/treaty\\_on\\_eeu.pdf](http://www.un.org/en/ga/sixth/70/docs/treaty_on_eeu.pdf) (consulted 9.12.2017)
- Treaty on Functioning of the European Union
- Договор о Таможенном союзе и Едином экономическом пространстве. Available at: [http://www.eurasiancommission.org/ru/act/trade/catr/nontariff/Pages/Dogovor\\_26021999.aspx](http://www.eurasiancommission.org/ru/act/trade/catr/nontariff/Pages/Dogovor_26021999.aspx)
- A Framework Strategy for a Resilient Energy Union with a Forward-Looking Climate Change Policy /\* COM/2015/080 final. Available at: <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=COM:2015:80:FIN> (consulted 9.12.2017)

#### 2. Websites

- Energy Community Secretariat . Available at: <https://www.energy-community.org/> (consulted 9.12.2017)
- The EAEU’s website. Available at: <http://www.eaeunion.org/?lang=en> (consulted 9.12.2017)
- The Eurasian Economic Union Commission’s website. Available at: <http://www.eurasiancommission.org/en/Pages/default.aspx> (consulted 9.12.2017)
- The World Trade Organisation website. Available at: [https://www.wto.org/english/news\\_e/news17\\_e/acc\\_blr\\_24jan17\\_e.htm](https://www.wto.org/english/news_e/news17_e/acc_blr_24jan17_e.htm) (consulted 9.12.2017)

## II SECONDARY SOURCES

### 1. Books

- Wenger A., Orttung R., Perovic J., Russian Business Power: The Role of Russian Business in Foreign and Security Relations, Routledge, 1 edition (October 16, 2006).
- Yergin D., The Quest: Energy, Security, and the Remaking of the Modern World, Penguin Books; Updated, Revised, Reprint edition (September 26, 2012), 832p.

### 2. Articles

- Kustova I., “Regional Electricity Cooperation in the South Caucasus - Energy Charter”, the Energy Charter Secretariat, April 2016. Available at: <http://www.energycharter.org/what-we-do/knowledge-centre/occasional-papers/regional-electricity-cooperation-in-the-south-caucasus/> (consulted 9.12.2017)
- Kyrgyzstan Revokes Hydropower Deal With Russia, January 2017. RFERL. Available at <https://www.rferl.org/a/qishloq-ovozi-kyrgyzstan-energy-dreams/27499926.html> (consulted 9.12.2017)
- Mankoff J., Eurasian Energy Security, Council on Foreign Relations, Council Special Report No. 43 February 2009.
- Pastukhova M., Westphal K. “A common energy market in the Eurasian Economic Union: implications for the EU and relations with Russia”, German Institute for International and Security affairs, February 2016. Available at: [https://www.swpberlin.org/fileadmin/contents/products/comments/2016C09\\_Pastukhova\\_wep.pdf](https://www.swpberlin.org/fileadmin/contents/products/comments/2016C09_Pastukhova_wep.pdf) (consulted 9.12.2017)
- Popescu N, “Eurasian Union: the real, the imaginary and the likely”, European Union Institute for Security Studies., Chaillot Papers N° 132, September 2014.
- Russia postpones scrapping oil export duties to 2022-2025”, Reuters, March 2017. Available at: <https://www.reuters.com/article/us-russia-oil-tax-exports/russia-postpones-scrapping-oil-export-duties-to-2022-2025-idUSKBN16K23F> (consulted 9.12.2017)
- “The Role of the Energy Charter Treaty in Fostering Regional Electricity Market Integration: Lessons Learnt from the EU and Implications for Northeast Asia”, the Energy Charter Secretariat, 2015 – p. 58. Available at: <http://www.energycharter.org/what-we-do/investment/investment-thematic-reports/the-role-of-the-energy-charter-treaty-in-fostering-regional-electricity-market-integration-lessons-learnt-from-the-eu-and-implications-for->

northeast-asia/ (consulted 9.12.2017)

- “The story that never ends. A new stage in the energy dispute between Russia and Belarus”, OSW, May 2017. Available at: <https://www.osw.waw.pl/en/publikacje/osw-commentary/2017-05-17/story-never-ends-a-new-stage-energy-dispute-between-russia-and> (consulted 9.12.2017)
- Toghiani T., Motesano F., Kozak I., “From completion to Compatibility Striking a Eurasian balance in EU-Russia relation”, Clingendael, October 2015. Available at: <https://www.clingendael.org/publication/competition-compatibility-striking-eurasian-balance> (consulted 9.12.2017)
- Wolczuk K., Dragneva R., “The Eurasian Economic Union: Deals, Rules and the Exercise of Power”, Chatham house, 2017. Available at: <https://www.chathamhouse.org/publication/eurasian-economic-union-deals-rules-and-exercise-power> (consulted 9.12.2017)
- Vinikurov E., “The EAEU and the EU”, Regnum, September 2016. Available at: <https://regnum.ru/news/2173129.html> (consulted 9.12.2017)
- Белокопытов А., “Энергетическое сотрудничество государств ЕАЭС: предпосылки, тенденции, перспективы” (A. Belokopytov “Energy cooperation of the EAEU Member States: tendencies and perspectives”) Available at: [https://www.imemo.ru/files/File/ru/conf/2016/29042016/01\\_06\\_Belokopytov.pdf](https://www.imemo.ru/files/File/ru/conf/2016/29042016/01_06_Belokopytov.pdf) (consulted 9.12.2017)
- Валовая Т., «Мы очень хорошо друг друга дополняем» ( T.Valovaya, “We complement each other quite well”). Available at: <http://eurasian-studies.org/archives/3564> (consulted 9.12.2017)
- Владимир Путин рассказал о перспективах сотрудничества России и Европы” (“V. Putin on Russia and Europe cooperation perspectives”), Rossiskay Gazeta, October 2011. Available at: <https://rg.ru/2010/11/26/putin.html> (consulted 9.12.2017)
- Кнобель А., “Евразийский экономический союз: перспективы развития и возможные препятствия”, Вопросы экономики, 2015 № pp.87-108 (A. Knobel “Eurasian economic union: perspectives and problems”, Voprosy ekonomiki 2015 № pp.87-108). Available at: [https://iep.ru/files/text/nauchnie\\_jurnali/knobel\\_vopreco\\_3-2015.pdf](https://iep.ru/files/text/nauchnie_jurnali/knobel_vopreco_3-2015.pdf) (consulted 9.12.2017)
- Кнобель А., “Цена Союза”, Vedomosti, 13 January 2014. Available at: <https://www.vedomosti.ru/newspaper/articles/2014/01/13/cena-tamozhennogo-soyuza> (consulted 9.12.2017)
- Путин В., «Новый интеграционный проект для Евразии — будущее, которое рождается сегодня» (V.Putin, «The new integration project for Eurasia – the future is being born today»). Available at: <https://iz.ru/news/502761> (consulted 9.12.2017)

- Шенец Л., “Создание общих рынков энергетических ресурсов как главный фактор повышения энергетической безопасности Евразийского экономического союза” (А. Shenec, “The creation of common energy markets as the main factor of energy security of the EAEU”), September 2017, Astana.
- “Кризис и налоговый маневр как испытание для ЕАЭС” (“Crisis and tax reform as as a test for the EAEU”). Available at: <https://www.vedomosti.ru/newspaper/articles/2015/02/17/integratsiya-ispitanie-eaes#/galleries/140737492096660/fullscreen/1> (consulted 9.12.2017)

# Energy Charter Secretariat 2018



**Energy Charter Secretariat**  
Boulevard de la Woluwe, 46  
B-1200 Brussels, Belgium

Mail: [info@encharter.org](mailto:info@encharter.org)  
Web: [www.energycharter.org](http://www.energycharter.org)  
Phone: +32 2 775 98 00  
Fax: +32 2 775 98 01