

## POLICY PAPER

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# Enhancing Energy Security of the EU and Ukraine: Common Responsibility

*Ukraine has been actively involved in the process of integration to the European Union in the energy sector, based on the EU-UA Association Agreement, as well as on the Energy Community Treaty. This legal basis obliges the parties - Ukraine and the EU - to adhere to certain rules and mechanisms of interaction, in particular in the gas sector. The Nord Stream 2 project threatens not only compliance with these rules but also the energy security of the parties, which forces Ukraine and the EU to look for ways to enhance interaction with the use of existing instruments.<sup>1</sup>*

### Introduction

The EU-Ukraine Association Agreement, the Treaty establishing Energy Community and other documents provide the legal framework for deepening cooperation between Ukraine and the EU in the energy sphere, including the gas infrastructure sector. Incorporation of the EU energy legislation to the legislation of Ukraine and adaptation of the regulatory framework of Ukraine to the EU norms creates de jure a single regulatory space that allows Ukraine to be considered as part of the EU + Ukraine common gas market. So, while complying with the EU gas directives, Ukraine also integrates into the EU internal gas market and becomes its important part.

The obligations and rights, defined in the EU gas directives and regulations, extend to both the EU member states and Ukraine. The EU common rules shape the regional cooperation in a spirit of mutual assistance to promote security of supply (SoS), support a sense of solidarity between states, especially in the case of a crisis of natural gas supply. The uncertainty around the future use of the Ukrainian GTS, the plans to import gas by the EU countries through routes that do not take into account the existing infrastructure facilities are all factors to influence security, significant socio-economic and political impact, which also threaten the security of gas supplies to Ukraine and farther to the EU, possible increase of gas tariffs and development of the EU-Ukraine gas cooperation.

Such a situation and the current trends in the gas sector, followed by the simultaneous increase of gas prices for consumers, affect the level of confidence of Ukrainian citizens to the European integration process in the energy dimension that may become a negative factor for the EU-Ukraine relations and the internal situation. At the same time, the Association Agreement and the priorities of the Eastern

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<sup>1</sup> Prepared on the results of the international round table «Strengthening Energy Security of Ukraine and the EU through Coordination and Common Actions Based on the Association Agreement» (22 November 2018, Kyiv, Ukraine).

Partnership contain new opportunities and mechanisms of gas cooperation that allow to coordinate plans, take into account mutual interests and take joint measures in the case of emergency or a crisis.

Therefore, on the one hand, in the gas sector of the EU-Ukraine cooperation, there is still a room for improvement and unmet commitments defined by the Association Agreement and the Energy Community Treaty, while, on the other hand, the parties need to deepen integration, cooperation and coordination of actions, first of all, in the gas sector. The society also needs explanations that the implementation of the EU gas regulatory acts gives Ukraine an opportunity to take advantage, as well as economic and security benefits of integration into the single European gas market, in particular, in taking decisions on the future of the Ukrainian gas transmission system and gas supplies to Ukrainian consumers. These important issues were discussed by the participants of the international round table "Strengthening Energy Security of Ukraine and the EU through Coordination and Common Actions Based on the Association Agreement" (22.11.2018, Kyiv)<sup>2</sup>, organized by the Centre for Global Studies Strategy XXI and the Konrad Adenauer Stiftung Office in Ukraine.

### Energy security of Ukraine and the EU: Key outcomes of the discussion

Strengthening energy security of Ukraine and the EU through coordination and common actions based on the Association Agreement is a multidimensional problem that thus requires an integrated approach, taking into account the implementation of the Association Agreement in the energy sphere by all parties, the legal framework and existing mechanisms for deepening the EU-Ukraine gas cooperation, including on the use of gas infrastructure, the current uncertainty about the future use of the Ukrainian GTS, plans for importing gas by the EU countries through the new pipelines that do not take into account the existing infrastructure capabilities were the subjects of the discussion within the round table.

At the discussion, there were two main directions: Ukraine's homework, which should be done for its own energy security, and the work which the European Union should do for its member states and Ukraine. Certainly, these issues were discussed in the light of threats generated by the Russian Federation. In this context, **Vitalii Martyniuk**, moderator of the round table, Head of the International Programs of the Centre for Global Studies Strategy XXI, reminded the provisions of Article 337 of the Association Agreement: *"The Parties agree to continue and intensify their current cooperation on energy matters for the enhancement of energy security."*

**Gabriele Baumann**, Head of the Konrad Adenauer Stiftung Office in Ukraine, drew attention to the importance of building Ukraine's relations with the EU in the context of the future transit and developing a clear vision of further cooperation with the European Energy Union. Establishment of the Energy Union is one of the main tasks for Vice-President of the European Commission Maroš Šefčovič. For the reason, President of the Centre for Global Studies Strategy XXI **Mykhailo Gonchar** mentioned Šefčovič's program speech made at the XII Central European Energy Conference on November 19, 2018 in Bratislava, in which he stressed the need to preserve the transit of gas through the Ukrainian GTS. At the same time, according to M. Gonchar, the EU is unlikely to provide such guarantees, and the price of Russia's "guarantees" is well known. At the same time, step by step the term of "energy security" disappears from the official documents of the European Union.

According to assessments of Acting Chairperson of the Verkhovna Rada of Ukraine Committee on Fuel and Energy Complex, Nuclear Policy and Nuclear Safety **Oleksandr Dombrovskyi**, energy security will be achieved if Ukraine becomes self-sufficient in energy resources, as today Ukraine has a surplus in electricity but a deficit in gas. He called energy efficiency the key issue for Ukraine's energy security that should lead to reduction of domestic energy consumption. In the gas sector, problems of energy security in Ukraine should be considered in two dimensions: external dimension - prospects of bypass gas pipelines and their impact on Ukraine; internal dimension - the mechanism of functioning of the Ukrainian gas transmission system in these conditions. As for the last one, Ukraine must complete the process of unbundling and find a reliable western partner to operate its GTS. O. Dombrovskyi noted that inside the EU there is a deep political conflict between the creation of the

<sup>2</sup> <https://geostrategy.org.ua/en/component/k2/item/1531-energetichna-bezpeka-ukrayini-ta-es-mozhliva-u-tisniy-spivpratsi-%E2%80%93-pidsumki-diskusiyi>

Energy Union and the implementation of the Nord Stream 2 project, and the consequences of this conflict influence Ukraine.

**Wolfgang Bindseil**, Deputy Head of the German Embassy in Ukraine, said that the state of Ukraine's energy security is now better than ever before, as the country began to consume less gas and carry out reforms in accordance with the Association Agreement. Meanwhile, according to his words, the process of unbundling should be completed as soon as possible, as it is a precondition for talks with western partners on the further reliable transit of gas through the Ukrainian territory. Without rejecting the political component of the Nord Stream 2 project from Russia's point of view, as Mr. Bindseil noted, it is a commercial project for the European companies and another route of supplying gas for Germany. Therefore, according to him, the Nord Stream 2 gas pipeline will be built, and Ukraine needs to create conditions for attracting western investments into its GTS and find powerful western partners to counter challenges from the side of the Russian Federation.

At the same time, **Karel Hirman**, Member of the Strategic Advisory Group for Support of Ukrainian Reform, adviser on energy issues of the Slovak Prime-Minister (2010-2012), called the Nord Stream 2 and the TurkStream as Kremlin's geopolitical projects, which, meanwhile, have a certain economic component for Gazprom and the European energy companies, involved in the project, but Nord Stream 2 is a threat to German trading companies. According to assessments of the Slovak expert, to negotiate the further gas transit through the Ukrainian territory, the European Union wants to receive from Ukraine a single vision of the future transit and to understand who will be an operator of the Ukrainian GTS.

From his side, the key reporter at the event **Igor Stukalenko**, Director on Energy Programs of the Centre for Global Studies Strategy XXI, said that the Nord Stream 2 project undermines the principles of the European gas market and, along with other factors and the blockade of Central Asian gas, reduces security of supply (SoS) and threatens the physical shut-down of gas transit through the Ukrainian territory to the EU, creating a danger of an "emergency situation" in the definitions of the Association Agreement.<sup>3</sup> Therefore, the active application of the provisions of the Agreement, which determines direct bilateral relations in the gas infrastructure sphere, available tools, in particular the initiation of direct consultations, and the consideration of Ukraine's interests in the system of security of supply and long-term plans of the EU, is a way of counteracting threats to energy security. He concluded that the Association Agreement and the adoption of the EU gas legislation transform Ukraine into a part of the EU market that should give it the same rights in the gas sector, which the EU member states have.

Advisor of the European Network of Transmission System Operators for Gas **Anton Kolisnyk** said that PJSC Ukrtransgaz is already involved into functioning of the European gas market and uses possibilities, which ENTSOG provides to the Ukrainian gas transport operator.<sup>4</sup>

Undoubtedly, the unbundling process in the gas sector of Ukraine should be completed as soon as possible. Nevertheless, as stressed Deputy Head of the Legal Department at NJSC Naftogaz of Ukraine **Yelyzaveta Badanova**, the transit contract with Gazprom, which is valid until the end of 2019, does not allow to complete the unbundling process in Ukraine. That is why Naftogaz of Ukraine tries to get consent from the Russian supplier to change the Ukrainian party of the contract, but Gazprom refuses to transfer the contract to a new system operator. Under such conditions, in her opinion, the process of unbundling cannot be completed by the end of 2019, although the necessary preparatory work is carried out.

The Nord Stream 2, as assessed **Oleksii Khabatiuk**, Head of the Energy efficiency department at NJSC Naftogaz of Ukraine, is a "Trojan horse" for the EU that undermines the basics of functioning of the European Union, because the project is aimed mostly against the EU than Ukraine but opens a window for the Kremlin for further offence actions against Ukraine. The representative of Naftogaz stressed that, in order to strengthen its own energy security, Ukraine should use internal reserves to reduce consumption, streamline the system of payment for gas, modernize the Ukrainian GTS, reform the subsidy system with the aim to re-direct it at stimulating energy saving.

<sup>3</sup> [https://geostrategy.org.ua/images/WS\\_22\\_Nov\\_SIO\\_Read\\_PDF.pdf](https://geostrategy.org.ua/images/WS_22_Nov_SIO_Read_PDF.pdf)

<sup>4</sup> <https://geostrategy.org.ua/images/2.pdf>

According to possible scenarios of the gas transit through Ukraine after 2020 in the context of implementation of the Nord Stream 2 and TurkStream projects<sup>5</sup>, presented by expert on energy issues of the Ukrainian Center for European Policy **Dmytro Naumenko**, the transit of Russian gas through the Ukrainian GTS will be preserved, but the question is what will be the amounts of this transit. He also noted that the voice of Germany had become increasingly important in the EU energy sector, and underlined that all the costs of the Nord Stream 2 project would ultimately be paid by German and other European consumers.

While defining its actions to ensure its own energy security, Ukraine must take into account the position of the EU, but steadfastly defend its own interests. Even if the Nord Stream 2 becomes a reality, as Mykhailo Gonchar summarized, this does not mean that Ukraine must stop opposing it. Ukraine needs to be prepared not for the scenario, when the unknown quantities in the scenario of the next gas crisis will be more numerous than the known ones.

### **Factors that influence security and the EU-Ukraine cooperation in the gas sector**

Energy security of Ukraine and the European Union are interdependent. There are a number of factors<sup>6</sup>, which affect the security of gas supplies both to Ukraine and the EU, in particular:

- Gazprom's Nord Stream 2 and TurkStream projects are being implemented at a rapid pace as well as related infrastructure projects that destroy the pillars of the European gas market;
- Contract uncertainty regarding the gas transit through the GTS of Ukraine to the EU. The transit contract with Gazprom ends at 10.00 a.m. on January 1, 2020;
- Reluctance of Gazprom to work according to the European law;
- Blockage of gas transit from Central Asia through the territory of the Russian Federation.

These factors give rise to a high probability of a complete disruption of gas transportation through Ukraine to the EU. The situation requires urgent coordinated action to strengthen Ukraine's and the EU's energy security. This is recognized in Ukraine, but remains without due attention in Brussels. The Association Agreement (AA)<sup>7</sup> contains provisions that allow coordinating joint actions, in particular regarding gas infrastructure, which is important for counteraction to the Nord Stream 2 project. However, the joint implementation of the objectives of the AA by Ukraine and the European Union has now become a one-way reporting process. The latest European Commission report looks like an act of verification by one side (the EU) of the other side (Ukraine), where there are no proposals and decisions on overwhelming gas issues. This also applies to the draft report of the European Parliament. However, the Committee on Foreign Affairs (AFET) of the European Parliament has amended the text: "Reiterates the crucial role of Ukraine in the European energy supply network; condemns the construction of the Nord Stream 2 pipeline, as it is a political project that poses a threat to European energy security and the efforts to diversify energy supply; calls for the project to be cancelled".<sup>8</sup>

In Ukraine and in the EU, awareness is growing concerning elimination of threats to common energy security (recent appeals from MEPs<sup>9</sup>, members of the Ukrainian Parliament<sup>10</sup>, Ukrainian civil society organizations<sup>11</sup>), but common decisions are needed to strengthen coordination and take into account interests in the gas sector to eliminate existing threats. Naftogaz proposed *«in coordination with*

<sup>5</sup> <https://geostrategy.org.ua/images/3.pdf>

<sup>6</sup> Prepared based on the report of Igor Stukalenko, Head of Energy Programs of the Centre for Global Studies Strategy XXI for international round table "Strengthening Energy Security of Ukraine and the EU through Coordination and Common Actions Based on the Association Agreement" (November 22, 2018, Kyiv).

<sup>7</sup> <https://www.kmu.gov.ua/ua/diyalnist/ievropejska-integraciya/ugoda-pro-asociacyu>

<sup>8</sup> <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P8-TA-2018-0518+0+DOC+XML+V0//EN&language=EN>

<sup>9</sup> <https://reinhardbuetikofer.eu/2018/11/06/gemeinsamer-offener-brief-zu-nord-stream-2/>

<sup>10</sup> [https://www.facebook.com/story.php?story\\_fbid=1015691963822244&id=590012243](https://www.facebook.com/story.php?story_fbid=1015691963822244&id=590012243)

<sup>11</sup> <https://geostrategy.org.ua/ua/analitika/item/1485-vidkritiy-list-pivnichniy-potik-2-rosiyskiy-troyanskiy-kin-proti-evropeyskoyi-bezpeki>

*Ukraine's international partners, to develop an Action Plan in the case of complete interruption of transit of natural gas through the territory of Ukraine to the EU after 2019».*

The EU-Ukraine Association Agreement provides a solid legal basis and direct bilateral relations to deepen cooperation in the field of gas infrastructure. This is important for the rapid resolution of strategic and urgent gas issues. In particular, Articles 274 and 338 of the AA oblige the Parties:

- to coordinate their actions on infrastructure developments;
- to cooperate on matters related to trade of natural gas, sustainability and security of supply;
- to act with a view to further integrate markets;
- to initiate consultations on important issues to elaborate joint decisions (for instance, to initiate consultations on realization of the Nord Stream 2 project);
- to take into account the energy networks and capacities of the other Party when developing policy documents and infrastructure development plans;
- to cooperate in the sphere of modernization and enhancement of existing infrastructure, creation of new infrastructure of common interest;
- to cooperate while installing of cross-border metering systems on external borders, as well as while implementing energy strategies and policies and in development/elaboration of forecasts and scenarios, based on timely exchange of information on energy balances and energy flows.

At present, these opportunities are not being used properly. For example, without consulting with Ukraine, it was decided to grant Gazprom access to the OPAL pipeline, which allows additional transportation of 7-10 billion cubic meters of gas annually bypassing the Ukrainian gas transmission system. There are also examples when additional infrastructure in the EU is planned without taking into account the capabilities of the GTS of Ukraine and its underground gas storages.

The European gas market is being implemented since 1998 with the aim to promote security of supply (SoS). Its legal basis consists of: Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas<sup>12</sup>; Regulation (EC) No 715/2009 of the European Parliament and of the Council of 13 July 2009 on conditions for access to the natural gas transmission networks<sup>13</sup>; Regulation (EC) No 713/2009 of the European Parliament and of the Council of 13 July 2009 establishing an Agency for the Cooperation of Energy Regulators<sup>14</sup>; Regulation (EU) 2017/1938 of the European Parliament and of the Council of 25 October 2017 concerning measures to safeguard the security of gas supply<sup>15</sup>; package of documents on establishment of the EU Energy Union 2015. Ukraine implements European legislation envisaged by the AA and the Treaty establishing the Energy Community<sup>16</sup>.

The Directive 2009/73/EC (Article 6) defines the common rules for the EU to establish the framework for cooperation in order to promote solidarity and safeguard security of supply, in particular in the case of energy supply crisis. Such cooperation should cover situations that have led or may lead to the disruption of gas supplies, including the coordination of emergency measures, the definition and development (construction, modernization) of infrastructure connections and the practical aspects of mutual assistance. The Directive 2009/73/EC (Article 36) also defines that the new gas infrastructure still in the planning period should be analyzed from the point of view of market effects and consequences for concurrence and security of supply. It is emphasized that where the infrastructure in question is located in the territory of more than one Member State, such plans should be considered by the EU agencies in order to better evaluate cross-border consequences.

With the special Regulation №2017/1938 concerning security of supply, the EU has strengthened security of supplies after the use of “energy weapon” by Russia in 2006 and 2009 and its hybrid warfare against Ukraine, that was unleashed in 2013-2014. By these means, a three-level system of

<sup>12</sup> <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:211:0094:0136:en:PDF>

<sup>13</sup> <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:211:0036:0054:en:PDF>

<sup>14</sup> <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:211:0001:0014:EN:PDF>

<sup>15</sup> <https://eur-lex.europa.eu/eli/reg/2017/1938/oj>

<sup>16</sup> <https://www.energy-community.org/legal/treaty.html>

reliability was developed, and the principle of solidarity was introduced for the first time. The participants of the system should help their neighbors in the case of gas crisis. The Regulation defines a role of ENTSOG in conduction of the whole-system modeling of gas supply and preparation of scenarios in the case of its interruption.

The Nord Stream 2 and the second line of the TurkStream are the projects that have transboundary effects for a number of the EU countries - Poland, Slovakia, Hungary, Italy, Romania, as well as the countries of the Energy Community - Ukraine and Moldova. The development of the European gas network should be effectuated within the Ten-Year Network Development Plan (TYNDP) envisaged by ENTSOG that includes: integrated network modeling; network development scenarios; European supply adequacy forecast and system stability assessment.

Consequently, the implementation of the European rules should ensure that the interests of the parties are considered, including the interests of Ukraine, which implements the European legislation and should be regarded as part of the EU gas market. Implementation of the EU gas legislation should strengthen coordination of actions and plans and mutual consideration of Ukraine and the EU.

In order to prevent and respond to emergencies or threats to them, the AA contains the Early Warning Mechanism (EWM), which, like Regulation No 2017/1938, provides for an early assessment of potential risks and includes the definition of an emergency situation: "Emergency situation is a situation causing a significant disruption / physical interruption of supply of natural gas between Ukraine and the European Union." The mechanism was already tested on March 1, 2018, when Ukraine sent the EU a note on the application of EWM in response to the threat of an emergency situation caused by Gazprom by violating its contractual obligations and refusing to comply with the decision of the Stockholm Arbitration. Russia, like in 2006 and 2009, proved to be an unreliable supplier. This time, a clear procedure prescribed by the Association Agreement was introduced that did not allow the emergency to develop into a crisis.

The full implementation of the Nord Stream 2 project may result in the disruption of Russian gas transportation through the Ukrainian GTS, and thus the disruption of gas supplies via Ukraine to the EU, that could lead to the state of emergency. In this case, the procedure provided by the Early Warning Mechanism of the AA may be applied.

Provided by the AA tools allow to resolve disputes between Ukraine and the EU, including those concerning the Nord Stream 2. For example, the Association Council: "...empowered to take decisions which are binding on the parts...". The Association Council, in particular allows:

- to initiate consultations with the EU on the threats to security of gas supplies to the EU and Ukraine (including those created by the Nord Stream 2);
- to intensify work on these issues of all institutional bodies, including the Association Committee, the EU-Ukraine Parliamentary Association Committee, the Civil Society Platform;
- to consider the need for the establishment of the Committee on Gas Industry and Network to strengthen coordination of plans and actions in the gas sector; consider the threat of an emergency situation created by the Nord Stream 2 (as defined in paragraph 2 of Annex XXVI).

Thus, after Ukraine's accession to the Energy Community and the signing of the Association Agreement with the European Union, Ukraine has begun the process of integration into the EU in the energy sector, including integration into a single European gas market. At the same time, the Association Agreement provides for a number of mechanisms and tools that need to be used to prevent the implementation of gas infrastructure projects that harm one of the AA parties. The Nord Stream 2 project became the "litmus test" of the effectiveness of the Energy Community and the full bilateral implementation of the Association Agreement, and its continued implementation undermines the foundations of the association, the creation of the European Energy Union and the functioning of the European gas market.



## **Recommendations for improving cooperation between Ukraine and the EU in the gas sector:**

1. The issue of energy security in the EU should be considered only in conjunction with Ukraine's energy security. The EU should treat Ukraine as an integral part of the European gas market and determine the mechanism for Ukraine's involvement in the functioning of the Energy Union.
2. The Parties should initiate creation of the ad hoc gas committee within the framework of the Association Agreement to strengthen the coordination of the plans and actions of Ukraine and the EU in the gas sector.
3. Ukraine and the EU should make a clear choice how to work with a monopoly gas supplier from the territory of Russia and confirm that they will deal with Gazprom only in accordance with the rules and respect to the EU gas law. A truly reliable and secure European gas market will be created through coordinated actions, taking into account mutual interests, effective use of the existing Ukrainian gas infrastructure to provide services for the transportation of gas to the European gas companies.
4. Consider the situation regarding the implementation of the Nord Stream 2 project as a threat of an emergency situation, as defined in Appendix XXVI (p.2) of the Association Agreement.
5. Extend the provisions of the Third Energy Package to offshore pipelines heading to the European Union.
6. Ukraine and the EU should discuss the least risky scenario for using the Ukrainian GTS to ensure a long-term reliable supply of Russian gas to consumers in the European Union.
7. In their new contracts with Gazprom, European companies must provide a point for the transfer of Russian gas on the eastern border of Ukraine, and Naftogaz of Ukraine should carry out its work on the technical provision of such a transfer, which will reduce the possibility of Russia using gas as the hybrid war weapon and increase the transparency of supply.
8. Envision the completion of the process of unbundling in the gas sector of Ukraine by the year 2020 in order not to violate current contracts for the supply and transit of gas between Naftogaz and Gazprom, while simultaneously creating the preconditions for attracting European partners and investments in the development and effective use of the Ukrainian GTS.
9. To develop practical possibilities for restoring the supply of natural gas from the Central Asian countries through the Ukrainian gas transportation system to consumers in the European Union, convincing Russia to stop blocking these gas supplies through its territory.
10. The EU should include energy in the scope of the regulatory approximation, as defined by Annex XVI of the Association Agreement.

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