

Energy Dialogue EU - Russia

# The Tenth Progress Report



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Cooperation between Russia and the European Union in the field of energy is aimed at ensuring security of energy supply and solving the tasks provided by the Road Map of the Russian-European Common Economic Space. The Road Map focuses on maintaining sustainable, reliable and continuous energy production, distribution, transportation and utilization and includes energy efficiency, energy saving, as well as renewable and the utilisation of alternative energy sources. The EU-Russia Energy Dialogue highlights one of the major areas of cooperation between Russia and the European Union and serves as the principal instrument to attain these objectives.

During the nine years of the existence of the Energy Dialogue, since October 2000, a lot has been achieved to enhance the cooperation in the energy sector between Russia and the member states of the European Union.

Within the framework of the Energy Dialogue a mechanism of consultations between the state institutions and businesses has been established in the form of Thematic Groups on the essential issues of the European Union's and Russia's Energy Policy. The following Thematic Groups have been established and currently operate:

- Energy Strategies, Forecasts and Scenarios;
- Energy Markets Development;
- Energy Efficiency.

The activities of the Thematic Groups focus on the following:

- comparative analysis of energy strategies and generation of development scenarios for the energy sector of Russia and the EU;
- research on energy markets development and progress of large-scale investment infrastructure project implementation;
- implementation of the EU – Russia Energy Efficiency Initiative aimed at increasing energy efficiency, primary energy savings and the use of renewable energy sources.

The EU – Russia Dialogue provides a forum for discussions, experience exchange and facilitation of cooperation projects, between experts nominated by the Member States and Russia, the European Industrialists Round Table, International Financial Institutions and the European Commission. The Thematic Groups operate as provided by the terms of reference and work plans approved or revised on an annual basis.

The priorities of the Energy Dialogue are discussed at the meetings of the EU-Russia Permanent Partnership Council (PPC) at the level of Ministers of Energy (in October 2005, December 2006, October 2008 and April 2009). Progress and the results are evaluated during regular meetings of the EU-Russia Energy Dialogue Coordinators (the Minister of Energy of the Russian Federation on the Russian side, and the Commissioner of the European Commission on Energy Issues on the European side).

## Introduction

The European Union and Russia have established a strategic partnership and conducted mutually beneficial cooperation in the energy sector. The European Union member states are the largest importers of energy resources from Russia. Russian gas and oil supplies provide for more than 25 percent of the overall consumption of energy resources in the EU member states, and there is a potential for its further increase.

The strategic partnership between the EU and Russia in the field of energy is aimed at ensuring long-term reliability, security and predictability. This partnership is an important component in the Parties' stable relations.

With regard to Russia's position as the major energy supplier for the EU, and the EU's position as Russia's largest consumer, the development of cooperation between the EU and Russia on issues related to ensuring reliability and security of energy supply and demand is of primary importance.

The Tenth Progress Report covers the results of activities of the three Thematic Groups operating within the framework of the EU-Russia Energy Dialogue for the period from November 2008 to November 2009. These activities have been performed in accordance with the terms of reference and work plans approved by the Coordinators of the EU-Russia Energy Dialogue.

The Report also covers the directions for further cooperation to enhance and advance the EU-Russia Energy Dialogue.

### 1. ENERGY STRATEGIES AND FORECASTS

The activities of the Thematic Group on energy strategies, forecasts and scenarios focus on the following:

- Exchange views and draw conclusions on the EU and Russian strategies, policies and forecasts in the energy field and bring adequate coherence in respective energy forecasts and scenarios by the year 2030;
- facilitating the development of the system of exchanging information and monitoring. This provides for increased transparency and mutual confidence in the energy field, timely determining potential mid- and long-term difficulties and analyzing them; joint efforts analyzing current issues of demand for energy sources and supply.

The Parties point out that the EU and Russia have generated mid- and long-term forecasts and development scenarios for the energy sector in the EU and Russia.

#### Forecasts and development scenarios for the Russian energy sector.

The basic document outlining guidelines for a long-term energy sector development strategy for Russia is the Russian Energy Strategy until 2030. The primary objective of the Energy Strategy until 2030 is to create an innovative and efficient energy sector in the country that would correspond both to the growing economy's demand for energy resources and to the foreign economic interests of Russia. The energy sector is also



expected to make a substantial contribution to the socially oriented innovative economic development of the country and its regions.

At the first stage of Energy Strategy implementation (2013-2015) Russia's fuel and energy sector is to facilitate early economic recovery.

The second stage (2020-2022) is defined by transition to innovative development and creation of a new economic infrastructure accompanied by increasing the energy efficiency of the economy and energy sector as well as by efficient implementation of innovative pilot and new capital-intensive energy projects in Eastern Siberia, the Far East, the Yamal Peninsula and sea shelf.

The third stage (until 2030) provides for further innovative economic development and application of conceptually new technological capabilities supported by the highly efficient usage of both traditional and non-hydrocarbon energy sources.

The fuel and energy balance forecast for Russia until 2030 involves: reducing the share of gas in the total primary fuel and energy resources consumption from 52% in 2005 to 46-47% by 2030; increasing the share of non-fuel energy sources in the total primary fuel and energy resources consumption from 11% to 13-14% by 2030; a large-scale decrease of energy intensity of the Russian economy and energy industry (by 2.1-2.3 times) accompanied by a limited increase of domestic consumption (by 1.4-1.6 times), export volume (by 1.1-1.2 times) and energy resource production (by 1.3-1.4 times).

It is expected that, at the first stage, the crude oil output in Russia will reach 486-495 mln tonnes, at the second stage, 505-525 mln tonnes and, at the third stage, 530-535 mln tonnes. Natural gas production is expected to reach 685-745 bcm, 803-837 bcm and 885-940 bcm respectively.

Until 2030 energy exports will continue to remain one of the most significant factors contributing to the economic development of Russia. At the same time their impact on national economy development will gradually decrease. This, in turn, will influence the export dynamics that is expected to slow down and stabilise by 2030.

#### Energy resources consumption forecasts by the member states until 2030.

The EU is one of the world's largest integrated energy markets and a major player on the world energy market, primarily as an energy importer. It imports around a quarter of the oil traded internationally, accounts for some 62% of international pipeline gas movements, some 21% of global LNG gas movements and some 28% of the hard coal imported from the world market.

The EU's domestic energy production covers less than half of its needs, with net imports accounting for 53.1% of energy consumption in 2007. Oil comprises the bulk of total net EU energy imports (60%) followed by imports of gas (26%) and solid fuels (16%). The proportion of imported electricity and renewable energy is negligible (less than 1%).

Net imports of crude oil into the European Union in 2007 amounted to 577.7 Mtoe (million tonnes of oil equivalent) and some 82% of the EU's consumption. Of this, 185 Mtoe (32.6%) was imported from Russia, 84.3 Mtoe (14.8%) from Norway, 55.5 Mtoe

(9.8%) from Libya and 39.5 Mtoe (6.9%) from Saudi Arabia. Other significant suppliers included Iran, Kazakhstan, Iraq and Nigeria.

Imports of petroleum products into the European Union in 2007 amounted to 287.4 Mtoe, while exports totaled 276.8 Mtoe, giving an overall net import balance of just under 11 Mtoe.

Net imports of natural gas into the European Union in 2007 amounted to 260.5 Mtoe, some 61% of the EU's consumption. Gas is mainly imported from four big suppliers: Russia 100.7 Mtoe (38.7%), Norway 65.8 Mtoe (25.3%), Algeria 41.8 Mtoe (16%) and Nigeria 12.6 Mtoe (4.9%), with further quantities from Libya, Qatar, Egypt and Oman. Around 87% of the gas imported into the EU arrives by pipeline, with the remainder LNG.

Imports of hard coal amounted to 156.8 Mtoe in 2007, some 47% of the EU's total consumption of solid fuels. Hard coal is sourced widely, with the largest sources of supply in 2007 being Russia 39.3 Mtoe (26.2%), South Africa 32.3 Mtoe (21.5%), Australia and Colombia 20.3 Mtoe each (13%) and the United States 14.6 Mtoe (9.7%)

#### Forecasts of Russian energy resources export to the EU countries until 2030.

According to existing scenarios, at the first stage, the total volume of crude oil exports from Russia would reach 243-244 mln tonnes, at the second stage, 240-252 mln tonnes and, at the third stage, 222-248 mln tonnes. The natural gas export volume would reach 270-294 bcm, 332-341 bcm and 349-368 bcm respectively.

The energy markets of the EU and CIS countries will remain Russia's major consumers until 2030. At the same time the EU's share is expected to decrease with regard to supply diversification and increase of Eastern exports to China, Japan, the Republic of Korea and the countries of the Asian-Pacific Region. By the end of the third stage, the share of Eastern supplies of liquid hydrocarbons (oil and oil products) would increase from the current 6% to 22-25% and of gas from 0 to 19-20%.

At the first stage, the forecasted volume of crude oil exports from Russia to Europe may equal 178-180 mln tonnes, at the second stage, 160-164 mln tonnes and, at the third stage, 122-138 mln tonnes. The natural gas export volume may reach 158-168 bcm, 189-194 bcm and 200-202 bcm respectively.

#### Activities of the sub-group on Energy Economics

The sub-group on energy economy was established under the Thematic Group on Energy Strategies, Forecasts and Scenarios in December 2008. In 2009, the sub-group held one coordination and two extended meetings.

The first extended meeting of the energy economy sub-group was held on 29 May 2009 in Brussels providing to the Russian side and to the independent experts detailed information on methods, instruments and model study of the energy industry development practiced in the EU. It also covered the activities of the International Energy Agency, Eurogas, and the University of Grenoble in the energy field. The National Technical University of Athens is currently implementing scenario evaluations for the European Commission and has already provided detailed information on energy model studies that are applied across the EU, including an overview of such models, as



PRIMES, PROMETHEUS, and GEM-E3. Besides, it informed the attendees of the existing scenarios and working results related to new scenario generation designed for post-recession development.

The second extended meeting of the energy economy sub-group was held on 21 July 2009 in Moscow. The presentation of the draft of the Russian Energy Strategy until 2030 was made at this meeting. In this regard, many issues were raised such as: developing model studies and instruments for generating energy industry scenarios in Russia; priorities and objectives set by the Energy Strategy until 2030; possible scenarios for post-recession development for the Russian energy industry; and strategy for the electrical energy industry of the country until 2030.

Based on the results of the meetings both sides agreed to continue exploring the issues raised at expert level in order to analyze the models that are being developed and results of simulation/modeling, in particular, with regard to consistency of the future energy resources export from Russia and energy import to the EU.

## 2. EU-RUSSIA ENERGY MARKETS DEVELOPMENT

Thematic Group on Energy Markets Development continues to conduct activities in accordance with the directions adopted when the group was created in 2007. Within the framework of the Thematic Group two subgroups continue to operate in the field of energy investment with industry representatives playing the leading role: in the field of infrastructure projects and energy resources trade.

The parties note that the implementation of projects in the field of energy in the European Union resulted in the improvement of the security of EU energy demand.

Russia remains the largest gas and oil exporter to the countries of the European Union. Natural gas is exported to the European countries primarily under long-term contracts.

In the area of electricity, the Russian Federation implements a formerly approved schedule of electrical energy and power markets' liberalization. Along-term power market model, which increases investor confidence and contributes to creating a solid basis for developing an electrical energy industry investment strategy, is being implemented.

The EU side believes that with the adoption of the 3<sup>rd</sup> Internal Energy Market Package ("Third Energy Package") the EU is consolidating its efforts towards achieving a fully effective market opening and a single European electricity and gas market. However, according to the assessment of the Russian side, the current situation is characterized by unfavourable investment climate for developments in the energy sector of the EU member states. In particular, the adoption of the Third Energy Package by the European Union significantly limits the activities of Russian fuel and energy companies in the EU market directly affecting their interests. The EU side does not share such assessment. It rather considers the Third Package which is fully in compliance with the Community's bilateral and international legal commitments to provide an attractive and stable regulatory framework also for Russian investments into the EU electricity and gas sector.

The sides assume that the Thematic Group could become an open platform for information exchange and discussion of this issue by all stakeholders, including representatives of the EU and Russian companies involved. The parties point out that diversification of both energy resources and transport infrastructure is an imperative of our time. In this framework, they support the development of electrical power trade between the European Union and Russia bearing in mind the necessity of guaranteeing the highest level of nuclear safety. According to the results of a large-scale joint Study of Prospective IPS/UPS-UCTE Interconnection that was recently conducted, in mid-term, linking the electrical systems' data by means of direct current connections appears most reasonable. Market developments on both sides should be further explored before deciding about the infrastructures which could support these developments. The EU side took note of the idea put forward by the Russian side to provide direct current connection the Kaliningrad region and Poland.

The Parties also support cooperation between Russian and European oil and gas companies in realization of a number of projects which will contribute to increase energy security of the EU and at the same time give security of the demand to Russia which is the EU largest oil and gas supplier.

Currently there are a number of infrastructure projects which are at various stages of implementation but all of them, by virtue of scale and importance, deserve the closest attention both of the European Union and Russia, including cooperation with transit countries in order to create stable conditions for the transit of energy resources. These include, in particular:

- development of the Shtokman gas deposit;
- construction of Burgas – Alexandroupolis oil pipeline;
- implementation of the joint natural gas transportation projects, including North Stream and others.

A meeting of the subgroup on energy infrastructures has been planned for January 2010 and will provide the ideal forum to understand the infrastructure policy on both sides and to enable a discussion on a list of concrete energy infrastructure projects of mutual interest.

The Parties emphasise the importance of a future agreement in the peaceful uses of nuclear energy.

The Parties agree that further work of the Thematic Group on energy markets development will focus on the following:

- further discussion and information exchange on two laws, the Federal law on Foreign Investment in Industries of Strategic Importance for State Defence and Security and the law regulating the key provisions for the EU's Third Energy Package implementation;
- evaluation of the impacts of new energy regulations on the EU and Russian markets;
- evaluation of cooperation with foreign investors both in the EU and Russia;
- information on regional energy markets development in Europe and perspectives of creating a common electricity market in the EU and CIS countries;



- joint seminars and conferences on the future development of EU-Russia cooperation in the field of electrical energy;
- evaluation of the impact of the financial crisis on the EU's and Russia's energy market development and infrastructure project implementation;
- discussing proposals on updating the list of priority infrastructure projects of mutual interest.

The EU-Russia cooperation in the area of energy policy will contribute to stability and predictability of world prices on energy resources in the future.

### 3. ENERGY EFFICIENCY AND RENEWABLE ENERGY

Improving energy efficiency in all sectors of economy and increasing the share of renewable energy resources (RES) has been one of the main priority areas of EU – Russia Energy Cooperation since the beginning of the Energy Dialogue.

Efficient use of energy and increased use of renewable energy sources contribute to economic growth, availability of affordable energy also in remote areas and environmental sustainability in the EU and in Russia.

In 2008 and 2009 Russia and the European Union continued and intensified their efforts in further developing legislative, regulatory, institutional and financial frameworks in order to put into practice the large potential of energy efficiency, energy savings and renewable energy, identified by the EU and Russia in their strategy documents.

The work of the Thematic Group supports these efforts. It provides an excellent forum for exchange of information and of experience between energy experts, industries and business from the EU and Russia, and international financial institutions.

The Parties recognise that thanks to the work of the Thematic Group there is constant information sharing and exchange of experience in the areas covered by the EU – Russia Energy Efficiency Initiative.

The preparation and implementation of joint projects are an expression of the desire to continue and enhance practical cooperation.

The Work of the Thematic Group was carried out in accordance with the objectives of the Energy Efficiency Initiative set in 2006, and in priority areas agreed upon by Parties in 2008. The following activities were implemented in accordance with a biannual Work Programme of the Thematic Group in the period from November 2008 to November 2009:

Two Meetings of the Thematic Group took place, one in Moscow on 5 December 2008, and the other on 29 July 2009 in Brussels. Particular focus was given to the following topics of common interest:

- development of policy and strategy documents, legislation and regulations on Energy Efficiency and Renewable Energy in the European Union and the Russian Federation;
- different support mechanisms and different formats for international cooperation for promotion of Energy Efficiency and Renewable Energy (IPEEC, GGFR, IRENA, Covenant of Mayors etc.);



- state of play of the implementation of joint projects and of the development of new projects of common interest.

Two Thematic Seminars were organised as a follow up to the discussions and to the exchange of information in the Meetings of the Thematic Groups. A seminar on renewable energy certification in the EU and in Russia was organised in cooperation with the joint EU – Russia project team on renewable energy on 4 October 2008 in Moscow. A seminar on best practice sharing on Energy Service Companies (ESCO's) took place on 4 December 2008 in Moscow.

Three joint EU – Russia cooperation projects on renewable energy, energy efficiency investments and energy efficiency management are currently being implemented.

Three Northern Dimension Environment Partnership projects on rehabilitation of district heating in Kaliningrad, Murmansk and Novgorod have been approved with the cooperation and financial support of the EU and Russia, the EBRD and the Nordic Investment Bank.

In 2008 the Parties stressed the importance of setting new priorities for the Energy Efficiency Initiative. To meet this objective, two concrete actions were implemented to promote closer economic cooperation between EU and Russian industry and business and further development of EU and Russia cooperation of the EU and Russia in international fora of cooperation on energy efficiency:

- A conference on "Realizing Russia's Energy Saving Potential, Enhancing the Energy Efficiency of the Russian Economy" took place at the margins of the International Forum for Innovative technologies, concepts and projects EMBIZ2009 on 10 – 12 November 2009, in Moscow;
- In May 2009 an agreement on setting up the International Partnership for Energy Efficiency Cooperation (IPEEC) was reached in framework of the G8. China, the Republic of Korea, Brazil, Mexico and India also became members of the Partnership. The Commission participates as an observer. The membership of the European Community is under consideration. It provides a platform for discussion, consultation and exchange of information. The Parties note the active development of the dialogue on energy efficiency issues between Russia and the Member States of the European Union. The Parties recognise the importance of facilitating practical partnership between the different stakeholders in the EU and in Russia. In 2010, particular attention should be paid to summarising the information about all existing frameworks of the EU – Russia energy efficiency and renewable energy cooperation.

The Parties note that EU-Russia cooperation in the area of legislation, regulations and institution building, cooperation between regions, the development and implementation of joint projects in the area of energy efficiency, use of renewable energy and energetic use of associated petrol gas will remain the main priorities in 2009 and 2010.

Cooperation in the following areas should be further developed in 2010:

- international cooperation in specific areas of common interest to Russia and the EU on energy efficiency, primary energy savings and renewable energy (energy efficiency in the buildings sector, improving methods for measuring and verifying energy efficiency improvements and an assessing energy efficiency mechanisms, cooperation on networking between the cities and regions, gas flaring reduction etc.);

- Reduction of greenhouse gas emissions in the energy sector;
- Efficient and Clean Coal Technologies;
- strengthening the cooperation with other EU – Russia sectoral dialogues on cross-cutting issues;
- promotion of closer economic cooperation between EU and Russian industry and business on energy efficiency and renewable energy;
- improving accessibility of information on energy efficiency legislation, regulations and measures, as well as improving cooperation and networking between EU and Russian citizens and companies.

The Parties reiterate the importance of developing new joint projects in the areas of common interest.

#### 4. EARLY WARNING MECHANISM

The Parties note that questions on formalising and improving the Early Warning Mechanism are regularly discussed in the Thematic Groups on Energy Markets Development and on Energy Strategies, Forecasts and Scenarios of the EU-Russia Energy Dialogue. In this context the Thematic Group on Energy Markets Development works on a short-term analysis, and the Thematic Group on Energy Strategies, Forecasts and Scenarios examines mid- and long-term issues.

In accordance with the working plans of the Thematic Groups, a joint seminar of the two Groups took place in March 2009 on the improvement of the EWM. The members of Thematic Groups noted the importance of formalising and developing the EWM and discussed the possibility of increasing the efficiency of this mechanism.

The Parties examine the possibility of involving transit countries in the EWM to maintain the stability of the existing transportation systems.

The Parties note that with regard to the crisis with natural gas transit from the Russian Federation to the European Union took place at the beginning of January 2009 they highly appreciate the signing of Technical Terms for Monitoring the Supply of Natural Gas through Ukraine on 10 January 2009 by the Russian party, European Commission and the Ukrainian side. The implementation of the monitoring mechanism enabled resuming supply in that direction.

The Parties highly appreciate the Memorandum on an Early Warning Mechanism in the Energy Sector signed by the Coordinators on 16 November 2009 within the framework of the EU-Russia Energy Dialogue.

#### 5. INTERNATIONAL LEGAL BASE FOR COOPERATION BETWEEN THE EU AND RUSSIA

##### New EU-Russia Agreement.

The Parties note the continuation of discussions on a New Agreement between the European Union and Russia, intended to replace the existing Partnership and Cooperation Agreement. Energy, as a strategically important issue of cooperation



between the European Union and Russia will be one of the most substantive elements of this agreement.

The Parties note the necessity to reflect in the energy chapter of the New Agreement the principles on energy security agreed at in the G8 Summit in St. Petersburg in 2006, as well as issues relating to energy efficiency and the reliability of demand, supply and transit.

#### Improvement of international legal instruments for energy cooperation and trade

The Parties reaffirm their interest in strong legal frameworks addressing energy trade and investment.

The Parties note that at the present time the demand increases for real operational mechanisms providing global and regional energy security. In particular, a legally binding international mechanism for dealing with emergencies in the field of energy does not exist.

The parties note that long-term international cooperation is possible only on the condition of fair risk sharing between all participants of the energy chain: suppliers, transit countries and consumers of energy.

In order to develop the principles of global energy security, established in the framework of the St. Petersburg Summit in 2006, Russia has proposed a Conceptual approach to a new legal base for international cooperation in the field of energy. This base foresees the creation of a multilateral legally-binding document that covers all aspects of global energy interaction.

The proposed Conceptual Approach contains several important principles that the EU subscribes to, notably non-discrimination and transparency as long as it does not undermine existing international agreements in the field of energy. The Parties envisage looking at how best to consider the ideas proposed in existing multilateral and bilateral contexts. In particular, these include the ongoing review of the Energy Charter Treaty; bilateral and multilateral negotiations such as the ongoing negotiations for the new EU-Russia Agreement, and other bilateral negotiations with third countries; as well as negotiations on possible specialised agreements on nuclear issues, such as the envisaged agreement on cooperation in the peaceful uses of nuclear energy.

#### CONCLUSIONS

The parties note that the Energy Dialogue continues to be an effective means of building confidence and increasing transparency in this field which is highly important for Russia's and EU's economy.

The Parties highly appreciate the results that have been obtained in the nine years of the existence of the Energy Dialogue.

The Parties note the important and fruitful work of the three Thematic Groups on Energy Strategies, Forecasts and Scenarios, on Energy Markets Development and on Energy Efficiency. These Groups have made a specific contribution to the further

development of energy cooperation between the European Union and Russia in the last years.

The Parties note progress in realising infrastructure projects and have the intention to continue the work on updating the list of projects of common interest.

The Parties consider that it is useful in the longer term to aim at ensuring a security of supply and demand of Russian hydrocarbons in the EU market under normal market conditions and take the necessary steps towards this end.

The Parties suggest that the Thematic Groups continue examining the development of energy markets, the comparative analysis of energy strategies, and the development of scenarios for the EU and Russian energy sector, as well as the implementation of joint initiatives for increasing the efficiency of energy use.

The parties stress the importance of a New Agreement including issues of energy cooperation between the European Union and Russia.

The Parties note the possibility to improve the international legal base in the field of energy. The Parties acknowledge that existing mechanisms for securing global and regional energy security should be further developed both for solving emergency situations and for their prevention.

The Conceptual approach to a new legal base for international cooperation in the field of energy proposed by the Russian side represents an important contribution in this respect.

The Parties consider that it is useful to continue the work of the three Thematic Groups, hold their meeting at least twice a year, and present reports of their meetings to the Coordinators of the EU-Russia Energy Dialogue and Permanent Partnership Council. Final reports of the Groups are to be presented in October 2010 and taken into account in the preparation of the Eleventh Progress Report.

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