THE EU INSTITUTIONAL CAPACITY IN SECURING ENERGY

This essay analyzes external energy policy as a product of institutional dynamics within the EU. The Commission treats energy purely as a commodity and chooses a market approach to shape energy policy. The Council could add the geopolitical dimension to EU external energy security but lacks unified backing from member states. While there are regions where the external market approach makes sense (e.g. Western Balkans), it is a tall order to expect this approach to address EU energy interests in the Caspian basin. One of the success stories in finding a proper mixture between the two approaches was active U.S. engagement in building the Baku-Tbilisi-Ceyhan (BTC) pipeline. The project's success has implications for European external energy policy-making, especially for projects in the Caspian region.

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Energy security is high on the agenda of decision-makers around the world. Global players have found themselves in an intense energy game for regional dominance. Decisions made today will have long-lasting implications for the future. Regional organizations, such as the EU, need to shape a common response for external energy in the name of its members. This article will question whether present EU Institutions and decision-making processes actually allow it to form and implement a credible external energy policy.

Energy security is a broad topic and touches upon various interconnected issues and policy areas.[1] It can be conceptualized as energy dependency on external sources. Projections show that by 2030 EU will import 90 percent of its oil, 80 percent of gas –60 percent of which will be from Russia – and 66 percent of the coal it consumes. Energy security, however, is a two-way street and involves both security of supply and security of demand. Looking at producers and consumers simultaneously explains why both are engaged in a diversification race. On a more concrete level, energy security relates to the security of energy infrastructure and installations. It is also a strategic issue that includes contextualizing European political and economic relations with Russia, Iran, Middle East, the Caspian region, Turkey and other transit countries as well as with growing energy consumers such as China and India. On policy level, energy security measures are interlinked with climate change mitigation and energy efficiency targets. An alternative dimension is to look at the evolving dynamics between national and supranational energy policies. Looking through this institutional lens crystallizes the kernel of European systemic inability to adopt an efficient external energy approach.

This essay will not discuss in detail most of the above mentioned aspects of energy security. Instead, it will focus on the manner in which relations between EU Institutions and its decision-making processes affect policy-making in the field of external dimension to energy. This institutionalist view tries to explain external energy policy as a result of ongoing dynamics between different EU institutions that define the field of possible solutions. The Commission treats energy purely as a commodity and due to its concise mandate is keener on choosing a market approach to address energy security – both for internal and external aspects of energy policy. The Council would prefer adding the geopolitical dimension to external energy security but lacks strong and unified backing from member states. While there are regions where the external market approach makes sense (e.g. Western Balkans), it is a tall order to expect this market approach to address EU energy interests in the Caspian basin. A solution lies in the right combination and sequencing of market approach and geopolitics. One of the success stories in finding a proper mixture between the two was active U.S. engagement

[1] Dimitrios Triantaphyllou, "Energy Security and Common Foreign and Security Policy (CFSP): The Wider Black Sea Area Context", *Southeast European and Black Sea Studies*, Vol. 7, No. 2, June 2007, pp. 289–302

in building the Baku-Tbilisi-Ceyhan (BTC) pipeline. The project's success has implications for European external energy policy-making, especially for similar upstream projects in the Caspian region.

EU Inter-Institutional Dynamics Shaping External Energy Policy

Relations between EU Institutions are based both on cooperation and intra-institutional rivalry. The latter is often deemed as simply 'turf wars' and not given much analytical attention in the field of energy policy. There are, nevertheless, several levels of interaction between institutions as each is following their own logic and mandate. The second level of analysis, more vital for this paper, is then to examine implications of these institutional rivalries on policy-making.

Most relevant EU actors in the external energy policy-making are the member states, the Commission, mainly the Directorate-General for Energy and Transport (DG TREN) and External Relations Directorate-General (DG RELEX), the Council, with High Representative for Common Foreign and Security Policy (CFSP) and regional Special Representatives.

Dynamics between member states and EU institutions are most relevant for the advancement of policy-making in the external energy domain. Member states still keep an upper hand on external relations and are not willing to yield their power to the EU. This holds true for energy relations, yet, recent gas disputes between Russia, Ukraine and Belarus have reminded member states of the shortcomings of keeping 27 separate policies with external energy suppliers. Members recognized a need to formulate a framework for common external energy strategy, the parameters of which touch upon political and energy dialogues with third countries that predominantly fall under the CFSP mandate of the Council. The actual effectiveness of present European energy strategy in securing external energy supplies is a separate issue and even Javier Solana recently stated that the EU at present has no credible external energy policy.[2]

On the other hand, the internal energy acquis is thick and well developed. Even though the European Community has no explicit jurisdictional competence in the field of energy policy, the Commission has increased its competence by linking the energy issue with competition and trade, i.e. with the provisions of the single market. This policy entrepreneurship of the Commission 'economized' the energy issue. Energy is seen as a commodity being part of a single market, which leaves little room for national politics. At present, important legislation is on the EU decision-making table attempting to create a genuinely interconnected and competitive internal market for gas and electricity. The disputable part of it is the creation of an unbundling regime that will separate the production and distribu-

[2] Javier Solana, EU High Representative for CFSP, ''The External Energy Policy of the European Policy'', speech given at the Annual Conference of the French Institute of International Relations, Brussels, 1 February 2008.

tion arm of large energy companies. Commission's proposal aims to ensure fair and non-discriminatory access currently hindered by large vertically integrated operators. Several members are not on board with this proposal and the Commission's position on some competition clauses is at odds with national states.

In shaping external energy strategy, the Council's and the Commission's competencies overlap. The latter has a concise mandate on European community policies such as trade, development, competition, research and environment. Here the Commission enjoys well-established independent legal basis and by linking the energy issue to European acquis it also has obtained nearly a monopoly over energy policy. What is more, the Commission has an exclusive competence when it comes to commercial relations with third countries. The Commission, therefore, has an interest in acting as a policy entrepreneur and defining external energy security as a lack of market governance in European neighborhood. The Commission, though, is not a unitary actor and various DGs have their own internal agendas, which are again shaped by various actors. In the external energy field both DG Energy and DG RELEX have a say in framing external energy policy. The former sees it as a simplified extension of internal regulatory energy framework and the latter as a part of broad foreign policy objectives, which intertwine with conflict prevention and resolution, non-proliferation and human rights.

The Council, on the other hand, has no institutional interest in linking external energy security with basic parameters of internal energy acquis. Even more, Solana is well aware that Europe cannot rely solely on market approach in guaranteeing energy supply and is "forced to mix politics with energy supply simply because that is the way the world is".[3] The Council, though, has substantially less power than the Commission and cannot enter in political and energy dialogues freely. Many EU member states are skeptical in forming a collective external energy security strategy and prefer bilateral agreements with producer countries. Numerous members have recently signed individual pipeline deals with Gazprom, even though this contradicts basic EU principles. The fact that a regional game for security of supplies is not being played in a vacuum needs to be added to the equation. Especially China and Russia at present seem immune to the creation of a multilateral energy regime and prefer to play it bilaterally and compete for scarce resources.

Market Governance vs. Geopolitics –Looking for a Balance

So far the paper analyzed European external energy strategy through the prism of inter-institutional relations and competencies. Present external energy strategy can be contextualized also through a prism of two opposing concepts – market-

[3] Javier Solana, "Energy in the Common Foreign and Security Policy", Greg Austin and Marie-Ange Schellekens-Gaiffe (eds.) Energy and Conflict Prevention, Anna Lindh Programme on Conflict Prevention, Sweden: Gidlunds, 2007.

[4] Richard Youngs, "Europe's External Energy Policy: Between Geopolitics and the Market", CEPS Working Document, No. 278, November 2007.

governance approach and geopolitics.[4] EU decision-making setting clearly divides energy security mandate between institutions with different authorities. This helps to explain the division between a market approach and an almost non-existent geopolitical leg. As energy security is becoming an external and collective issue, it is less clear, if the commodity driven view will address all the challenges. The political dimension has to be included when dealing with external partners, but has to go beyond mere engagement in political dialogues and be based on concrete projects.

Is there a case in which a pure market governance approach is working well in external energy relations? Present EU energy strategy for the Western Balkans is built around the concept of establishing a regional Energy Community. The process aims to extend EU's internal energy market to Southeastern Europe (SEE) by creating a regulatory and economic market framework capable of attracting financial injections, enhancing security of supply while keeping in mind the environmental dimension, and developing conditions for competition on both the electricity and gas markets. Regional governments have all embraced the Energy Community process that aims to bring them closer to the EU regulatory mechanism.

Energy Community Treaty (ECT) obligations, though, are very much aligned with EU's internal energy acquis, and adopting the treaty goes hand in hand with the EU enlargement policy. It offers a semi-EU energy membership to a set of countries that have a clear EU perspective. The reason why the market governance approach works in SEE, then, has more to do with conditionality and a carrot of eventual membership than with effectiveness of EU external energy policy. While the countries with no such guarantee in their pocket are more reluctant to mimic EU acuis and incorporate it in their regulatory framework. This holds true for Russia and South Caucasus, while Turkey is somewhere in between. As EU Energy chapter is about to open for Turkey, the country has achieved enormous success in harmonizing with EU standards, though it is still reluctant to join the ECT process.

The Western Balkans have not avoided a geopolitical game. With the region's substantive potential to be a new energy corridor for Europe, Russia is exercising its power and placing a Trojan horse in an immediate European zone of influence. The most recent case involves using political leverage on Serbian government to seal a deal on the South Stream route and gain ownership over Serbian National Oil Industry (NIS).

It seems that the external energy market governance approach is successful as long as EU is the only powerful actor in the region. As this condition is rarely satisfied, other powers often prevail and out-race Europe in making energy deals.

A real problem with the success record of present external energy strategy is that there are no further enlargements on the horizon. What is the viable alternative to membership carrot that would leverage European power in persuading non-members to comply with EU standards of promoting transparent, predictable and secure energy relations?

The shortcoming of each of the strategy is that none is sustainable in its extreme. The pendulum between the market governance approach and geopolitics works best if in balance. The former can only work well with member states and to-be members. As Caspian countries at present are not on this list, there is no interest to comply with EU standards. Pure geopolitics are a dangerous extreme for Europe as this game is not defined on EU terms. While China, Russia and several resource rich countries are well equipped to use energy as a token of power in international relations this is not the case with Europe. Geopolitical assessment and cooperation need to find a right balance in EU energy policies – soon!

Time is of value in the energy contest. "Big deals are being made every day… Our future options seem to be narrowing while others *move in a determined manner*".[5] The nature of upstream energy business is such that it favors long-term contracts and solutions that bring stability. Energy deals being sealed in the Caspian today will have long-lasting implications for European energy security and its role as a regional power. Proposed EU market governance solutions take time to materialize and yield benefits between involved stakeholders. The geopolitical approach played by big regional energy demandeurs, on the other hand, has immediate effect and the potential to close 'windows of opportunity' still open for Europe.

BTC (Baku-Tbilisi-Ceyhan) Pipeline and Lessons Learned

A different approach, the one that innovatively combines market governance and geopolitics, would work best. The active engagement of the U.S. administration in 1998-2004 in the settlement of the BTC oil pipeline is an example. The BTC route circumvents Russia, hence prevents Moscow from achieving a monopoly over Caspian export routes to Europe. While the BTC project demanded engagement and tremendous coordination between corridor governments, the World Bank, EBRD and private sector, political momentum was gained once the US government was fully engaged. The U.S. support was crucial in three areas: in obtaining a formal guarantee on costs of construction which gave a green light to companies, commercial risk was further decreased as the U.S. provided political risk insurance for the project through Overseas Private Investment Corporation (OPIC), and in working closely with the leaders of respective governments.[6]

[5] Javier Solana , EU High Representative for CFSP, "The External Energy Policy of the European Policy'', speech given at the Annual Conference of the French Institute of International Relations, Brussels, 1 February 2008.

[6] Richard L. Morningstar, "The New Great Game? Opportunities for Transatlantic Cooperation in the Caspian Region", *Transatlantic Thinkers Paper Series*, Bertelsmann-Stiftung, 2007.

This type of backing made the BTC project commercially feasible in the absence of market governance rules.

The success of the BTC pipeline process set a template of parameters for future engagement with the region. It prioritized the building of a strategic energy infrastructure. Only when the Caspian countries were physically independent from Russia would they become receptive to broader political dialogues coming from the West. Independent pipeline infrastructure is a vital element of sovereignty for the Caspian states and very limited cooperation with the West is possible before this precondition is achieved. Azerbaijan and Georgia are a case in point.

Only when EU leaders understand the importance of right sequencing of geopolitical and the market governance approach can substantive cooperation with the Caspian region become feasible. As long as vital infrastructure is being constructed in directions leading away from Europe, towards China and Russia, the European role will be limited to a political dialogue with the Caspian.

The complex decision-making structure of the EU and inter-institutional dynamics prevents the EU from speaking in a unified voice as the U.S. administration did in the case of the BTC pipeline. Considering these limitations, the EU will need to put significantly greater effort in organizational coordination to replicate BTC's success. It will have to work with private partners and international organizations with a stake in the project. Safeguarding commercial interests does not necessarily equal creating market conditions as a precondition for engagement. Good governance is best achieved through direct cooperation in concrete projects that make economic sense and are of strategic importance.