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European Energy Charter Update

Russia's Position at the Basic Agreement Negotiations

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When in December 1991 the European Energy Charter was being signed by the European Community, the US, Canada, Japan, Australia, Russia, and the CIS states (with the exception of Turkmenistan), all parties expressed their readiness to further develop the cooperation outlined in the charter by drafting a so-called Basic Agreement. Unlike the charter, the Basic Agreement would be a multilateral trade, political, and economic document enforceable by law. It would contain sections on access to resources (regulations governing investment), access to markets (regulations governing trade), and other related issues such as transit, access to capital and technologies, conditions for doing business, etc.

Negotiations on the Basic Agreement—still underway at the present time — should result in approval of the final text as well as follow-up protocols concerning specific branches of the energy industry: hydrocarbons; efficient energy generation (with an emphasis on environmental issues); and nuclear energy (emphasizing safety issues). If ratified, the resulting group of documents is expected to be unprecedented, creating a single energy space for the entire industrially developed world with uniform regulations governing investment; business activity; energy transportation; transit; environmental protection; nuclear safety; and access to technologies, energy, financial resources, and energy markets.

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The first round of negotiations on the Basic Agreement and related protocols revealed that most Western countries want to see them adopted with lightning speed. The Russian delegation, on the other hand, is intent on a more detailed deliberation on all the drafts, primarily because they contain a number of issues familiar to the West, but completely new to Russia. Although the agreement was originally slated to be signed in Lisbon in late June, Russia—either because of a lack of appropriate legislation and infrastructure or due to preoccupation with its difficult transition to a market economy—is not yet ready to put some of the proposed regulations into practice.

As it stands today, the Basic Agreement covers key sectors of the Russian economy as well as the country's relations with foreign companies. The agreement is likely to be of paramount importance in drafting both Russian economic laws and a national judicial code, particularly in terms of foreign investment, foreign business activity, rules of competition, monopoly control, government procurement, and ruble convertibility.

Providing a Balance of Interests

Like any international agreement, however, the Basic Agreement should provide a balance of interests for all its members. Russia is particularly interested in access to the commodity, capital, and technology markets of member-countries, as well as in attracting foreign credits and receiving transit protection guarantees. The positions of Norway and, to a certain extent, Canada and Australia are similar to that of Russia on these particular issues.

The rest of the European Community, Japan, and the US, meanwhile, are hoping that the Basic Agreement will provide their importers and investors legal and safe access to foreign energy resources. The East European states tend to side with this group, having traditionally been importers of liquid fuel and often playing the role of transit states.

As a result of differing interests, certain issues have become particularly sensitive to the post-Communist bloc during the negotiations: introduction of world prices on energy, granting equal rights to foreign and national investors, liberalizing the energy trade, application of GATT regulations to foreign business

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activity, and making national currencies convertible.

The main difficulty facing Russia, the CIS states and, to some extent, the East European states, however, is that some of the legislative adjustments required by the agreement will take a considerable amount of time to implement. Consequently, during this period these countries will only partially be able to fulfill those obligations imposed by the agreement. For this reason, one of the most important issues on the agenda is to work out a regulation permitting those countries undergoing transition to a market economy to introduce the required legislation on a step-by-step basis. Such a regulation would list both the legislation and the steps to be taken for its eventual enforcement, wherever possible projecting specific dates.

Other Disagreements

Another problematic point is that the Western delegations are insisting on adding certain regulations to the agreement—like the repatriation of foreign investment and revenues gained from them as well as compensation in freely convertible currencies for their possible requisition by the state—which Russia cannot yet accept without serious domestic amendments.

In addition, regulations governing trade between the signatories of the Basic Agreement have not yet been worked out. Originally, the European Community delegation proposed a so-called "two-track approach," in which trade between states that are both Basic Agreement and GATT members would be governed by GATT rules, while trade between those countries and non-GATT members (such as Russia and other CIS states) would be regulated by special rules. In other words, two different sets of trade regulations within the Basic Agreement were originally planned — regulations which would have discriminated against Russia and other ex-Communist states.

In view of the unacceptability of this proposal to the Russian side, the US delegation suggested that all trade under the Basic Agreement be governed by GATT regulations. Russian representatives supported this initiative for two reasons: first of all, because it meant that Russia would be an equal trading partner; secondly, because Russia would establish a relationship with GATT, whereas until now it has been just an observer. By signing the Basic Agreement, the process of Russia's assimilation into GATT would be simplified significantly. That is, the transition period provided for by the Basic Agreement would then automatically become a transition period to full membership in GATT.

What Russia Stands to Gain

Although negotiations have sometimes proved frustrating, Russia's participation in the international agreement could become an important step towards its integration into the global economy. For instance, an analysis of the projected balance of Russian rights and obligations under the Basic Agreement reveals that in exchange for granting foreign investors the same rights of access, production, refining, and transportation of mineral resources as those enjoyed by Russian nationals according to Russian Federation law, the Russian side stands to gain a number of benefits, including:

- More liberal access to markets, know-how, and capital;
- Guarantees of eventual membership in GATT and the abolition of all current discriminatory restrictions on trade with Russia;
- Fair transit conditions;
- Access to the investment markets of Western energy and transportation industries.

Other indirect but important benefits of the Basic Agreement are as follows:

- Its regulations will also cover Russia's historically sensitive relations with the CIS states, making cooperation easier and more amicable;
- Russia's participation in the Basic Agreement will not only considerably improve Russia's role in the system of international cooperation and division of labor, but it will also contribute to the attraction of large-scale investments to key sectors of the national economy which can remain under strict governmental control;
- For the first time, a kind of industrial integration will be set up at the global level in which Russia will occupy a leading position. This, in turn, will strengthen Russia's position when competing with oil-producing states of the Middle East.

What Russia Is Looking to Gain

The Russian delegation has its own goals during negotiations of the Basic Agreement and related protocols:

- To work for a reasonable balance of rights and obligations for Russia with regard to its current economic policy;
- To take full advantage of the transition period in order to facilitate Russia's adjustment to international norms and regulations as reflected in the Basic Agreement (i.e., to seek all possible temporary privileges for Russia concerning those regulations the country would be unable to implement by the time the agreement and protocols were put into effect;

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- To introduce special regulations which would guarantee proper control over investments in Russia;
- To synchronize resolution of the aforementioned problems with the gradual involvement of the CIS states;
- To develop informal contacts which are emerging between Russian and CIS experts.

Questions Still Remain

Despite the obvious interest of many Russians in seeing the agreement signed, some Russian parliamentarians and entrepreneurs will undoubtedly be divided over Russia's participation in the Basic Agreement. Questions about the future of national resources, the "sacrifice" of Russian interests to those of foreign investors, and similar issues are already being hotly debated.

In addition, certain state and quasi-market structures in the highly monopolized Russian energy industry will be reluctant to accept the main premise of the Basic Agreement—foreign access to state resources—perceiving it as a threat to their monopoly on the energy market. Ultimately, the outcome of the Basic Agreement will depend on whether Russia is planning to join the world economic community, accepting its general principles, or whether it will seek ways of improving its economic position by other means.

One More for Total

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Project Economics

According to sources familiar with the contract, Total expects to earn a rate of return of 17.9% on its Komi project. *RPI* also obtained the following financial projections which are based on assumptions that world oil prices will average $150 a ton ($20 a barrel) and inflation will run at 4.5% per year during the 30-year life of the project.

1) Engineering and production costs will amount to $5.304 million (in current prices).

2) Capital expenditures will be $118 million;

3) Operating expenditures will amount to $31.120 billion;

4) Transportation expenditures (oil pipeline) will be $999 million.

The Russian side will be responsible for paying $2.716 billion of these expenditures. RPA

Negotiating Production Deals

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[2] Increasingly, national ministries and committees have administrative units that operate at the local level (e.g., the Anti-Monopoly Commission, the Ministry of Fuel and Power, etc.). These offices must also be "lobbied" as part of the approval process.

[3] Before the new venture is formerly registered, local government (region) officials can only grant preliminary approval of land allocations. The actual allocation cannot take place until after registration.

[4] For example, a May 1992 decree exempts the KomiArcticOil joint venture from paying the export tariff until such time as the original investment is paid off. (Ruling No. 957-r of May 27, 1992). The Novokuibysherskii petrochemical combinat has been freed from paying export tariffs through 1994 to enable it to purchase equipment for capital development (Ruling No. 934-r of May 25, 1992).

Gulf Canada and British Gas

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erations. According to *RPI* sources at Komineft, over the recent months the joint venture produced over 300,000 tons of oil which it did not ship because of the legal uncertainties. These sources indicate that now—after the export-tariff situation has been resolved in favor of the venture—this entire volume will be exported for hard currency to the West. RPA