

CEE Bankwatch Network

Address:

Na Rozcesti 1434/6, 190 00 Prague 9, Czech Republic

Identification number in the register:

93834493808-49

March 7, 2011

To: DG Energy - ENER.A.3
'International Relations and Enlargement'
European Commission

Re: CEE Bankwatch Network contribution to the public consultation process regarding the external dimension of EU energy policy

Dear Commissioner,

CEE Bankwatch Network is grateful for the opportunity to participate in the consultation process regarding the external dimension of the EU's energy policy. Over the last fifteen years Bankwatch has been involved in monitoring the development of the EU's energy policy in the eastern European Neighbourhood Policy (ENP) countries and Central Asia. With this present submission we would like to focus your attention on EU energy policy impacts especially in terms of the sustainable and democratic development of the above-mentioned countries, and to ensure that the external actions of the EU's energy policy respond to the challenges of climate change.

In October 2009 the European Council called for at least 50 percent worldwide emission reductions and aggregate developed country emission reductions of at least 80-95 percent by 2050. The adoption of internal European 20-20-

20 targets can be considered as the first step towards these necessary reductions. However, the policy will definitely fail if the external dimension of EU energy policy continues to be as described below and does not integrate the overarching objectives of the EU defined in the Treaty and other EU policies: it must strive above all to deliver sustainable development, environmental and biodiversity protection, including long-term climate goals, the promotion of human rights and development in the countries outside the EU.

The European Neighbourhood and Partnership Instrument (ENPI) strategy paper 2007-2013 for the eastern neighbourhood region involves contradictory strategic objectives. The first of these is sustainable development and environmental protection, which underpins all EU legislation and policies. However, the second priority, “the need to ensure the diversification and security of energy supplies to the EU”, emphasises the need for the further extraction and transportation of the Caspian Sea’s oil and gas resources to Europe, and– thus prioritises it over the development of an environmentally friendly energy sector within the region. The paradigm has been strengthened by the EU’s Eastern Partnership initiative, where Energy policy represents the core element. The EU’s approach to energy security involves Ukrainian and South Caucasus oil and gas pipelines. The South Caucasus pipeline holds a particular strategic importance on account of its ability to provide natural gas to the planned Nabucco pipeline, the EU’s flagship diversification project. In this context, the Eastern Partnership aims to increase the EU’s ‘energy interdependence’ with the partner countries via pipelines, electricity interconnections and convergence towards the EU energy policy.

This trend has, in recent years, been willingly taken up by East ENP countries, who have been focusing on opportunities to develop unsustainable and environmentally unfriendly mega projects that could present more opportunities for international trade. This has been to the detriment of more of a focus on the development of renewables that would serve a bigger number of communities within the countries.

Our responses to the consultation questions below are complemented by two case studies in the Annex that provide further arguments for the positions expressed in the submission.

Question 1: Should the EU promote further energy market integration and regulatory convergence (notably as regards energy market regulation, environmental and safety standards) with its neighbours? Is there a need for a differentiated approach between the Eastern and Southern neighbours or between countries?

The EU should promote further regulatory convergences (notably as regards energy market regulation, environmental and safety standards), especially for those countries that are part of or will soon become part of the EU Energy Community (EEC). The EEC amounts to a de facto partial integration of these countries into the EU single market. Ukraine and Moldova have also signed the treaty, but have yet to ratify it. Turkey, Norway and Georgia are contemplating the same step. The EEC is currently the most far-reaching integration offer in the energy sector that the EU is extending to its neighbors and represents one of the most pronounced forms of gradual integration.

The EU should support the above-mentioned countries in their adoption of a list of EC directives in the areas of electricity (two directives), gas (one directive), environment (11 directives) and renewable energies (two directives). Additionally, competition articles 81, 82 and 87 of the EU Treaty form part of the Energy Community Treaty (ECT) requiring the participating countries to follow EU competition law. The EU should closely follow how these countries are establishing independent national energy authorities, regulators and transmission system operators, to unbundle integrated companies, to set up national and regional electricity and gas market action plans and to develop an anti-corruption programme.

In addition, expanding and deepening the EEC should promote and establish a privileged position for renewable energy along with the development and implementation of Climate Change law packages. It would also be important to ensure EU support for its immediate neighbourhood so as to develop national climate protection programs in accordance with the UNFCCC and to set up financing plans appropriate to those objectives. The development of renewable sources of energy and energy efficiency must be a significant element in all national climate protection programs.

The approaches and financial interventions should be country tailored in order to ensure efficient action.

Question 2: Should the EU take concrete actions to foster greater investment in renewable energy sources in its neighbouring countries? What actions?

The EU's concrete actions should foster greater investment in renewable energy sources and energy efficiency not only in the neighborhood area, but also in the Global South, with the primary obligation of all external action under the Treaty of Lisbon being to eradicate poverty and promote sustainable development.

Therefore EU external energy actions must concentrate on decentralised and zero emission energy sources, with the primary goal being to increase access to energy for the poor and to support the development of local economies.

From this point of view the main priority should be to concentrate on energy efficiency measures. In order to ensure the delivery of great benefits to the entire region, it is crucial for EU energy policy to tackle in-depth prevailing and appalling energy inefficiency – a Soviet legacy. Improving energy efficiency in the region will strengthen not only its economic competitiveness, will lower fuel poverty and improve energy security but will also lower carbon dioxide emissions, thereby mitigating climate change.

Until now the European Investment Bank 's (EIB) lending outside of the EU has concentrated on climate-damaging projects as well as environmentally and socially harmful large hydropower projects, while its lending for new renewables constituted only EUR 321 million out of EUR 7 billion in the years 2002-2008¹. This approach “promotes a large-scale and export-oriented energy model rather than supporting small-scale decentralized energy projects that are more appropriate and effective in meeting basic needs in rural areas²”. Therefore the EU should ensure support through its institutions, including the different regional banks, to “support alternative, small-scale decentralised energy projects which take account of the needs of local communities and the economic realities of different countries, and to set specific targets and monitoring guidelines to ensure that energy lending will benefit the poor³”.

The most important obstacle for the development of truly renewable energy and to ensure energy efficiency, both in the immediate neighborhood as well as in the Global South, is the lack of a suitable legal framework to provide the long-term sustainability of projects and programs. This, therefore, should be the major focus for the EU: to ensure that legal frameworks, together with environmentally sound road maps and financial packages, are developed.

Donor coordination should be one of the most integral aspects of the work, not to undermine the development of renewables and energy efficiency through business as usual projects and programs that unfortunately represent a large share of the portfolios of almost all the international financial institutions (IFIs), and that also have a strong lobby in the state structures of almost every country, especially where the energy sector is eminent. The EU's

¹ Change the lending, not the climate, CEE Bankwatch Network, 2009.

² European Parliament resolution of 17 February 2011 on the World Bank's energy strategy for developing countries, <http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P7-TA-2011-0067&language=EN&ring=B7-2011-0128>

³ European Parliament resolution of 17 February 2011 on the World Bank's energy strategy for developing countries, <http://www.europarl.europa.eu/sides/getDoc.do?type=TA&reference=P7-TA-2011-0067&language=EN&ring=B7-2011-0128>

Neighbourhood Investment Facility (NIF), that aims to maximise the effects of EU funding by increasing the complementarity of funds and through the leveraging effect, should take on a leading role in the process of moving renewables and energy efficiency initiatives higher up the agenda of the IFIs.

Question 3: What measures should the EU take to reinforce and focus its partnerships with key suppliers (of hydrocarbons and other energy sources) and transit countries? What should be the focus of such enhanced partnerships? (What countries? What topics?)

The external dimension of the EU's energy policy should fully reflect Article 21 of the Treaty of the European Union (TEU), that stipulates that the EU in its external actions is obliged to "help develop international measures to preserve and improve the quality of the environment and the sustainable management of global natural resources, in order to ensure sustainable development, with the primary aim of eradicating poverty", as well as "consolidate and support democracy, the rule of law, human rights and the principles of international law". It further states that "The Union shall ensure consistency between the different areas of its external action and between these and its other policies."

Therefore, the EU Energy policy should be subordinated to EU Development policy and contribute to its advancement in line with the above directions. Unfortunately we see opposite approach of aggressively promoted energy security as security of supplies through new interconnections with the neighbouring countries and other regions such as in the "Energy 2020 A strategy for competitive, sustainable and secure energy", that states "The construction of new interconnections at our borders should receive the same attention and policies as intra-EU projects. Such links are essential not only for our neighbours but to ensure the EU's stability and security of supply. There will be specific emphasis on the Southern corridor and the effective start of projects of European interest, in particular Nabucco and ITGI."

The EU has up to now focused primarily on energy issues in Central Asia from the perspective of establishing links between energy consumers in Europe and energy producers in Central Asia, with a focus on hydrocarbons. In addition, of the so called "usual" partner countries such as Azerbaijan and Kazakhstan with whom the EU has had long-term cooperation since the early nineties, in recent years the EU has significantly increased its presence and communication with Turkmenistan and Uzbekistan. The argument for this is based around the assumption that non-engagement or even sanctions with these countries is counterproductive, and therefore through broadening energy ties with said countries the EU can ensure the broadening and intensification of the human rights dialogue, the support and promotion of regional cooperation, and enhance the involvement of EU institutions including the

EIB and the EBRD. While in theory this approach appears attractive, in practice it has quite a number of deficiencies, and Azerbaijan is a good example of such. Azeri civil society has started to express increased concerns regarding the role of the EU's Energy cooperation Agenda⁴ in terms of democratization and human rights protection. Some predictions from as far back as 2005 stated that "The current blemishes – problems in the area of democratization – did not seem to affect the emerging priorities in the bilateral relations [EU-Azerbaijan] in the coming five years"⁵. According to the Freedom House, Azerbaijan has not improved its record in the last five years⁶ and the country status is 'not free' again in 2010. Meanwhile, President Ilham Aliyev consolidated his authoritarian rule with a March 2009 referendum that eliminated presidential term limits.

While there has been almost no progress regarding democratisation and human rights protection, in economic areas the EU has definitely been more successful. For example, the EU's mediation efforts (of August 2010) to solve the territorial differences between the Caspian Sea littoral states of Azerbaijan and Turkmenistan can be considered to be quite successful, yet it remains difficult to recall any significant progress in those countries regarding democracy and human rights protection based on EU initiatives and efforts.

There are also alarming signs that the EU will also support the development of large hydropower in the mountainous areas of Kyrgyzstan and Tajikistan, with the aim being to promote a greater energy balance across the region and the development of a regional electricity market. And again, alongside other EU institutions, the EBRD and EIB are both keen to get involved in the new energy game. During his last briefing Commissioner Pielbags stressed that if there would be support for Uzbekistan to develop a more efficient water irrigation system and decrease the ambition of Tajikistan, then a compromise could be found⁷. While compromises can always be found at the state level (the Baku-Tbilisi-Ceyhan pipeline is a good example of this), the affected ones are not the heads of State that sign the agreements but ordinary poor people who live in the area and who often have no means to apply for remedies.

The issues of human rights and democracy must be mainstreamed into the EU external energy policy, by formulating upfront conditions for the EU's engagement with countries where hardline governmental regimes exist, such as Turkmenistan. Furthermore, the EU's proposed actions should be screened against their implications

⁴ Memorandum of Understanding on a Strategic Partnership between the European Union and the Republic of Azerbaijan in the field of energy, Council of the European Union, Brussels, 23 October 2006.

⁵ http://www.ecologic-events.de/hertie-school-2008/reading_lists/download/alieva_eu_south_caucasus.pdf

⁶ Political rights 6, civil liberties 5, <http://www.freedomhouse.org/template.cfm?page=22&year=2010&country=7775>

⁷ Post-Lisbon: How to achieve coherence between energy security and development policies? Briefing session for Parliamentarians and policy makers, Brussels, 9 February 2011

for sustaining undemocratic regimes by strengthening the economic base of their existence in the countries where the extractive industries are controlled by powerful elites.

Annex.

Where the EU's external energy policy goes wrong in the Eastern Neighbourhood countries

1. Case of Ukraine – Plans to import nuclear and coal-derived electricity to the EU

In recent years we have witnessed the evolution of the EU's approach to Ukraine's energy sector. As a result of the gas disputes between Russia and Ukraine, the EU has become more involved in attempts to reform Ukraine's gas sector and in guaranteeing the uninterrupted transit of gas to the EU by diplomatic means.

Another aspect of the EU's involvement is often overlooked – namely the EU's interest in importing electricity from Ukraine. In November last year Jerzy Buzek, the president of the European Parliament, openly called for the EU's joint purchases of nuclear-derived electricity from Ukraine and Russia⁸. The support of EU institutions for electricity transmission infrastructure in Ukraine shows how the infrastructural foundations for this plan are to be laid with the use of European public money.

Ukraine's plan to increase electricity generation

In the national energy strategy up to 2030 and adopted in 2006, Ukraine's government foresees massive investments in its energy sector. Based on the plans to move from electricity production based on gas to coal, there will be at least a two-fold rise in Ukraine's greenhouse gases emissions between 2005 and 2030.

⁸http://www.eib.org/attachments/general/events/warsaw_26112010_buzek_en.pdf

The Energy Strategy contains plans to increase the coal consumption two or even three times (depending on the scenario chosen). It is worth mentioning that Ukraine's coal industry is traditionally unprofitable and requires significant financial support from the government. In 2008, the coal sector received funding of UAH 7,475.68 million (nearly EUR 1 billion), which is approximately three percent of Ukraine's annual budget. However, the largest share of funding is used to cover the prime cost. In 2008, approximately 60 percent of all money provided to support the sector was used to offset losses.

Another element in the puzzle is Ukraine's plans to expand its nuclear industry. The Ukrainian Energy Strategy foresees the construction of 22 new reactors in the period up to 2030 – however such plans look extremely unrealistic if not utopian, though the construction of two reactors – Khmelnytsky 3 and 4 – has already reached an initial stage of process.

Increased electricity generation will not only satisfy local needs, but is also aimed at increasing export volumes to 25 TWh in 2030. This volume is close to the amount of electricity generated in Slovakia in 2007. The most promising market for Ukraine's electricity is, of course, the integrated energy market of the EU.

Transmission infrastructure

For these export plans to be realized, massive investments in Ukraine's electricity transmission infrastructure are needed. In the last five years, two European public lenders, the European Investment Bank (EIB) and the European Bank for Reconstruction and Development (EBRD), have invested in a number of high voltage (HV) transmission line (TL) projects belonging to Ukraine's state owned company Ukrenergo. Until now both banks' loans for a series of four projects were worth approximately EUR 650 million. An additional EUR 13 million was spent in the form of grants for technical assistance from the EU's Neighbourhood Investment Facility.

Recently, on October 12, 2010, the EBRD published a procurement notice for the development of the feasibility study for Second Backbone UHV Corridor, a major 750 KV East-West power line that will connect three of Ukraine's nuclear power stations. The construction of this power line was foreseen by the Energy Strategy of Ukraine, which presents it as an important tool for creating the conditions for the integration of the Ukrainian grid into the European network and to bring about a significant increase in the export of Ukraine's electricity.

Alternatives

The EU's reliance on dirty energy sources, even when outsourced to neighbouring countries, does not make the EU safer. Neither the risk brought by greenhouse gases emitted in Ukraine nor the radiation from its nuclear power plants respect borders. On top of these factors, importing subsidised electricity from Ukraine will undermine EU efforts to improve energy efficiency across the continent-wide economy and to spur the development of domestic renewable energy sources.

In the electricity transmission sector in Ukraine, as well as in the rest of the region, instead of focusing on export-oriented mega projects that are damaging to the local environment, the EU should concentrate its efforts on supporting renewable energy projects that have undergone a visible boom since new legislation on “green tariffs” was adopted. As far as it goes with electricity transmission, priority should be given to low-voltage local grid (below 110kV) modernisation and the development of technical solutions for the integration of state-of-the-art renewable energy sources into the outdated grid design that persists across the region.

2. Case of Georgia – The potential to export electricity through environmental destruction

Georgia is a country rich in hydropower potential. Large hydropower accounts for 85 percent of the country's electricity – annual output of around 8.5 TWh from hydropower almost satisfies the needs of the domestic market.

Georgia's plan to increase electricity generation

In recent years Georgia's government has sought to position the country as a future regional renewable energy hub⁹. According to President Saakashvili, the energy sector should constitute one of the three pillars of Georgia's future economic development (along with agriculture and tourism) and the government expects to attract investments worth around USD 5 billion in the next few years. The plans include highly controversial large hydro cascades mainly in mountainous areas of Georgia, including the Khudoni HPP (702MW, annual output 1.5 TWh) on Enguri, the Nenskra cascade (600 MW), the Namakvani cascade (450 MW, annual output 1.6 TWh), and the Nenskra Cascade (438 MW, 1.2 TWh). The planned projects do not comply with the principles of sustainable

⁹ Regional Power Transmission Enhancement Project, Georgia, www.adb.org

development and do not represent renewable energy¹⁰, while they may have serious negative impacts on the environment, drastically change the social and demographic situation in Georgia's mountainous regions and also promote the destruction of cultural heritage.

Transmission infrastructure

As one of the preconditions for becoming a regional hub based on so called renewable energy, the Government of Georgia is considering the construction of new transmission lines. According to the ministry of energy, the first stage task is to ensure the harmonisation of Georgia's energy system with that of Turkey, and to subsequently gain access to the South-East European market by 2015-2017¹¹.

The Construction of the Black Sea Energy Transmission System started in 2009. The aim of the project is the rehabilitation and construction of a "315 km high voltage grid connecting the Georgian and Turkish power networks, to connect the power grids of the Southern Caucasus countries and increase electricity exports to Turkey and Europe, while bolstering energy security in the region".

The project is co-financed by KfW with EUR 100 million (a EUR 75 million loan plus a EUR 25 million grant), the EBRD and the EIB have earmarked EUR 160 million (EUR 80 million loans each), and the Neighbourhood Investment Facility (NIF), has provided an EUR 8 million grant for project preparation¹².

The new transmission line will help to export excess energy in the summer time, as well as support the stabilisation of the transmission system, as currently the transportation of electricity from western Georgia (where the majority of the HPPs are located), to the east (where major consumers are located) relies on one single 500kv line. As a result of the projects the disruptions of electricity supply to Tbilisi and other eastern Georgian regions will cease. The new line will have a capacity of up to 1,000 MW, excessive for Georgia's current demand, but pertinent in the face of increasing investment. The Georgian government's hopes lie in exporting existing excessive electricity outside of Georgia. It is expected that by 2018 the big hydropower plants will have been constructed, and this line will be fully utilised.

¹⁰ <http://www.internationalrivers.org/en/blog/zachary-hurwitz/2011-2-25/european-parliament-urges-world-bank-out-large-dams>

¹¹ http://csrdg.ge/index.php?module=text&link_id=149&lang=geo&lang=geo

¹² South Caucasus united by common electricity grid <http://www.enpiinfo.eu/files/features/FT28%20east%20Georgia%20EN.pdf>

In addition, at the end of 2010, the Asian Development Bank started preparatory works for A new regional transmission line¹³. The project aims to support the enhancement and strengthening of transmission capacity for electricity trade and transit with Armenia, Azerbaijan and Turkey.

Unsolved problems of the Georgian energy sector

While the government is intent on attracting billions to construct these new large HPPs, existing problems associated with Georgia's energy sector are unsolved.

At present consumer tariffs for energy are relatively high in Georgia in comparison to the neighbouring states. Since the biggest share of expensive energy is consumed by the population, existing high tariffs and prices on energy are a huge burden on households of a transitional country where many families still live in poverty. The difference between energy generation, transmission and distribution tariffs are significantly high in Georgia in comparison to other countries. Energy generation costs are relatively low, since the biggest share of electricity is produced in the local Hydro Power Plants (HPPs). Nevertheless, losses in the local energy system are still quite significant, which has its impact on the high prices set by distribution companies.¹⁴

Another side of the problem is that energy intensity in the country is still more than twice the world average. Energy production is still highly extensive in Georgia. The share of energy in the country's GDP is three times higher than the EU average. Since Georgia is a net importer of energy, increasing energy prices in the world market directly influence issues related to local consumption. Georgian business is left in an uncompetitive position both in terms of competing with imported products on the local market and possible exports.

It is therefore obvious that the most cost effective and sustainable approach for resolving Georgia's energy needs would be to increase investments in energy efficiency and energy saving.

Piotr Trzaskowski
Energy and Climate Coordinator

ul. Wspólna 41 lok. 72, 00-519, Warszawa, Poland
tel.: (+48) 228920086

¹³ Regional Power Transmission Enhancement Project, Georgia, www.adb.org

¹⁴ L.Jervalidze, State Policy of Georgia in the Energy Sector

e-mail: piotrt@bankwatch.org

Manana Kochladze
Regional Coordinator for Caucasus

62 Chavchavadze avenue,
0162, Tbilisi, Georgia
Tel.: (+995) 32292773
email: manana@bankwatch.org