Barometr Regionalny
Tom 16 nr 5

Cross-Border Cooperation between Poland, Russia and Ukraine on Oil and Gas Trade — an Attempt at Reflection in the Context of Energy Security

Wojciech Konaszczuk
Maria Curie-Sklodowska University, Poland

Abstract

The issue of supplies of raw materials in the form of crude oil and natural gas to the European Union, including Poland, is a complex and problematic one. Changes in the geopolitics of the end of the 1990s within Europe caused the necessity of changes in international agreements concerning oil and natural gas trade among their parties — EU countries. The simultaneous independence of Ukraine as a state entity from Russia caused complications not only of a political but also of an economic nature. The aim of the article is to present the author's view on the complexities of crude oil and natural gas trading between Poland, Russia and Ukraine and an attempt at analysis. The legal-dogmatic and statistical methods made it possible to identify important conclusions for the future, the most important of which include: the need to renegotiate bilateral agreements between Russia and Poland, the need to renegotiate bilateral agreements between Poland and Ukraine, and the need to develop a common EU position within the security policy of this international organization (i.e., the European Union).

Keywords: gas transmission, oil transmission, restrictions on gas trade, restrictions on oil trade, Russia, Ukraine, Poland, cross-border trade in energy carriers

JEL: F02, F15, F42, K32, Q4

The level of prosperity of societies within individual countries depends on various factors, including economic conditions, including issues related to cross-border (international) transport of goods and services. In turn, the degree of international obligations creating most-favorable conditions for trade depends on the will of the sovereign in power. In the past, the level of treaty obligations in this respect depended solely on the will of the Contracting Parties, and now it must take into account the obligations of the Contracting Parties arising from their participation in international organizations, military alliances or armed conflicts. The purpose of this article is to draw attention to the complexity of the processes of trade in two selected carriers of oil and natural gas through the prism of the neighborhood of three countries and on the basis of geographical criteria. The leading thesis is based on the assumption that the level of current legal obligations of international trade participants effectively reduces the profitability of trade in the indicated carriers, contributing to the emergence of unfavorable phenomena in the economy and beyond.

The introduction to the analysis in the article is a thesis with which the author agrees that "trade cures destructive superstitions... and wherever there are mild customs, there is trade; wherever there is trade, there are mild customs" and "the natural result of trade is that it encourages

* The nationalities are listed according to the alphabetical order only, without any other criteria.

E-mail addresses of the authors
Wojciech Konaszczuk: wojciech.konaszczuk@poczta.umcs.lublin.pl

peace. Two nations that trade with each other become interdependent and their relationship is based on mutual needs."[1]

Relations between trading nations are therefore based on mutual needs and expectations. Trade in natural resources occupies a special place among many areas of trade, as reflected in many UN resolutions and the activities of many international organizations, including the United Nations Conference on Trade and Development (UNCTAD). The Fourth UNCTAD Conference in Nairobi in 1976 adopted the so-called common programme relating to the need to regulate 18 raw materials through international agreements and to establish a Common Fund to secure them.[2] As a result, on 28 June 1980 an agreement regulating the trade in raw materials was adopted.[3]

The demand for energy sources has increased rapidly since the second half of the 20th century. These include derivatives of crude oil such as diesel oil, petrol and derivatives in the process of crude oil rectification, as well as natural gas called "blue fuel" in the literature on the subject. In the process of ensuring the energy security of a country or a group of countries, oil and natural gas play the most important role, which are the basis for further redistribution of products or obtaining the final product from them in the form of diesel oil or electricity. It should also be stressed that these natural resources belong to the so-called primary energy sources, as opposed to white or green energy, which belongs to the renewable energy group.

The problem of trading in energy carriers within the countries listed in the title, apart from the obvious benefits associated with obtaining financial resources by the Russian Federation, also has other consequences. Undoubtedly, the geopolitical conditions of Poland, Ukraine and other European countries (both EU and non-EU) require taking into account the specific "dependence" of their economies on the supply of raw materials from the Russian Federation (Konoplyanik and Walde 2006).

The countries of Western Europe, starting from the period after the Second World War, tried, with various results, to become independent from oil and gas supplies from the Union of Soviet Socialist Republics (USSR). The establishment of the European Atomic Energy Community was to serve this purpose. It should be emphasized that the importance of this problem was so significant that it became one of the grounds for the creation of the European Atomic Energy Community (EAEC) Agreement by way of an interstate agreement.[4]

Currently, the concept of energy security of the European Union Member States, including Poland, which has been a member of the European Union since 1 May 2004, is based on the original model based on natural sources.[5] In the case of the European Union, the total consumption of energy carriers in all EU Member States accounts for 18,0% of global demand.[6] In this group, the share of individual raw materials is as follows: oil — 36,9%, natural gas (including LPG and LNG)[7] — 24,5%, solid fuel (hard coal, wood) — 17,6%, nuclear energy — 14,2%, renewable sources — 6,6%, other — 0,2%.[8] As it results from this, the most important raw materials on the global energy market are concentrated around derivatives of crude oil and natural gas.

1. Montesquieu, Spirit of Laws, bk. 20, CHS. 1–8 (Chapter 4 Republican Government, Document 2), [@:] http://press-pubs.uchicago.edu/founders/documents/v1ch4s2.html.

2. See: UNCTAD TD/218, vol. 1., 1976.05.31.

3. See: UNCTAD TD/326, vol.1., 1983.06.02.

4. See: Traktat między Królestwem Belgii, Królestwem Danii, Republiką Federalną Niemiec, Republiką Grecką, Królestwem Hiszpanii, Republiką Francuską, Irlandią, Republiką Włoską, Wielkim Księstwem Luksemburga, Królestwem Niderlandów, Republiką Austrii, Republiką Portugalską, Republiką Finlandii, Królestwem Szwecji, Zjednoczonym Królestwem Wielkiej Brytanii i Irlandii Północnej (Państwami Członkowskimi Unii Europejskiej) a Republiką Czeską, Republiką Estońską, Republiką Cypryjską, Republiką Łotewską, Republiką Litewską, Republiką Węgierską, Republiką Malty, Rzecząpospolitą Polską, Republiką Słowenii, Republiką Słowacką dotyczący przystąpienia Republiki Czeskiej, Republiki Estońskiej, Republiki Cypryjskiej, Republiki Łotewskiej, Republiki Litewskiej, Republiki Węgierskiej, Republiki Malty, Rzeczypospolitej Polskiej, Republiki Słowenii i Republiki Słowackiej do Unii Europejskiej, podpisany w Atenach w dniu 16 kwietnia 2003 r. DzU z 2004 r. nr 90 poz. 864.

5. Q&A Ukraine Gas Raw BBC News, 4 January 2006.

6. [In the journal European practice of number notation is followed — for example, 36 333,33 (European style) = 36 333.33 (Canadian style) = 36,333.33 (US and British style). — Ed.]

7. LPG-Liquified Petroleum Gas, LNG-Liquified Natural Gas.

8. See: EU Energy Policy Data. SEC (2007) 12, Brussels, 10 January 2007.

It should be stressed that Poland has geographical conditions which ensure its natural gas resources. Until 2009, Polish natural gas deposits were estimated at approx. 678 billion m^3 of natural gas. Currently, gas production in Poland covers 40% of domestic demand, which means that the remaining 60% must be imported. In 2012, the Polish Geological Institute in cooperation with the American Geological Survey (USGS-U.S. Geological Survey), based on archival data from the years 1950–1990, assessed oil resources in the so-called shale formations in the Baltic–Podlasie–Lublin Basin. According to the estimation, the maximum resources may amount to 1 920 billion m^3 of natural gas and 535 million tons of crude oil. It should be emphasized with optimum probability that the resources for natural gas are in the range of 346–768 billion m^3 and 215–268 million tons for crude oil.[9] The main production area is the Lower Poland, Przedgórze and Carpathian Mountains. In 2011, taking into account production from gas fields, 5 645 million m^3 of "blue fuel" were extracted from oil fields from condensate fields in Poland. It should be emphasized that the highest gas production at the moment is in the industrial field.

Production there has been going on continuously since 1970. Quite a significant problem of Polish production is the very large dispersion of mining plants.[10] There are 283 documented deposits in Poland, of which 35 in the Carpathians alone. Another problem faced by experts in the energy sector is the high level of sulphation. This causes the necessity of costly desulphurization, which puts into question the profitability of extraction. In this situation, extraction in Poland can only be an alternative to import.

The Russian Federation is one of the largest exporters of crude oil and natural gas in the world. It is ranked eighth in the group of countries. Cooperation between the USSR and the European Communities should be sought even during the so-called "Cold War." When the representatives of the European Coal and Steel Community (France, Germany, Italy, Belgium, Holland, Luxembourg), taking into account economic factors, were forced to sign an agreement and import crude oil and natural gas from the USSR. The large-scale supply of "blue fuel" to Western Europe began at the end of the 1950s. The periods 1971–1972 and 1981–1983, when the supply of energy carriers from Arab countries was limited, were a particular period which contributed to the rapid increase in exports to Europe. This undoubtedly contributed to an increase in the level of energy security as well as to a strengthening of closer mutual relations between the European Communities and the USSR (Sadegh-Zadeh 2007). After the collapse of the USSR, the process of establishing mutual relations between these entities can be divided into three basic stages. The first one was initiated when the Prime Minister of the Netherlands-Lubbers, at a conference of EU member states in Berlin in 1991, proposed the inclusion of the legal successor of the USSR-Russian Federation in the programme of European cooperation in the energy sector.[11]

Earlier, at the European Council meeting in Dublin in June 1990, the Prime Minister of the Netherlands suggested that economic recovery in Eastern Europe and the then Union of Soviet Socialist Republics could stimulate and accelerate cooperation in the energy sector. This proposal was welcomed by the Council, which asked the Commission of the European Communities to examine how best to implement such cooperation. In February 1991, the Commission put forward the idea of creating a European Energy Charter. Following discussions on the Commission's proposal in the Council of the European Communities, the European Communities invited the other countries of Western and Eastern Europe, the Union of Soviet Socialist Republics and non-European members of the Organisation for Economic Cooperation and Development (OECD) to attend a conference in Brussels in June 1991 to start negotiations on a European Energy Charter. The negotiations on the Energy Charter Treaty and the Energy Charter Protocol on energy efficiency and related environmental aspects were successfully concluded in 1994.[12] The Energy Charter Treaty entered into force on 16 April 1998.

9. In 2011, 10 411 million m^3 of natural gas was extracted from an Polish industrial reservoir.

10. The presented data come from the official reports of the Polish Geological Institute, as on 2019.04.28, that are available at the website http://www.pgi.gov.pl/.

11. See: Dz.U.UE.L.94.380.24; Dz.U.UE-sp.12-1-199.

12. See: The Energy Charter Treaty and the Energy Charter Protocol on Energy Efficiency and Related Environmental Aspects. Lisbon.1994.12.17.

Among its provisions, the promotion of cooperation between the Communities and third countries and the diversification of energy supply are among the most important demands.[13] In this phase, the Foreign Ministers of the Russian Federation, Germany, France, the Netherlands, the United Kingdom and the Russian Federation prepared the institutional framework for the creation of a common working area. The second stage, in turn, was initiated in 1994 with the signing of a Partnership and Cooperation Agreement between the Russian Federation and the European Union, which established a formal basis for contacts between them in the field of energy. In the same year, the Russian Federation also signed the Energy Charter Treaty. This agreement created a formal basis for trade between the European Union and third countries, including the Russian Federation, on the basis of transitional provisions. It regulates the principles of trading in energy carriers between members, establishes the principles of investments in this sector, formulates standards for the sale of energy products and introduces dispute resolution mechanisms.[14] In April 1998, the so-called Transit Protocol was adopted.[15] It was aimed at adapting the provisions of the Energy Charter Treaty to the principles and regulations of the World Trade Organization (WTO) (Liesen 1999).

The amendments have been ratified by 35 States Parties and provisionally applied by 10 States Parties.[16] Undoubtedly, the provisions of this international agreement were the result of demands and demands of the Russian side concerning facilitation of trade in energy carriers, including "blue fuel." Pursuant to Article 1 of the aforementioned agreement, amending Article 29 of the Energy Charter Treaty, its provisions apply to trade in energy materials and products and energy-related equipment if none of the Contracting Parties is a member of the WTO. Trade in energy materials and products and energy-related equipment between States, at least one of which is not a member of the WTO, shall be governed, by the provisions of the WTO Agreement, as applied and practiced with regard to energy materials and products and energy-related equipment, by the members of the WTO among themselves, as if all Contracting Parties were members of the WTO. An exception is made for those countries which were members of the Union of Soviet Socialist Republics. In this context, it may be regulated, subject to the provisions of Annex TFU by an agreement between two or more such States, until 1 December 1999 or until such time as that Contracting Party accedes to the WTO, whichever is the earlier.[17]

Such a solution was dictated by the Russian Federation's reservations regarding the "unequal" treatment of the Russian Federation in relation to the World Trade Organization member states. Articles 26 to 28 of the TEC provide for procedures for investor-to-state party and state party disputes. Such disputes are usually resolved by ad hoc arbitration tribunals. At least eighteen such disputes have been initiated between investors and states, two of which have been completed, two have been suspended and fourteen are still pending (Nowacki 2010).

This solution was beneficial for the Russian Federation on the grounds that it was not a part of the World Trade Organization and therefore it was able to apply favorable solutions with regard to customs duties, quotas or subsidies for its exporters. However, this situation not only did not result in more favorable cooperation, but also gave rise to a procedure under Article 45 of the Energy Charter Treaty against the Russian Federation. The ruling of the tribunal selected from the arbitrators of the Permanent Court of Arbitration in The Hague was issued on 30 November 2009. The case was brought before the court by the shareholders of Yukos, namely: Yukos Universal Ltd., Hulley Enterprises Ltd. I Veteran Petroleum Trust (the last two having their registered office in Cyprus). These shareholders held a total of more than 60% of the shares in Yukos.[18] The lawsuits were filed in February 2005 and the amount of damages claimed exceeded USD 100 billion.

13. Energy Charter Organization, https://energycharter.org/.

14. To date, the United States has not signed the Energy Charter Treaty. However, they have observer status in an organization of which 51 countries are members, including all EU Member States.

15. Final Act of the International Conference and the Decision of the Energy Charter Conference with respect to trade-related amendments to the Energy Charter Treaty (OJ L.98.252.23, OJ L.98.252, OJ EU-sp.12-2-42). It is worth noting that the agreement entered into force on 23 July 1998 and was announced only on 12 September 1998.

16. Energy Charter Organization, https://energycharter.org/.

17. Final Act of the International Conference and…, op. cit.

18. See: Hulley Enterprises Ltd. vs. Russian Federation (case AA226), Yukos Universal Ltd vs. Russian Federation (case AA227) and Veteran Petroleum Trust vs. Russian Federation (case AA228).

The complainants accused Russia of violating the provisions of the Treaty (i.e., Article 13), which prohibits nationalization or expropriation of investments unless the expropriation is made for a purpose which is in the public interest, not discriminatory in nature, is carried out in accordance with due process of law and is accompanied by the payment of immediate, adequate and effective compensation. The Court confirmed the obligation of the Russian Federation to apply the Treaty provisions and gave rise to further judicial action (Giorgetti 2010).

The re-nationalization by the former Council for Mutual Economic Assistance (GCC) of the oil and gas sector is nothing new. The disintegration of the system of the Comecon states and at the same time the states belonging to the Warsaw Pact resulted in an uncontrolled sale of assets in the form of companies responsible for the energy sector in the 1990s. In the first decade of the 21st century, the share of foreign entities in this sector in Poland, Russia and Ukraine exceeded 51%.

As far as Ukraine is concerned, this country does not have significant oil and gas resources. From the point of view of resources and extraction of hard coal, it belongs to the world's leading companies. However, coal as an energy source remains outside the boundaries of this study.[19] Ukraine, on the other hand, has an infrastructure enabling the supply of natural gas and crude oil to Poland and the European Union from Russia. Approximately 25% of the natural gas demand in all EU Member States comes from Russia. In turn, 80% of gas supplies are supplied through Ukraine. Gas and oil pipelines run through the territory of Ukraine. In the case of the gas pipeline, this is the Yamal pipeline, which supplies gas from Russian territory to Europe via Belarus and Ukraine.

The transport of more than 110 billion m^3 of gas through the territory of Ukraine demonstrates the very important position that Ukraine can fulfil in relations between the European Union and the Russian Federation. The pipeline is a very important element and instrument of both policy and a broader spectrum of international relations. Decision-makers in Brussels, Kiev and Moscow are fully aware of this fact. In order to illustrate the thesis that it is important for the European Union and Poland not only from the point of view of the economy, law, but also international law and security, the fact that the supply of natural gas through Russia to EU Member States is restricted by Ukrainian transit is a testimony to this. At the turn of December and January 2005/2006, Gazprom, the largest operator and exporter of energy carriers, terminated the provisions of the agreement with respect to Ukraine. According to the company's representatives, the reason was that the selling price of the raw material for Ukraine was too low. As a result, Gazprom cut off gas supplies to Ukraine as a result of a lack of agreement between the parties. Given that Ukraine did not have sufficient strategic energy resources to secure increased demand in winter, gas supplies to Poland, Germany, Hungary and the Czech Republic were reduced, and to a lesser extent to Austria and Italy. Ukraine has partly benefited from supplies to other customers in order to secure its market. For importers from Austria, Germany, Poland, Italy and Poland, supply fell by 32% over several days of the crisis compared to the assumed level.[20] Following negotiations between Russia and Ukraine and the setting of a satisfactory price, supplies to the EU countries have been restored.

The most difficult situation took place at the turn of 2008 and 2009, when the Russian Federation significantly reduced supplies to Ukraine. In this case, there was also a situation where natural gas supplies to EU countries were reduced as a result of the use of natural gas from the Federation by Ukraine. Serbia, Slovakia (where the disaster state was introduced due to dependence on Russian gas supplies in 100%), Hungary, Bulgaria and Austria were the most affected. Such a decision was taken by RosUkrEnergo, which also concluded a contract in 2006 for the supply of gas to PGNIG SA in the amount of 2,5 billion m^3 annually. With regard to crude oil, Ukraine has at its disposal the Druzhba pipeline, its southern part supplying mainly crude oil to EU countries, but also partly to southern Poland.[21] Oil, similarly to natural gas, is one of the basic export goods of Russia.[22]

19. See: Judgment of 2009.02.03 — Maritime Delimitation in the Black Sea (Romania vs. Ukraine); more at the website https://www.icj-cij.org/.

20. Q&A Ukraine Gas Raw BBC News, 4 January 2006.

21. Poland is also crossed by the second pipeline of the Druzhba pipeline, which runs through the territory of Belarus. The Polish section starts in Adamowo in Podlaskie Voivodship and runs to Leipzig in Germany.

22. European Refineries Supplied by the Druzhba Pipeline, https://www.cnbc.com/2019/04/25/russia-oil-germa

Trade in crude oil does not encounter such big problems as trade in natural gas. The basis for such a state of affairs should be seen in the fact that oil, in contrast to "blue fuel," may, due to its physicochemical properties, also be supplied by tankers. In opposition to natural gas, whose liquefaction requires time-consuming and expensive technology, crude oil can be loaded in its original state in ports on tankers and delivered to the manufacturer. Moreover, a kind of commercial and energy blackmail of the main player — i.e., the Russian Federation, is impossible due to the status of the countries exporting crude oil, which are members of the OPEC organization.

The problem of oil trade is also not subject to such large economic fluctuations as gas, because its price is regulated decisively by world stock exchanges and transport is independent of the transmission system.[23]

Unlike other European countries, such as Italy and Germany, which depend on gas supplies from Russia, Poland has already developed methods to diversify supplies of both gas and crude oil. In the case of Poland, in November 2018 an agreement was signed between the Polish Gaz-System and the Danish Energinet, which provides the basis for the construction of a gas pipeline under the name of Baltic Pipe. The projected construction of the gas pipeline is likely to be completed in 2022. From the end of 2022, the pipeline will be able to import 10 billion m^3 of natural gas annually from deposits on the Norwegian Shelf. Supplies via the Świnoujście gas port to Poland will be able to reach Poland with approximately 16 billion cubic meters of gas from suppliers other than the Russian Federation.[24]

In international trade, this situation creates a very good negotiating position for Poland. Diversification and independence from supplies of raw materials from Russia may result in lower purchase prices of these raw materials in the future, while at the same time reducing the costs of raw materials transmission through Ukraine.

Finally, it should also be emphasized that as part of cross-border cooperation with Ukraine, natural gas is imported to Poland as part of the local transmission line Ustiług–Zosin–Moroczyn. In 2007, 17,5 million m^3 of gas was transmitted via this line. In the future, it is proposed to increase the capacity to 0,8 billion m^3. The condition, however, is to increase production on the Ukrainian side. The objective is to increase the volume of production on the Ukrainian side.[25] This goal can undoubtedly be achieved through a Polish-Ukrainian joint venture.

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23. See: The Russo-Ukrainian gas dispute of January 2009: a comprehensive assessment. By Simon Pirani, Jonathan Stern and Katja Yafimava, Oxford Institute for Energy Studies, February 2009, NG 27, [@:] https://www.oxfordenergy.org/wpcms/wp-content/uploads/2010/11/NG27-TheRussoUkrainianGasDisputeofJanuary2009AComprehensiveAssessment-JonathanSternSimonPiraniKatjaYafimava-2009.pdf?v=f2e6e3b9bff5.

24. See: To już oficjalne. Baltic Pipe do października 2022. Published 2018.11.30, [@:] https://wiadomosci.radiozet.pl/Polska/Budowa-Baltic-Pipe-Umowa-o-budowie-gazociagu-wchodzi-w-zycie.

25. See: Gaz z Ukrainy — pojawia się i znika. News published on 24 April 2011 at http://energetykon.pl/index.php/2011/04/24/gaz-z-ukrainy-pojawia-sie-i-znika/.

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