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Energy Co-operation in the Wider Europe: Institutionalizing Interdependence

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Abstract

The EU's response to concerns about energy security is to diversify sources of supply and delivery routes. To this end it seeks to engage potential energy partners across the wider Europe in an institutionalized regime based on the norms of the internal market. This article uses regime theory to evaluate the viability of the strategy. From this perspective, the willingness of the EU's partners to make commitments to institutionalized co-operation will depend on two sets of variables: their interests in resolving the co-operation problems that arise across the energy supply chain; and the 'pull' of the EU in relation to countervailing hegemonic powers in the region. The research tests this argument by examining the co-operation interests of energy consumers, transit countries and producers, and the architecture of emerging institutions in the respective regional contexts. It finds that while energy consumers and transit countries in the EU's immediate neighbourhood are prepared to commit to binding multilateral institutions, co-operation with energy producers is constrained by asymmetries of interest and regional geopolitics, and is likely to take the form of more flexible bilateral agreements.

Introduction

Energy security has escalated in the EU agenda amid concerns over Europe's dependency on imported energy and its reliance on Russian gas. EU strategy is threefold. First, it seeks to pool the risks of import dependency by realizing its long-standing objective of a fully integrated and competitive internal market,

expanded to include new Member States and accession countries in south-eastern Europe that are particularly exposed to dependency on Russia. Second, it seeks to diversify its sources of supply by accessing the huge gas reserves of the Caspian basin and central Asia, and opening up a delivery route – the Southern Corridor – that bypasses Russia. Developing new gas fields in these regions, and constructing the proposed Nabucco pipeline to deliver the gas to Europe, involves complex logistical problems and requires massive investment. The Commission's approach is to build co-operative relations with key producer and transit countries to facilitate the requisite commercial agreements. The third strand of Commission strategy stems from its belief that, in the long term, 'markets are the best way of ensuring safe and affordable energy supplies', and that 'a wider European market will enhance security of supply throughout Europe' (Commission, 2003, p. 5; 2006a, p. 2). In developing its relations with producer and transit countries, it therefore attempts to persuade them to align their energy sectors with the internal European market, creating 'a common regulatory space with common trade, transit and environmental rules, market harmonization and integration' (Commission, 2006b, p. 16).

In pursuit of these objectives, the EU has evolved a framework of institutions for co-operation with neighbouring consumer, transit and producer countries. Recognizing that there is no single template for energy co-operation, it proposes a series of three concentric circles of co-operation (Van Aartsen, 2008). At the core of the structure is the internal EU market. A second circle consists of countries willing to integrate with the internal market via the Energy Community – a treaty-based organization embodying the EU energy *acquis*, designed primarily for the EU's neighbours in south-eastern Europe but with potential for developing into a 'pan-European energy community' (Commission, 2006b, p. 16). The third circle is made up of countries beyond the Energy Community, with more flexible partnership institutions geared to encouraging minimum legal standards and good governance.

EU energy security has attracted increasing academic attention (Youngs, 2007, 2009; Schmidt-Felzman, 2008; Haghighi, 2007), and it is recognized that external energy relations are the key to security of supply. There has been little research, however, into the institutions that the EU has created in the attempt to consolidate its relations with strategically important energy partners in the wider Europe. The present article aims to redress this neglect. It also seeks to contribute to the wider literature relating to the EU's capacity for exerting influence beyond its borders. In contrast to the dominant approach which sees the institutions of external governance largely as an extension of internal EU governance (see Lavenex, 2004, 2008), the article employs regime theory to predict the sort of institutional commitments that the EU's partners will be prepared to make. The overarching hypothesis is that institutional

commitments will depend on the co-operation needs of energy producer, transit and consumer countries, and the associated collective action problems.

I. Institutionalizing Interdependence

Regime theory seeks to explain why and under what conditions states co-operate, and the institutions they build to facilitate co-operation. From a realist perspective, states are motivated by narrow self-interest and the pursuit of power. International politics is therefore an arena of relentless competition, which can only be regulated through strategic alliances conducted in line with the balance of power through bargained diplomacy. Regime theory retains the assumption that states are self-interested, but denies that self-interest precludes co-operation. The basic condition of co-operation is interdependence. When interests are interrelated, states are vulnerable to the conduct of others, the independent pursuit of narrow self-interest is counterproductive, and there are incentives to co-operate in the pursuit of common or complementary interests. Institutions emerge in response to the need for 'principles, norms, rules and decision-making procedures' to manage the collective action problems that threaten to undermine co-operation (Keohane, 1984, p. 57). The agreement of states to participate in institutions is explained by their expected utility; the anticipation that they will help them to achieve their objectives.

The design of co-operative institutions is thus explained by the configuration of interests that motivate states to co-operate, and the functional requirements of the co-operation problem (Martin, 2001; Koremenos *et al*., 2001). Two dimensions of the problem are significant in institutional design: distribution and enforcement (see Lavenex, 2008, pp. 945–96). *Distribution* effects arise when states have divergent or asymmetrical interests in co-operation and/or where the benefits are unevenly distributed. Lavenex uses the example of migration, where the benefits of co-operation are shared unequally, between sending, transit and receiving countries. *Enforcement* problems occur where states have a common interest in co-operation, but where there are incentives to defect from agreements for short-term gain. A typical example of this type of problem is EU market liberalization (Martin, 2001, pp. 42–3). International institutions, it is argued, are shaped by the nature of the problem they are designed to solve. Distribution issues constrain co-operation, giving rise to relatively decentralized and flexible institutional arrangements (Koremenos *et al*., 2001, p. 775). Enforcement problems, on the other hand, require binding rules and centralized institutions to monitor compliance. Compliance institutions intrude into national sovereignty, and this can be an impediment to co-operation (Martin, 2001, p. 43).

Regime theory also generates expectations about the bilateral/multilateral dimension of institutional design. In general interdependence introduces incentives for multilateralism, but these might vary with the configuration of state interests and the nature of the co-operation problem. Where there are common interests in the enforcement of generalized rules, and where distributional issues are less acute, multilateral institutions can be expected to predominate (Rixen and Rohlfing, 2005, pp. 3, 22). Severe distributional issues, on the other hand, might be difficult to handle in this context, because they involve the pursuit of particularistic interests which conflict with the 'generalized principles of conduct' on which multilateral institutions are based (Ruggie, 1992, p. 571). Under these circumstances, 'multilateral norms may complicate attempts to co-operate', and a dominant power may choose instead to create an overlapping series of bilateral agreements (Martin, 2001, pp. 43–6). Where partners possess different kinds of power, it has been argued, and are vulnerable to different kinds of risk, piecemeal bilateral bargaining may be better adjusted to achieving the 'variable mix of [. . .] benefits and opportunities [. . .] the parties severally wish to achieve' (Strange, 1983, p. 353).

The introduction of power into the equation suggests that functional need alone cannot explain the emergence and design of institutionalized co-operation, and that the analysis of pan-European energy co-operation patterns must be attentive to the distribution of power across the wider Europe. Regime theory conceives of power primarily in terms of the presence or absence of hegemony. A hegemon facilitates the creation of a regime, acting as a focal point for co-operation, and persuading others to defer to its norms and institutional preferences. Ideological hegemony depends, however, on the belief of secondary states that they will benefit from the regime, and an underlying complementarity of interests (Keohane, 1984, pp. 137, 242). Co-operation in the absence of hegemony is more difficult, since a non-hegemonic regime lacks a focal point and underlying ideology.

Functional theories of international co-operation have been criticized for over-reliance on rationality. The design of international institutions, it is argued, is often less than perfectly rational, and may be subject to historical inefficiency (March and Olsen, 1989). One way of avoiding the 'functional fallacy' is to show that actors are rational, and that choices between institutions were informed by the anticipation of functional benefits (Keohane, 1984, p. 80). A second criticism is that functional theory is blind to the effects of domestic institutions and culture on orientations towards international institutions, and this article will be attentive to these effects as an intervening variable in the willingness of the EU's partners to engage in institutionalized co-operation.

II. Methods and Data

The central empirical question of this article is whether and how the EU can tie strategically important energy partners into institutionalized co-operation embodying internal market norms. From the perspectives of regime theory outlined above, the answer to this question will depend on the co-operation needs arising between energy producer, transit and consumer countries, and the characteristics of associated collective action problems. Section III of the article therefore identifies the generic co-operation problems that occur along the energy supply chain, the different ways in which they can be handled and the distribution/enforcement issues that they raise. Section IV focuses on the two variables that shape institutions in regime theory: first, the interests of the EU's partners in a co-operation regime based on EU market norms; second, the hegemonic attraction of the EU in relation to countervailing energy hegemons like Russia or China.

Sections V and VI of the article address the dependent variable; the institutions of EU energy co-operation, and the willingness of the EU's energy partners to make commitments to those institutions. Institutional variation is modelled on three dimensions:

1. Bindingness/flexibility: whether the underlying agreement is based on a treaty under international law, or merely on political commitments to co-operate; the legal status of rules and the 'slack' allowed in implementation.
2. Centralization/decentralization: are important institutional tasks like compliance monitoring or dispute settlement performed by an executive or secretariat?
3. Multilateralism/bilateralism.

On this basis three models of energy co-operation are constructed:

The Energy Community model: multilateral co-operation, based on treaty commitments to binding rules, with compliance monitoring and dispute settlement carried out by centralized institutions.
The partnership model: a hybrid of multilateralism and bilateralism, codified in relatively flexible political commitments, with decentralized and predominantly intergovernmental institutions.
Diplomacy: bilateral intergovernmental bargaining, codified in non-binding Memoranda of Understanding, with minimal or no supporting institutions.

The main hypothesis of the article is that the Energy Community model will be attractive to countries that have common interests in market integration or a stable and efficient regime for regulating the transportation of energy, and

that recognize the functional need for multilateral enforcement institutions. Where interests are more asymmetrical – as between consumer and producer countries – co-operation may be constrained by distribution problems and institutions are likely to conform to the more flexible partnership model or bilateral diplomacy.

A second hypothesis relates to the 'pull' of the EU as a regional hegemon in the face of competing hegemonic powers. A key source of power is accession conditionality – the leverage the EU is able to exert on aspirant members (Vachudova, 2005; Schimmelfennig and Sedelmeier, 2004). Countries with a perspective on accession can therefore be expected to defer to the Commission vision of a pan-European, liberal energy regime based on the institutional model of the Energy Community. CIS (Commonwealth of Independent States) countries with ties to Russia and its energy empire may seek to redress their dependency by deepening their relations with the EU, but are likely to prefer less committing institutional arrangements.

Country selection is sensitive to both functional need and regional power distributions. Co-operation needs will vary between consumer, transit and producer countries, so selection was made to include consumers in south-eastern Europe (Romania, Croatia and Serbia) and the Mediterranean (Morocco); transit countries (Turkey, Egypt and Azerbaijan); and producers (Algeria, Turkmenistan; Egypt and Azerbaijan are also modest producers). Selection is also sensitive to the regional power variable. The countries of south-eastern Europe and Turkey have accession perspectives, Mediterranean countries have long-standing association agreements with the EU, while Azerbaijan and Turkmenistan are CIS countries subject to Russian influence.

Research is based, first, on interviews with 24 senior officials in the EU Commission and national ministries and regulatory authorities.[1] All had close involvement in the institutions of energy co-operation. Interviews were designed to identify the interests of the EU's partners in institutionalized co-operation, and to evaluate their readiness to make commitments to the obligations involved in the respective models of co-operation. Interviews were triangulated against each other, and against data from EU documentation, the specialist trade press and the regional intelligence bulletins. Where interview access was restricted, the research relied exclusively on the latter.

[1] European Commission (DG Transport and Energy, and DG External Relations); Energy Community Secretariat; European Investment Bank; UK Department of Business Enterprise and Regulatory Reform; European Federation of Energy Traders; the regulatory authorities of Austria, Croatia, Romania, Serbia and Egypt; the energy/economics ministries of Croatia, Romania, Serbia and Morocco; Ministry of Foreign Affairs, Egypt; Ministry of Petroleum, Egypt.

III. Co-operation Needs across the Energy Supply Chain

Interdependence between energy producers, transporters and consumers provides strong functional need for co-operation (Haghighi, 2007, pp. 1–2). Generating electricity or extracting gas, and transporting it to the point of consumption, requires intensive co-operation in large-scale, long-term investment. The central problem revolves around creating a stable framework to satisfy the security needs of consumers and producers, and to handle the inherent investment risk (Youngs, 2009, pp. 6–10; Correljé and Van der Linde, 2006; Stern, 1998, 2001).

There is, however, disagreement over how to structure commercial energy relations between advocates of market and non-market forms of contracting. The former argue that the optimal way of satisfying the security needs of both consumers and producers is through the international market. The latter point to the inherent limitations of energy markets, particularly in natural gas. Sources of supply are often remote from the point of consumption, requiring the construction of a dedicated pipeline. Pipeline projects are not commercially viable until producers make contractual commitments to supply the gas, and energy companies in the consumer country make similar commitments to purchase it. Pipelines may not be re-deployable if the underlying supply agreement breaks down. Relations between producers, transporters and suppliers thus require a high level of trust and commitment (CERA, 2007, p. I-7). These commitment needs, they argue, are best met by the tried and tested model of long-term, oligopolistic, bilateral agreements between producer states, consumer governments and national champions (Youngs, 2009, p. 6). Electricity is more amenable to the market model. Power generation is more mobile and can be located in proximity to consumption. It is easily transported across the grid infrastructure, so a generator is less dependent on a particular purchaser. Long-term contracting is less pervasive and transnational market liberalization less onerous, so the conflicts between the two are less intensive.

Market liberalization poses a direct challenge to long-term contracting, because it entails the break-up of oligopoly relations between producers and suppliers, and prohibits agreements that foreclose markets. It also entails a shift in the allocation of the risks arising from changes in demand and price fluctuation. Long-term bilateral agreements often include ‘take-or-pay’ clauses by which the buyer undertakes to purchase an agreed volume of gas for a fixed period of time at an agreed price (Haghighi, 2007, pp. 20–4). The purchaser thereby assumes the risk, while the supplier is guaranteed security of demand. Market liberalization thus alters the allocation of risk to the disadvantage of producers (CERA, 2007, p. I-7; CIEP, 2004, p. 131) and they

have resisted its incursions into the international energy economy. Conflicts between market and non-market principles constitute a classic distribution problem standing in the way of the emergence of an international energy regime.

These two forms of commercial relations generate distinctive co-operation needs. In market-making the main co-operation problem lies in co-ordinating and harmonizing rules about the break-up of vertically integrated monopolies, open access to pipelines and wires, and transparent and equitable terms of transit. There is considerable potential for countries to defect from agreements by bending the rules to give 'national champions' hidden privileges. Solving this enforcement problem requires common standards of governance and regulation, applied by multilateral regulatory institutions (Youngs, 2009, p. 8). Long-term bilateral deals between oligopolistic energy companies, on the other hand, require a different form of institutional facilitation. Commercial partners seek reassurance about the stability of the underlying political relationship, and this can be provided by strategic bilateral alliances concluded through energy diplomacy.

IV. Interests in Energy Co-operation

In regime theory, the choices that states make about the design of co-operative institutions depend on the interests that they have in co-operation, and the specific characteristics of the problems that motivate them to co-operate. The previous section of the article highlighted the co-operation problems that arise in the energy sectors, and the alternative approaches to resolving them. This section examines the way in which the EU's energy partners in south-eastern Europe, the Mediterranean and the Caspian Basin perceive these problems, and how they conceive their interests in the alternative models of co-operation.

South-East European Interests

As energy consumers, the countries of south-eastern Europe share the EU's security of supply concerns and have a common interest in market integration. Most of the countries in the region have an import dependency of more than 40 per cent, and four countries are more than 80 per cent dependent on natural gas imports from Russia. Governments in the region recognize the benefits of a large regional market in promoting investment in new capacity, and diversifying energy sources. Market liberalization also fits well with beliefs of domestic actors in the efficiency gains to be derived from exposing inefficient state enterprises to competition. Interviews revealed a pervasive consensus

among national officials about the need for a uniform regulatory and legislative framework across the region, and a recognition that this requires multilateral co-operation with institutions geared to solving the attendant enforcement problems (interviews).

Alongside functional interests in the Energy Community model, the countries of south-eastern Europe had wider interests in co-operation as a step towards accession. Although Community membership was not initially a condition of accession, treaty negotiations took place in the 'general atmosphere' of accession (interviews). Participation demonstrated a commitment to EU membership, helped to prepare countries to meet accession requirements and offered opportunities to learn the EU system (interviews). Access to financial assistance was also an important incentive for Energy Community participation. Membership conferred a 'badge of approval' enabling countries to bypass the conditions attached to loans (interview).

Turkey's interests in energy co-operation are more complex than its neighbours across the Bosphorus. Strategically located at the intersection of oil and gas transit routes between central Asia, Russia and Europe, it holds the key to the regional energy economy. It has sought to maximize the economic benefits by balancing relations with Brussels and Moscow, participating in both the EU's Southern Corridor project and Russia's rival South Stream pipeline. The balancing act is difficult to reconcile with Turkey's aspirations to EU accession. Moreover, while energy co-operation with the EU could go hand in hand with accession, the two agendas have tended to derail each other. Turkey has played 'hard to get' in energy co-operation in order to retain its leverage in accession negotiations, and the EU has resisted its blackmail strategy. In the longer term, however, EU interests in energy co-operation and Turkish aspirations for accession are complementary, and there are already indications of a more conciliatory approach in Ankara. Turkey also has a functional interest in co-operation, since integration with European markets would serve its aspiration to become a regional energy trading hub.

Mediterranean Interests

The interests of the southern Mediterranean energy producers conflict with EU interests in competitive markets. Where economies are heavily reliant on revenues from energy exports, the state has a strong interest in keeping control either through state ownership or by ensuring that ownership rests with 'insiders' (Van der Meulen, 2009, p. 849). State ownership is the norm, and market liberalization threatens the privileges accorded to the state enterprises that dominate energy extraction and supply. Moreover, the bilateral supply agreements that have predominated in the gas sector enable producers

to control their export markets, and to guarantee security of demand, and these may also be threatened by liberalization.

Algeria relies on European markets for around 95 per cent of natural gas exports, so it has a strong interest in co-operative interdependence with the EU. Historically, exports have taken the form of wholesale supply agreements with European companies, but the state-owned gas company Sonatrach now aspires to enter *retail* markets via joint ventures with Eon Ruhrgas and Gaz de France. This intensifies interdependence, raising issues of reciprocity (access to downstream European markets in return for easier access for European operators to upstream development in Algeria) (Stein, 2008, pp. 103–5). At the same time, however, it seeks to diversify its energy relations through co-operation with Gazprom and other Russian companies, and is also one of the most active members of the GECF (Gas Exporting Countries Forum) which some see as a potential gas OPEC (Organization of the Petroleum-Exporting Countries) (Darbouche, 2007). Its orientation towards the EU is therefore to balance co-operation with a determination to maintain its energy autonomy. There is also an underlying conflict between EU market liberalization and Algerian preferences for long-term take-or-pay contracting (Haghighi, 2007, p. 24).

Recent discoveries have set Egypt on the way to becoming a medium-volume producer of natural gas, and it has a strong interest in accessing European markets. Egypt has a long-term commitment to liberalization, but the domestic market remains underdeveloped, and 'different market dynamics' limit the potential for integration with the European market under EU rules (interview). It remains concerned, however, about the security of European demand. In particular it seeks long-term assurance that recent EU interest in co-operation is more than merely a temporary effect of the downturn in EU–Russia energy relations.

While neither Algeria nor Egypt has an interest in integration with the internal EU market, both have interests in sub-regional market integration. Egypt co-operates with the EU in a project for an Arab gas pipeline with potential to reach Turkey, and thereby connect to Europe via the Southern Corridor. The project is also linked to the creation of a Euro-Mashreq gas market, and Egypt has recognized the utility of the EU's legal and regulatory model for providing the institutional template (interview). Algeria accepts a similar logic in electricity, and is a central participant in a project to create a Euro-Maghreb power market with potential for increasing its exports to southern Europe. At the same time, however, it has vetoed proposals for creating a Maghreb gas market (interview).

While energy producers are ambivalent to integration with the EU market, consumer countries have a strong interest in integration. Almost entirely

dependent on imported gas, Morocco is a strong supporter of extending the Mashreq gas market project to the Maghreb. It also has a persuasive interest in power market integration, both to mitigate its present import dependency, and to help realize its aspiration to develop green (primarily wind-generated) electricity for export to Europe (interview).

Except when it suits their interests in sub-regional market integration, then, the Mediterranean producers see little functional need for multilateral institutions of market governance. Nor can the countries of the region be persuaded to defer to EU norms by the allure of EU accession, since only Morocco has distant aspirations to membership. Association agreements under the umbrella of the ENP (European neighbourhood policy) provide collateral benefits in the form of financial assistance to the region, but the scale is relatively modest. An attempt has been made in the ENP to replicate forms of accession conditionality that have proved successful in central and eastern Europe by offering new forms of enhanced co-operation, conditional upon commitment to common values and the implementation of agreed priorities (Commission, 2007; see also Commission, 2003, 2004). Enhanced co-operation, however, remains too ill-defined to serve as an incentive to align with EU energy norms. Algeria has explicitly rejected the concept, and only Morocco has shown significant interest in upgrading its status in the ENP (Darbouche, 2008, p. 372).

Caspian/Central Asian Interests

The countries of the Caspian Basin all have large-scale natural gas resources, and they are therefore central to the EU's strategy of energy diversification. As CIS countries, however, they are subject to Russia's regional hegemony, and this is reinforced by the energy infrastructure – gas transit routes go mainly via Russia, and Gazprom accounts for virtually all their exports (CASE, 2008). Russia has exploited its 'energy satellites' ruthlessly, imposing sub-market prices, and although it sweetened the deals once the EU began to show an interest in the region, it has failed to meet the aspirations of the CIS countries for energy independence (Overland, 2009). Consequently, the latter have developed strategies of market diversification, and therefore have an interest in developing transit routes to European markets bypassing Russia. Since this is contingent upon constructing a Trans-Caspian pipeline, however, the interest is essentially long-term.

The foremost gas producer is Turkmenistan, already a major exporter, with the fourth-largest reserves in the world. Although Russia is its principal energy partner, potential gas transit routes run in all directions, and a pipeline to China is nearing completion. Ashgabat's multi-vector foreign policy

reflects the energy map (Overland, 2009), but perennial gas disputes with Russia underline the importance of openness to co-operation with Europe, and Turkmenistan has pledged to supply gas to Nabucco in the event of its realization.

Azerbaijan has been the most consistent of the CIS countries in asserting its energy independence from Russia and engaging with Europe and the US (Kjaernet, 2009). It thus has strong interests in developing its potential as a hydrocarbon corridor to the west. It already exports a significant volume of oil to the west via the Baku–Tblisi–Ceyhan pipeline, financed through a partnership with European oil companies. It has the potential to serve as the main transit route for central Asian gas to the EU's Southern Corridor and – while only a modest producer – was the first country to commit gas supplies to the Nabucco project.

For all the Caspian and central Asian countries, however, interests in co-operation are constrained by a mismatch between the liberal market norms of the EU regime and domestic energy sectors characterized by the accumulation of ownership, policy-making and regulatory functions in the hands of the state. More generally, relations with the EU are also inhibited by the incongruence between the human rights norms of the EU and the profoundly authoritarian nature of domestic regimes in the region. The ratification of Turkmenistan's Partnership and Co-operation Agreement has been stalled for a decade by human rights issues. With its energy export options, it may be concluded, it has little need to adopt EU norms that intrude into the domestic regime.

V. The Institutions of External Energy Governance

Regime theory suggests that the design of pan-European energy institutions will reflect the interests and co-operation needs of the partners, and/or the capacity of a hegemonic power to persuade secondary states to defer to its institutional preferences. It predicts that energy consumer countries with common interests in market solutions to their security of supply problems will be inclined towards binding multilateral institutions geared to mitigating the enforcement problems that arise in competitive energy markets. By contrast, while interdependence with the EU gives energy producers an incentive for co-operation, conflicts of interest over how to structure relations across the supply chain will create distribution problems that constrain the scope for co-operation. Testing these expectations involves first defining the alternative institutional designs available to the EU's interlocutors, and that is the purpose of this section of the article.

The Energy Community

The Energy Community is a multilateral organization ingeniously designed to bind non-Member States to EU law without admitting them to EU institutions. Its legal basis is the TEEnC (Treaty Establishing the Energy Community), an agreement under international law, and an integral part of the EC legal system. As such, it is thus legally binding on both Energy Community members and the EC itself. Its objective is to 'organise relations between the Parties and create a legal and economic framework in relation to [. . .] the electricity and gas sectors' (TEEnC, Art. 2), and it commits the signatories to adopting and implementing 14 acts of EU secondary legislation relating to energy, the environment and competition. Majority voting in many areas of the treaty means that Member States can be bound by decisions to which they have not consented.

Since the TEEnC forms an integral part of the EC legal system, it may be directly effective in conferring rights that can be relied upon in domestic courts. If an action for infraction of the treaty was referred by a domestic court to the ECJ (European Court of Justice) it would be for the Court to establish direct effect. Energy Community practitioners are divided on the issue. While some believe the Treaty could be held to be directly effective (interview), others believe in a broader application: 'it would lead to chaos in the economies of the Balkans if it was applied directly' (interview). At present, then, Energy Community commitments fall short of hard law, although there may be some potential for rules to 'harden' over time.

The structure of the Energy Community is quite highly centralized, resembling the EU itself. The main decision-making body is the Ministerial Council, supported by a Permanent High Level Group of officials. Executive functions are carried out by a Secretariat that monitors Treaty compliance and implementation, and has powers to propose measures to the Ministerial Council. These powers endow the Secretariat with the potential for 'driving' the Community. While some national officials would like the Secretariat to exploit its potential more fully (interview), others express concerns that it is too assertive and 'acting like the Commission' (interview). Alongside the quasi-hierarchical institutional apparatus of the Energy Community are institutions designed to promote an exchange of best practice: the ECRG (Energy Community regulatory group) and the Athens and Maribor forums of energy sector stakeholders. While there is some evidence that the regulators' group is effective in generating regulatory convergence through socialization, the forums are generally dismissed as purveyors of 'paper-ware' or 'subsidized tourism' (interviews).

The compliance mechanisms of the Energy Community are relatively weak. Infringement proceedings are conducted by the Secretariat and, failing resolution, cases are referred to the Council. Sanctions against non-compliance are blunt, and there is no legal remedy. Compliance mechanisms thus rely heavily on political pressure exercised in the Ministerial Council. Since few Member States are wholly compliant with Treaty obligations this kind of peer pressure is generally ineffective. One way of intensifying the political pressure is for the Commission to play a more activist role in enforcement, but its strategy tends to be one of consensus building rather than 'cracking the legal whip' (interviews). A second compliance mechanism operates through accession conditionality. Compliance with the *acquis* is a condition of accession and non-compliance can be 'punished' by the Commission suspending the accession process. However, the Commission often has other priorities in accession negotiations, and may thus turn a blind eye to compliance failures in energy in return for compliance in priority areas (interview).

The Partnership Model

The 'partnership model' is based on the ENP, a multilayered system of comprehensive bilateral agreements, concerted through multilateral institutional arrangements operating for the most part on the basis of political commitments rather than binding rules. The prototype was the EMP (Euro-Mediterranean Partnership) in which energy was merely one of six 'priority areas' within the wider relationship. More recently, however, energy security has become the 'driver' of the ENP, with new partnerships designed specifically to upgrade energy relations with key producer or transit countries. Recent initiatives include the Eastern Partnership with transit countries in the Southern Caucasus, a framework of co-operation with the littoral states of the Black and Caspian Seas, and the EU–Central Asia strategy. The particularities of these arrangements vary, and only the Eastern Partnership is formally part of the ENP. However, they embody a common set of institutional principles comprising the partnership model.

The structure is a hybrid of bilateralism and multilateralism. The contractual basis of the bilateral relationship is the AAs (Association Agreements) or PCA (Partnership and Co-operation Agreement). Each agreement has an institutional apparatus in the form of an Association Council (of foreign ministers), a supporting committee (of high officials) and technical sub-committees for the different chapters of the agreements, but the energy sub-committees are relatively recent and have not yet progressed beyond procedural matters (interview).

Multilateral activity is highly decentralized, operating at three levels. First, co-operation is steered by intergovernmental conferences of foreign and/or energy ministers that agree objectives. Energy minister conferences are envisaged biennially although in practice they tend to be less frequent. Unlike the Energy Community, there is no secretariat to sustain the process between ministerial conferences. Second, more routine exchange occurs in forums or working groups of ministry officials and experts. Some of these groups are merely convened ad hoc to prepare the ground for ministerial conferences, but others are standing groups meeting every six months or so on particular themes like market convergence or renewable energies. Regional groups of energy sector regulators are also starting to emerge, geared to regional regulatory convergence and knowledge exchange. A third form of multilateral co-operation occurs around flagship projects of common interest, institutionalized in 'co-operation centres' located in the region and supported by EU financial assistance. This form of technical co-operation 'on the ground' generates concrete outputs demonstrating tangible benefits for the participants (interviews).

Unlike the Energy Community, the partnership model has no treaty foundation and no legal code. It operates instead on the basis of declarations of intent to co-operate, statements of agreed priorities and action plans or 'roadmaps' for 'legislative and regulatory approximation' and 'convergence with EU policy objectives' (Commission, 2004, p. 15), but they stop short of incorporating specific parts of the *acquis*. Moreover, compliance mechanisms are weak. Action plan commitments are too broad to serve as benchmarks against which to evaluate implementation. The EU attempts to make financial assistance conditional on progress towards implementing agreed policy objectives, but assistance is only loosely tied to implementation so conditionality lacks credibility.

Bilateral Diplomacy

Since 2006 Commission President Barroso, external and energy Commissioners Ferrero-Waldner and Piebalgs, and foreign policy representative Solana have been hyperactive in shuttle diplomacy with the central Asian gas producers and key transit countries along the Southern Corridor. The underlying purpose is to create 'mutually beneficial partnerships' along the gas supply chain, based on joint commitments to a transparent and equitable legal and regulatory framework. Agreements take the form of bilateral MoUs (Memoranda of Understanding) or plurilateral intergovernmental agreements designed to underpin commercial contracts by reducing political risk. The terms vary with the status of the participants and their willingness to make

commitments. Some are little more than declarations of intent to co-operate in the pursuit of common objectives. Others go much further in defining the scope of the co-operation, the incentives offered by the EU (financial and technical assistance) and commitments in terms of market integration and the creation of market institutions, and some go so far as to include commitments to elements of the energy *acquis*.

Parallel to bilateral diplomacy, there has been a trend towards plurilateral summits designed to consolidate political support for Southern Corridor infrastructure projects. Activity culminated in 2009 in the Budapest, Sofia and Prague summits, the latter concluding in the Southern Corridor Declaration of commitment to the Nabucco project, determination to overcome 'commercial and non-commercial problems' and intent to create the requisite legal and regulatory structures. While declaratory diplomacy does not resolve the many commercial and logistical issues surrounding Nabucco, it may provide political 'comfort' to the commercial partners in the project. The Commission regards the agreement as a 'synergy' of previous activity in energy partnerships and diplomacy, and a vindication of 'the EU method'. Significantly, it was followed shortly by an Inter-Governmental Agreement between the EU partners in the Nabucco consortium and Turkey, resolving the legal and regulatory issues standing in the way of the project.

VI. Participation and Commitment

With common interests in market integration, the energy consumer countries of south-eastern Europe (Albania, Bosnia-Herzegovina, Bulgaria, Croatia, FYR Macedonia, Montenegro, Romania, Serbia and Kosovo) readily accepted the Energy Community model of binding multilateral institutions geared to resolving the enforcement problems that accompany market-making. Moreover, all these countries have a perspective on EU membership, so the Commission was able to able to mobilize accession incentives to persuade governments to buy into its vision of a wider-European energy regime. Consequently, treaty negotiations were relatively problem-free – they were concluded within a year. Ukraine and Moldova gained accession in 2009 (conditional on meeting the terms of the EU *acquis* in gas).

Having been a central player in negotiations, Turkey resisted signing the treaty. This was part of a strategy for using its pivotal role on the EU's corridor to central Asia as a bargaining chip in accession. The reversal of this posture in opening negotiations for Energy Community accession in 2009

was recognition that co-operation served its EU accession aspirations better than intransigence. It was also evident that co-operation was a prerequisite for the realization of the Nabucco project, without which its potential as a transit country would remain hypothetical.

Despite the generally favourable climate for co-operation, however, Energy Community participants seek to retain sufficient flexibility to allow each country 'to choose its own path to liberalization' (interview). The need for flexibility is particularly marked in natural gas, where there are conflicting interests in market and non-market forms of contracting. Here there is a general preference for a 'light-handed' application of the *acquis*, allowing exemptions from market principles for long-term contracts that often underpin pipeline investment (Energy Community, 2006). Flexibility also allows Bulgaria and Serbia to reconcile their gas market commitments with energy partnerships with Russia on which they continue to rely (interviews). A flexible interpretation of the *acquis* thus sidesteps some of the distribution problems involved in gas co-operation.

The Energy Community model has limited potential beyond the consumer countries of south-eastern Europe and neighbouring transit countries that have long-term EU accession aspirations. Energy producers resist participation in binding forms of multilateral co-operation that constrain their energy sovereignty. They can, however, be persuaded to participate in the more flexible partnership model. Indeed, all the main producer and transit countries in the wider Europe participate in this type of co-operation:

- Euro-Mediterranean Energy Partnership (Algeria, Egypt, Israel, Jordan, Lebanon, Libya (Observer), Mauritania, Morocco, Palestinian Authority, Syria and Tunisia);
- Eastern Partnership (Armenia, Azerbaijan, Georgia, Moldova, Ukraine and Belarus);
- Black and Caspian Seas Energy Co-operation (Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Tajikistan, Turkey, Ukraine and Uzbekistan);
- The EU–Central Asia Strategy (Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan).

Commitment to partnership institutions, however, is subject to wide cross-national variation. Algeria resists making commitments even to the more flexible model of partnership. It has yet to conclude an action plan under its association agreement, and has 'rejected the whole edifice of [EU] governance norms' (Youngs, 2007, p. 9). Its preferred mode of co-operation with the EU is one of bilateral 'dialogue and consultation' around 'mutual interests' (Khelil, 2003). The government proposed institutionalizing dialogue in

the form of an MoU, but although the Commission took up the initiative, agreement has proved elusive (Darbouche, 2008, pp. 371–83). As an emerging gas producer, Egypt has an interest in predictable interdependence with the EU, but has limited interests in market integration, and therefore prefers more flexible forms of partnership geared to dialogue and 'an exchange of data about supply and demand'. It has a strong preference for tailor-made forms of bilateral partnership that can be 'more advanced than regional forums operating at the level of the lowest common denominator' (interview). Morocco is the only Mediterranean country in this study with an interest in strengthening the multilateral dimension of the Mediterranean energy partnership (interview).

It remains to be seen whether the Eastern Partnership can develop a stronger platform of co-operation than its Mediterranean counterpart. The partners have a shared interest in a legal and regulatory regime to enhance their reputation as reliable energy carriers. Moreover the partnership offers the prospects of extensive collateral benefits including enhanced trade co-operation, visa-free travel and €600 million in financial assistance. A year after its launch, however, the partnership had yet to take shape. Further east, the EU–Central Asia Strategy resembles little more than a marriage of convenience.

Diplomacy may be the weakest form of co-ordination, but it has the potential to engage partners beyond the EU's traditional spheres of influence. The EU now has energy MoUs with Azerbaijan, Egypt, Jordan, Kazakhstan, Morocco, Turkmenistan and Ukraine. Dialogue does not equate with influence, however, and commitments vary quite widely. Relations with Turkmenistan have until recently been constrained by its energy ties to Russia and – after years of isolationism – the absence of a culture of dialogue. Ashgabat was slow to respond to EU overtures, and the 2008 MoU is minimalist in its commitments. The terms of engagement changed dramatically in 2009, however, when Gazprom reneged on a gas price deal, unilaterally shutting down delivery at the border and causing a major pipeline explosion. The incident precipitated an immediate diplomatic shift, with the Turkmen president distancing himself from Moscow and heralding the need to 'create a new system of relations with Europe'.

By contrast, Azerbaijan's consistent strategy of energy independence from Moscow has meant that it has been much more open to institutionalized co-operation with the EU. Its MoU contains a commitment to market integration with the EU, and alignment to parts of the energy *acquis*. It played a large part in initiating co-operation among the littoral states of the Black and Caspian Seas (the Baku initiative), and was a key player in the 2009 Southern Corridor agreement.

Conclusions

This article set out to ask whether the EU can tie its energy partners in the wider Europe into meaningful institutional co-operation, and to explore the type of institution in which they can be persuaded to participate. The answer to the first part of the question is in the affirmative, but with a caveat. Although the core Energy Community participants are the consumer countries of south-eastern Europe, it has attracted countries – Ukraine, Turkey and Georgia – lying on Europe's strategic energy routes. The Community thus has the potential to constitute a pan-European energy *transit* regime, based on the norms of the internal EU market. To be sure, the research has revealed uncertainties over the robustness of its compliance mechanisms and the status of the Energy Community *acquis*. These are understandable, however, in terms of Martin's (2001) observation noted earlier in the article that compliance mechanisms intrude into national sovereignty and can impede institutionalized co-operation. A degree of flexibility allows underdeveloped energy economies wriggle-room to adapt to the disciplines of the internal EU market, and may have served to facilitate the Energy Community agreement.

With the possible exception of Azerbaijan, however, there seems little prospect of attracting gas producers in the Mediterranean, Caspian Basin and – still less – central Asia to participate in the Energy Community model of co-operation. These countries can be persuaded by the prospects of collateral benefits – trade expansion and visa-free travel – to engage in the partnership model of co-operation, but in the absence of credible commitments and compliance mechanisms, the model falls short of a regime in the accepted sense of the term. For these countries, piecemeal bilateral diplomacy is the most productive model of co-operation: it meets the institutional preferences of the producer countries, and has also yielded tangible returns in the form of agreement that provide a political foundation for the commercial deals required to realize Nabucco. Bilateralism, however, also has its limitations: its high transaction costs, and the difficulty of sustaining it over the long term.

The article has shown evidence supporting the hypothesis that commitment to co-operation with institutions reflects a rational calculation of the anticipated benefits, and that these will differ between energy consumers, carriers and producers. Thus the south-eastern European countries perceive the benefits of the Energy Community model as a way of solving the enforcement problems associated with market integration and the ultimate benefit of large markets for security of supply. Transit countries like Ukraine and Turkey have an interest in a rule-based regime to enhance their predictability

and reliability as energy carriers. These countries thus share common interests in the Commission's vision of a pan-European energy regime and are therefore prepared to accept the associated obligations. The *asymmetries* of interests and power between the EU and producer countries in the Mediterranean and Caspian regions and central Asia are less conducive to multilateral co-operation. In Strange's (1983) terms, flexible bilateralism is more attuned to the 'variable mix of benefits and opportunities' that the partners wish to achieve.

Geopolitics clearly plays a role in shaping regime formation. Participation in the Energy Community is motivated in part by the 'pull' of the EU as a regional hegemon and the allure of accession. Covariation between accession incentives and functional co-operation need makes it difficult to separate the two effects. Consumer and transit countries with the strongest interests in the Energy Community model also have perspectives on EU membership. The readiness of Ukraine and Turkey to participate in the Community despite the uncertainties of their accession prospects, however, suggests that functional need operates independently of accession incentives. The participation of countries without accession aspirations in the EU–Maghreb electricity market and EU–Mashreq gas markets points to a similar conclusion.

For the countries in the Caspian Basin and central Asia, commitments to an EU energy regime are heavily dependent on foreign policy towards Russia. Gazprom's capricious behaviour towards its erstwhile clients means that energy relations are inherently unstable. Regional geopolitics are not conducive to multilateralism, further reinforcing the logic of bilateral diplomacy. Moreover, for these countries an EU regime of liberal market norms challenges the concentration of state ownership and control over the energy sector. Domestic institutions, it must be conceded, are an intervening variable in the relationship between functional need and commitment to EU-led co-operation institutions.

A final question, which this article has not addressed, relates to the *effects* of the emerging EU energy regime on the domestic energy sectors, and the behaviour of energy companies in the partner countries. Institutionalist theory suggests that institutions shape behaviour, but that influence depends on institutional density – the thicker the institutions the stronger the influence. From this perspective the influence of EU energy norms outside the confines of the Energy Community can be expected to be severely limited by the weakness of the institutional architecture. There is, however, little or no research into the capacity of the EU to Europeanize energy in the wider Europe, and this must be high on the energy policy research agenda.

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