

# Gas transit risks in Ukraine: political and legal dimensions

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# Transit risks in Ukraine have been significantly rising over last years and especially after 2014

- Physical security of the transit system may not meet a “stress-test” of increased utilization without huge investments: around 8 bln. USD for 7-10 years
- Political unpredictability and “frozen” military operations in the country
- Accidents on pipelines and other strategic energy infrastructure objects
- Enactment of Law authorizing Ukrainian Security Council to cease at its discretion transit of Russian gas through Ukraine
- Multibillion arbitration cases between Gazprom and Naftogaz on supply and transit issues

# **Transit risks in Ukraine have been significantly rising over last years and especially after 2014 (cont.)**

- Administrative acts of Ukraine aimed at unilateral (outside arbitration) increase of gas transit tariff 1,5 times as compared to contractually agreed tariff
- Imposition by Ukrainian antimonopoly committee of 3,4 bln. USD fine on Gazprom for alleged abuse of dominance on “Ukrainian market of gas transit services” (which Gazprom has never rendered but only received).
- Lack of trust between the parties which narrows prospects of mutually acceptable decision by the end of 2019 when the current transit contract ends.

# **Russian approach to the transit risks: diversification of gas transportation routes**

Efforts to build new gas pipeline routes directed both at South-East and North-West of Europe:

- Nord Stream 1 was put into operation in 2011-2012
- South Stream was completely ready for construction by 2014
- Nord Stream 2 was initiated in 2015 by signing the shareholders agreement
- TurkStream was initiated in 2016 by signing the Intergovernmental agreement on October 10, 2016

# EU approach to new “Russian” pipeline projects

- European Energy Security Strategy (May 2014): “the most pressing energy security of supply issue is the strong dependence from a single external supplier” (only Russia is mentioned as such supplier)
- European Council (December 2015): “new infrastructure should comply with...EU legislation” and “objectives of the Energy Union”
- What are the objectives of the Energy Union and who defines them?

# EU approach to new “Russian” pipeline projects (cont.)

- The European Commission:
  - Called for “suspension” of South Stream Project and its “re-evaluation in light of the EU’s energy security priorities” (May 2014) and triggered such suspension by a “letter of formal notice” sent to Bulgaria (June 2014)
  - Suspended approval of Settlement agreement on OPAL of 2013 = prevented full utilization of Nord Stream 1
  - DG Energy claimed applicability of the Third Energy Package to Nord Stream 2 = questioned its current corporate structure
- Several high-ranked officials of the EU made public statements against Nord-Stream-2 alleging that it is not in line with “Energy Union objectives” (M. Sefcovic) and with “energy security requirements” (D. Tusk)

# EU: transit of Russian gas through Ukraine should continue post-2019

- European Commission: Ukraine should remain an “important transit state” (State of the Energy Union Report, November 18, 2015).
- Vice-President of the European Commission for the Energy Union: “if the aim of [Russian projects] is... [exclusion of] Ukrainian transit route, they are not acceptable to the EU” (July, 2015).
- Whether and how this approach correlates with the objective of security of gas supply to the EU?

# Legal approach: shall transit risks be shared between supplier and customers?

- ▶ Art. 79 (1) of Vienna Convention on Contracts for the International Sale of Goods 1980: “A party is not liable for a failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control and that he could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract or to have avoided or overcome it, or its consequences”
- ▶ CISG Advisory Council: “change of circumstances that could not reasonably be expected to have been taken into account, rendering performance excessively onerous (“hardship”), may qualify as an “impediment” under Article 79(1)” (Opinion No. 7)
- ▶ If unforeseen transit risks (including sharp increase of transit fees) render performance of gas supplier’s contractual obligations excessively onerous and qualifies as an impediment:
  - ▶ the supplier may be relieved from liability
  - ▶ revision of gas supply contracts may be triggered to restore balance of interests of the parties
- ▶ Therefore the Russian gas supplier should not be considered as the only taker of Ukrainian transit risks – they are shared with EU customers

## Conclusions

- ▶ Pipeline projects supported by market and compliant with law should not be hampered by political considerations
- ▶ Discussion of means to fairly allocate and mitigate transit risks should be held without delay in an open manner between all interested parties

**THANK YOU!**