



Making Association Work: Achievements in and obstacles to reforms in energy, transport and environment

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Introduction¹

The Association Agreements (AA) concluded between the EU and the three Eastern Partnership countries — namely Ukraine, Moldova and Georgia — are amongst the most comprehensive and detailed agreements the EU has concluded with any third country. Crucially, they are very ambitious in terms of law harmonization. The three associated countries have committed themselves to adopting a substantial part of the EU's rules — the so-called *acquis communautaire*.

However, the scope and depth of reforms required from the associated countries is at odds with their current level of socio-economic development. While the EU expects the AA to serve as a blueprint for the modernization of Georgia, Moldova and Ukraine, the relevance of its *acquis* to their needs is to a large extent questionable.

This policy brief discusses the key issues faced by the partner countries in conducting domestic change (defined here as transposition and implementation of EU rules) in response to the AAs in the energy, environment and transport sectors. With the Deep and Comprehensive Free Trade Areas (DCFTAs) and visa liberalization, the EU offers clear rewards in exchange for massive reforms (in the form of easier market access and people mobility, respectively). In contrast to trade and mobility, such tangible rewards are largely absent in the energy, transport and environment sectors. Therefore, we ask whether the EU's promise of modernization through the *acquis* has proven effective to entice the three associated countries into wide-ranging policy change in these sectors.

Evidence and analysis

Our research has sought to identify the conditions for a successful transfer of the EU's rules in the areas of transport, environment and energy. We assumed (i) that in these areas there are fewer external benefits to implement EU rules compared to the areas of trade and mobility, and (ii) that the adoption of these rules crucially hinges on their direct relevance to the governments of associated countries. In exchange for their efforts of law harmonization in trade and visa related matters, the associated countries were rewarded by better access to the EU's market and a visa-free regime for their citizens. These rewards entailed political benefits for the elites as well, also in terms of electoral success, given the strong support expressed by citizens for enhanced mobility to the EU for instance. The picture differs for transport, environment and energy. While harmonization in some of these areas can be rewarded by better connectivity to the EU (as indicated in the Eastern Partnership 2020 deliverables), such external rewards are limited for now. Therefore, in order for associated countries to reform, either the direct relevance of these rules should be made more pronounced, or the EU's rewards should be bigger.

Importantly, adopting rules related to the *acquis* in transport, energy and environment sectors is not at the core of associated governments' priorities. While AA commitments are mentioned in government programs, the national development policy of associated countries is centred on basic market and rule-of-law reforms — as in

¹ This policy brief is based upon the research presented in: Maniokas, K., Delcour, L., Gazizullin, I., Berbeca, V., Muntean, I. and Munteanu, I. (2019) 'Political Economy of Law Harmonization in EaP Countries: Informal Adjustment of Association?', *EU-STRAT Working Paper No. 18*, Berlin: Freie Universität Berlin.; and Delcour, L., Dimitrova, A., Maniokas, K. and Wolczuk, K. (2019) 'State capacity, state capture and their effects on the implementation of Association Agreements in the Eastern neighbourhood', *EU-STRAT Deliverable 6.4b*, 7 March.

Ukraine — or on liberal development policies — as in Georgia. Moldova formally seems to be the most enthusiastic about embracing EU norms as a blueprint for modernization, yet as our research indicates there is a clear disconnect between this formal position and the country's effective reforms (or lack thereof). In addition, awareness about the risks associated with transport, environment and energy is very limited in all three societies, with the important exception of risks connected to the uncertainty of energy supplies. **The domestic resonance of EU rules in these sectors is therefore weak.**

Against this background, the main results of our research are puzzling. We find that the **transposition and implementation of EU *acquis* in the domains of energy, transport and environment are patchy, yet better than expected in light of the above considerations on the limited rewards available and the weak resonance of EU rules.** This is mainly because **there is an on-going informal adjustment of the AA, which is about reducing the scope of the commitments taken**, as in the case of vehicle inspections in Georgia, electricity unbundling in Ukraine and Moldova, and transport and environment in Ukraine. This affects the cost-benefit ratio of domestic elites, as it reduces the costs borne upfront by the partner countries. The EU, it seems, tacitly agrees with, and supports this process. For instance, our findings show that there has been no visible pressure exerted by EU institutions on Ukraine to comply with its own commitments in transposing the environmental *acquis*. This adjustment has thus far been the main condition for a successful transfer of EU rules in energy, transport and environment. However, while this informal adjustment helps to lighten the burden of law harmonization and facilitates the adoption of the EU's *acquis*, it is discretionary and does not seem to follow any blueprint. Therefore, it triggers uncertainty over future regulations among different stakeholders, such as civil society, businesses and investors.

The societies in associated countries are rather oblivious to the reduction of risks central to EU rules, be it by decreasing road accidents or reducing environmental damage. Yet, **these issues are entering the public agenda**, albeit slowly, as the cases of the Dniester river hydropower and vehicle inspections in Georgia can attest. For instance, issues related to road and car safety have gained prominence in recent years in Georgia, concomitantly to the planned transposition of an EU directive on roadworthiness tests (Directive 2009/40/EC of the European Parliament and of the Council of May 6, 2009). While the reintroduction of technical inspections for vehicles is very costly for Georgia,² the emergence of issues related to road safety in both the governmental agenda and media reports contributed to altering the cost-benefit analysis of the Georgian authorities. Combined with support from businesses interested in supplying testing equipment and providing testing services, this swayed the balance in favour of an accelerated transposition of the 2009 directive.

Our research also confirms that **the EU's *acquis* empowers some previously weak environmental groups and encourages civil society to take action** against actors with rent-seeking interests. For instance, Ukraine's intention to build six hydropower plants along the Dniester River triggered protests from environmental NGOs in both Moldova and Ukraine. Moldovan NGOs' explicit criticisms contributed to raising the awareness of the Moldovan Parliament, and the latter adopted a declaration in 2017 expressing deep concern over the six planned hydropower plants, as these could affect water quality and the ecosystems of the lower Dniester/Dniester delta and would also create significant water supply difficulties in Moldova. In Ukraine, NGOs used the platforms set up under the Eastern Partnership Civil Society Forum to issue a joint appeal to the prime minister, calling for revising the government's plans. In addition, Ukrainian experts pointed to the weak economic justification for

² The costs are estimated at approximately USD 800 million.

the project. Therefore, local environmental groups strategically use approximation with EU standards to both enhance their influence in the policy process and demonstrate the direct benefits of adopting the *acquis*. This increases the domestic resonance of the *acquis*. However, given that domestic environmental awareness is only nascent, compliance with the related EU *acquis* will be a long process.

All three associated countries **vary in terms of their performance in transposing and implementing the *acquis***. Ukraine seems to have problems with both, starting with transposition, as the government does not have clear support from the parliament. Therefore, the transposition and implementation of EU rules require the opening of a window of opportunity in order to proceed.

In Georgia, the liberal developmental outlook limits the scope of transposition and implementation, but approximation with the *acquis* is ongoing, despite weaker indirect benefits due to the lack of physical connections to the EU's market. This outcome can be explained by both the Georgian authorities' political interest in the EU's presence and a rather high administrative capacity, as in the case of the energy regulator.

In Moldova, our research highlights gaps at the level of secondary legal acts and implementation due to weak administrative capacities and rent-seeking interests, two factors reinforcing each other.

In both Moldova and Ukraine, the setting-up of fully independent energy regulators has proven a major challenge, owing to the **continuous pressure from the tightly interconnected political elite and business actors**. Since 2014, the Moldovan authorities have increasingly interfered in the governance of the National Energy Regulatory Agency (ANRE), thereby undermining its impartiality and watering down its competences. The dismissal of ANRE's Director General by the Moldovan Parliament in 2013-14 (in breach of both national legislation and EU *acquis*) serves as a blatant example of the extent to which the ruling elite can resist reforms when they (in that case, ANRE's decisions) threaten their political and financial interests. In Ukraine, until 2017, the regulator (the National Energy Utility and Regulatory Commission, NEURC) has failed to act as a fully independent regulator and remained pliable to the preferences of top officials, such as President Poroshenko, and of the big players in the sector, such as the Firtash-Lyovochkin group and Akhmetov's DTEK group.

Our case study on unbundling also indicates that **rent-seeking practices, combined with security vulnerability** to Russia over Transnistria, explain Moldova's poor record in addressing the key problems of its electricity market. As a result of a controversial tender in early 2016³, Moldova continued to purchase energy from the Cuciurgan power plant in Transnistria, owned by the Russian holding company Inter RAO UES. This is despite the fact that buying electricity from Transnistria contributes to fuelling the Transnistrian gas debt, as Transnistria does not pay for its gas supplies and has accumulated debts totalling over 80 % of Moldova's GDP.⁴ Yet as a consequence of the authorities' growing interference in ANRE's governance, the Moldovan regulator is not in a position to ensure a level playing field for energy operators and to guarantee a transparent functioning of the market.

³ See Delcour, L., Dimitrova, A., Maniokas, K. and Wolczuk, K. (2019).

⁴ Cenuşa, D. (2017) 'Moldova. Pulling the Strings: Russia's Control over Moldova's Energy Sector', in Expert Forum, Energy, Russian Influence, and Democratic Backsliding in Central and Eastern Europe, National Endowment for Democracy, p. 51.

Our analysis confirms that the **EU's assistance is relevant when non-implementation is caused by a lack of administrative capacities**, as in the case of energy market functioning related to energy unbundling. Thus, in all three countries the Energy Community secretariat's support (combined with tight monitoring) was important to advancing the transposition of unbundling rules and its partial implementation.

EU conditionality seems to be working in Ukraine only for a limited number of reforms, which directly relate to the country's existential interests, such as the reform of the gas sector. It has to be noted, though, that the effects of EU conditionality are reinforced in a context of **high security vulnerability** to Russia. In addition, pressure for reform is exerted not only by the EU, but also by the US and the IMF. For example, the US is fully aligned with the EU-driven reform of the energy sector. As Ukraine was hugely dependent on Western aid, it had no other choice than to comply with external actors' demands and renew the composition of the NEURC. The EU's growing pressure on Moldova has also led to a reduction in rent-seeking, but meets strong resistance as it threatens the core interests of the dominant coalition. In Georgia, the EU's interest in the implementation of the AA rules related to energy seems lower. The EU needs Georgia as a success story within the Eastern Partnership, and therefore it tends to turn a blind eye on patchy implementation.

Implementing EU rules in the areas of energy, environment and transport will only become more complex over time. In other words, the burden of commitments deriving from the AA will become heavier for the associated countries as the transitional periods expire. At the same time, the adoption and application of EU rules will not be formally abandoned, as the AAs are key political priorities for both the three EaP countries and the EU. Against this background, it is likely that both the implementation of EU rules by associated countries and the application of conditionality by the EU will remain declaratory.

Policy recommendations

Strategic recommendations

- The transposition and implementation of the EU rules, especially in non-trade related sectors such as energy, environment and transport, are costly and require a **stronger economic rationale**. The EU could provide such economic rationale by initiating a **common economic space based on the opening of services sectors, which would include the EU, the Western Balkans and the three associated countries**. This would contribute to fostering exchanges of experience between the associated countries and the Western Balkans in terms of implementing the acquis. It would also strengthen connectivity with associated countries, a key priority outlined in the 2020 deliverables for the Eastern Partnership. Crucially, **this economic space would contribute to mobilizing political elites and societies behind the painful agenda of transformation, while also creating additional levers for the EU to promote sustainable reform**.
- In order to both alleviate the burden of implementation and enable an effective application of EU rules, the EU could move toward a more formal and systematic **adjustment of the AA**. This would entail **increased sequencing and focusing** on key provisions, as well as providing more visible incentives.
- The institutions set up as part of the AA have a key role to play in this adjustment process. **The Association Council, the Committee, and sub-committees may provide increased guidance by mainstreaming socio-economic development objectives into the process**. This would also contribute to moving away from the

key role currently played by the European Commission's services, and to strengthening local ownership. The Association Agendas need to reflect this adjustment process, too. Currently, they add new priorities to the commitments made as part of the AA, thereby only making the burden of implementation heavier. The Association Agendas would need to focus on a limited number of priorities, while postponing some other obligations stemming from the AA.

- Focusing, however, **has to follow a certain explicit logic**. This logic could be gradually spelt out either in the AA implementation reports or in a horizontal paper for all three associated countries. A comparative assessment of the EaP associated countries by the European Commission and civil society, **and the screening exercise** could be the best tools to achieve it.

Operational recommendations

- The EU needs to provide **increased capacity building** in sectoral legal harmonization. A good example is how the Energy Community secretariat supports transposition efforts related to unbundling through the EU4Energy project. The EU could also create a joint facility supporting the reforms in all three associated countries.
- However, technical assistance and capacity building are not sufficient to induce change. Therefore, the EU could step up its **interventions at the political level and coordinate them better with its operational interventions and technical assistance**. Such a **political involvement** is especially needed to support the regulators, in light of the repeated interferences in their governance and work. When facing situations where the rule of law is threatened, the EU needs to activate political conditionality. In addition, the EU could better support the reform process by extending innovative assistance approaches, such as the Support Group set up in Ukraine, as well as assistance focused on reforms via delegated agreements.
- The EU could step up its support to **local actors** in the energy, transport and environment sectors. Initiatives such as the Covenant of Mayors have played a key role in raising local awareness about environmental issues, while also contributing to increased energy efficiency. The EU could launch similar initiatives on other environmental topics (e.g., water pollution) with the support of the European Investment Bank/European Bank for Reconstruction and Development.
- The EU could also seek to **systematically empower civil society to oversee implementation of the AAs** in the energy, transport and environment sectors. Given the tight connection between business interests and political elites (especially in Ukraine and Moldova), civil society plays a critical role as a monitor, especially on issues related to energy and environment. The EU could therefore offer increased and more systematic support to NGOs involved in these sectors.



The EU and Eastern Partnership Countries An Inside-Out Analysis and Strategic Assessment

Against the background of the war in Ukraine and the rising tensions with Russia, a reassessment of the European Neighborhood Policy has become both more urgent and more challenging. Adopting an inside-out perspective on the challenges of transformation the Eastern Partnership (EaP) countries and the European Union face, the research project EU-STRAT seeks to understand varieties of social orders in EaP countries and to explain the propensity of domestic actors to engage in change. EU-STRAT also investigates how bilateral, regional and global interdependencies shape domestic actors' preferences and scope of action. Featuring an eleven-partner consortium of academic, policy, and management excellence, EU-STRAT creates new and strengthens existing links within and between the academic and the policy world on matters relating to current and future relations with EaP countries.
