Russia and the WTO

Russia’s Case Against the EU Concerning the Third Energy Package

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Abstract

The European Union adopted the so-called “third energy package” in 2009 with the aim to make the energy market more effective, increase the security of supply and to create an internal market in gas and electricity. The Directive concerning common rules for the internal market in gas (2009/73/EC) regulates the effective unbundling of energy production and supply interests from the network and sets forth provisions for the prevention of control of transmission systems by third-country undertakings unless they satisfy the unbundling requirements and will not put at risk the security of energy supply of the EU Member States and the Community. The third energy package raises a number of potential concerns for the Russian Federation, which after its accession to the WTO filed a dispute in the WTO Dispute Settlement Body and claims that the measures in the EU’s third energy package are inconsistent with a number of obligations and specific commitments of the EU and its Member States. Russia claims that the measures restrict imports of natural gas originating in Russia and discriminates against Russian natural gas pipeline transport services and service suppliers, including Gazprom, the Russian state-owned gas company, most affected by the requirements of the third energy package. At first look, many of the claims submitted by Russia seem promising and the dispute is certainly one of the most important energy disputes brought to the WTO Dispute Settlement Body, since trade in energy has not been addressed before. Having evaluated the measures in the light of the WTO principles, this thesis concludes that it is unlikely that the WTO panel will interpret the unbundling measures as being inconsistent with the GATS principles, but the third-country certification measures may well give rise to violation of the GATS principles of most-favoured-nation treatment and national treatment.
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Uppsala, 10 August 2016
## List of Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>DSB</td>
<td>The Dispute Settlement Body</td>
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<td>DSU</td>
<td>The Understanding on Rules and Procedures Governing the Settlement of Disputes</td>
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<td>EU</td>
<td>The European Union</td>
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<td>GATS</td>
<td>The General Agreement on Trade in Services</td>
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<td>GATT</td>
<td>The General Agreement on Tariffs and Trade</td>
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<td>ISO</td>
<td>Independent system operator</td>
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<td>ITO</td>
<td>Independent transmission operator</td>
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<td>LNG</td>
<td>Liquefied natural gas</td>
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<td>LTSC</td>
<td>Long-term supply contract</td>
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<td>LTTC</td>
<td>Long-term transportation contract</td>
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<td>MFN</td>
<td>Most-favoured-nation treatment</td>
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<td>NT</td>
<td>National treatment</td>
</tr>
<tr>
<td>TSO</td>
<td>Transmission system operator</td>
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<tr>
<td>VIU</td>
<td>Vertically integrated undertaking</td>
</tr>
<tr>
<td>WTO</td>
<td>The World Trade Organization</td>
</tr>
</tbody>
</table>
Table of Contents

Abstract 3
Acknowledgements 5
List of Abbreviations 7

1 Introduction 11
1.1 Background 11
1.2 Aim 12
1.3 Delimitations 12
1.4 Method and Materials 13
1.5 Disposition 14

2 The WTO 15
2.1 Legal Framework 15
2.2 Energy within the WTO 16
2.3 Dispute Settlement 17
2.4 Russia’s Accession to the WTO 18

3 EU–Russian Gas Trade 20
3.1 Role of Russian Gas in EU Energy Supply 20
3.2 Implementation of the Third Energy Package and Russia’s Concerns 22

4 Legal Analysis of the Dispute European Union and Its Member States – Certain Measures Relating to the Energy Sector 24
4.1 Introduction 24
4.2 Applicability of the GATS 25
4.3 Has the European Union and its Member States Undertaken Specific Commitments on Pipeline Transportation Services? 28
4.4 Claims and Main Arguments of the Russian Federation 29
4.5 The Measures at Issue 31
4.5.1 The Unbundling Measures 31
4.5.2 The Third-Country Certification Measures 34
4.6 Claims of Violation of the National Treatment Commitment under Article XVII of the GATS 36
4.7 Claims of Violation of the MFN Treatment Commitment under Article II:1 of the GATS 43
4.8 Claim of Violation of the Market Access Commitment under Article XVI of the GATS 47
4.9 Claims of Violation under Article VI of the GATS 50
4.10 Justifications under Article XIV of the GATS 53
4.11 Summary 56

5 Concluding Remarks 58

List of References
1 Introduction

1.1 Background

The Dispute Settlement Body (DSB) of the World Trade Organization (WTO) composed a WTO panel on 7 March 2016, pursuant to the request of the Russian Federation in EU – Certain Measures Relating to the Energy Sector.\(^1\) In its request, dated 30 April 2014, the Russian Federation argued that the measures in the directives and regulations of the European Union, implementing the so-called “third energy package”, unjustifiably restrict imports of natural gas and discriminate Russia and are inconsistent with the European Union’s obligations under the WTO law. The third energy package was adopted by the European Union in July 2009 in order to improve the functioning of the internal energy market and resolve structural problems by liberalizing the European natural gas and electricity market. The aim is to primarily make the energy market more competitive and reduce prices. The most controversial area covered by the third energy package is a requirement of unbundling vertically integrated energy suppliers from network operators in the Directive 2009/73/EC\(^2\). This unbundling requirement is extended to third parties active in the common market and is often called the “Gazprom Clause”, as the Russian state-owned gas company Gazprom, the main foreign supplier of gas to the European Union, is most affected by the requirement. Russia is currently Europe’s largest gas supplier. Gazprom now faces a legal obligation to separate its production and supply activities from transmission operations on the European territory and to allow access to its gas pipelines to other energy companies. The clause raises concerns about the compatibility with obligations of the European Union under the WTO law, in particular GATS and GATT. Russia’s accession to the WTO made it possible to file a dispute and challenge the European measures relating to the energy sector. The dispute is interesting because it will provide the DSB with an opportunity to address trade in energy, which is an area that has been

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discussed minimally in WTO jurisprudence. The result could have major impacts on the applicability of the WTO law and on the European energy law and policy.

1.2 Aim

The aim of this thesis is to review the dispute European Union and its Member States – Certain Measures Relating to the Energy Sector, in which Russia contested certain measures taken by the European Union and its Member States in relation to the energy sector, and in particular examine the compatibility of the unbundling and the third-country certification measures with the obligations under the current WTO law, more specifically the GATS. The legitimacy of the claims as regards to unbundling and the third-country certification measures, raised by the Russian Federation in the requests will be evaluated. Do the clauses constitute a potential violation of the current obligations of the European Union under the legal framework of the World Trade Organization, in particular of the GATS disciplines, and to what extent? Additionally the perspective and the possible outcome of the dispute as regards to the first part of the request will be speculated. Before analysing the inconsistency of the unbundling regime and the third-country certification clause, the thesis sets out with an introduction of the World Trade Organization and the EU-Russian gas market. Additionally an overview of the purposes behind the third energy package will be described as well as what obligations and conditions the legislative package imposes.

1.3 Delimitations

According to Russia’s request for WTO consultations dated in 8 May 2014, the major concerns for Russia were the unbundling obligations and the third-country regime that extend the unbundling obligations to third parties active in the common market by requiring that TSOs in each Member State shall be certified as complying with the relevant unbundling requirements. When such certification is requested by a transmission system owner of a TSO controlled by a person or persons from a third country, the granting of a certification shall not jeopardize the security of supply of the
Member State and the EU. Other issues invoked in the Russian request include the requirement of ensuring implementation of a system of third-party access to the transmission and distribution system and LNG facilities in the EU, infrastructure exemptions granted, capacity allocation measures and so-called “projects of common interests” measures. It is not possible in this thesis to analyse each of these claims raised in the request for establishment of a panel. Therefore only the legitimacy of the claims relating to the unbundling regime and how the requirement is extended to third countries active in the natural gas market will be assessed, since they may violate some fundamental WTO principles: the most-favoured-nation (MFN) treatment and the national treatment (NT). The Market Access obligation under Article XVI of the GATS and the Domestic Regulation obligation under the Article VI of the GATS will also be discussed since Russia claims that the unbundling measures as implemented in laws of certain Member States restricts market access, and some Member States do not seem to administer the third-country certification measures in a reasonable, objective and impartial manner.

### 1.4 Method and Materials

This thesis employs the traditional legal dogmatic method for answering the problem statements. The legal dogmatic method is used for describing and examining the current state of the applicable law and analysing the law in relation to the legal issue *de lege lata*. The method is chosen based on the aim of this thesis, which is to examine whether the unbundling and the third-country regimes in the third energy package are inconsistent with the obligations under the current WTO law, in particular with GATS. For this purpose, the analysis of the dispute is based on a close examination of the GATS as well as official WTO documents, such as the requests for consultations and establishment of a panel by the Russian Federation, keeping in mind that the dispute is currently under panel proceedings and no panel report is yet adopted by the Dispute Settlement Body. A principal feature of the WTO dispute settlement process is that consultations, panel proceedings and Appellate Body proceedings are confidential and

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there is a lack of transparency. All written submissions of the parties are treated confidential and the meetings of panels with the parties take place behind closed doors. Therefore the examination of the claims will rely on secondary sources and focus on a selection of literature on WTO law and a rather restricted number of legal articles, which are frequently cited and published in recognised international law journals, such as Journal of Energy & Natural Resources Law, European Energy and Environmental Law Review and publications from the Oxford Institute for Energy Studies (OIES). The fundamental principles in GATS will also be described through doctrine consisting of final panel reports adopted by the DSB. The third energy package is described with the help of the relevant acts and commentaries.

1.5 Disposition

This thesis proceeds as follows. The second chapter provides with a presentation of the legal framework of the WTO. The status of energy within the WTO and rules applicable will be described. It further describes the process of the WTO dispute settlement and illuminates also briefly Russia’s accession to WTO in August 2012. The focus in chapter three describing the EU-Russian gas trade is twofold. The chapter will first discuss the role of Russian gas and Gazprom in EU energy supply. Thereafter, the purposes behind the third energy package in creating an internal energy market will be addressed. In chapter four the Russian claims relating to the unbundling regime and the third-country requirement will be discussed. The chapter provides first with an introduction of the dispute proceeding to date and presents Russia’s requests, and then an overview of the legal framework of the third energy package, the concept of unbundling and third-country certification. Thereafter, it will be evaluated whether, and to what extent, the claims are consistent with the obligations under the current WTO law, in particular with principles in GATS. The chapter discusses the fundamental obligations in turn and leads to examination of possible justifications. Lastly some concluding remarks will be presented.

2 The WTO

2.1 Legal Framework

This section will provide with an overview of the legal framework of the World Trade Organisation, formally established in 1995, establishing the legal ground-rules for international commerce. The WTO’s main function is to liberalise trade and to ensure that trade between nations flows smoothly, predictably and freely.\(^5\) The origins of the WTO lie in the multilateral General Agreement on Tariffs and Trade of 1947 (GATT 1947), which used to be the *de facto* international organisation for international trade for decades, and aimed at reducing tariffs on trade in goods. The provisions under the GATT 1947 are now integrated into the GATT 1994, which is one of the multilateral agreements annexed to the Agreement Establishing the World Trade Organisation (WTO Agreement).\(^6\)

The WTO’s trade rules, negotiated and signed by a large majority of the world’s trading nations, cover not only trade in goods, but also trade in services and intellectual property\(^7\) and rules and procedures governing the settlement of disputes\(^8\). The *General Agreement on Trade in Services* (GATS), inspired by the same objectives as the GATT, is also annexed to the WTO Agreement and establishes fundamental legislative framework within which Members can undertake and implement commitments for the progressive liberalisation of trade in services.\(^9\) Under the Article I:1, the GATS applies to measures by Members affecting trade in services. It contains general rules, such as the most-favoured-nation (MFN) treatment and rules on transparency\(^10\), which apply across the board to measures affecting trade in services, and sector-specific rules, which application depends to an extent on the specific commitments undertaken by Members.

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\(^6\) Van den Bossche & Zdouc (n 4) 75-82.

\(^7\) Trade-Related Aspects of Intellectual Property Rights (TRIPS).

\(^8\) Dispute Settlement Understanding (DSU).

\(^9\) More in Van den Bossche & Zdouc (n 4) 45-47.

\(^10\) Article III requires each Member to publish all measures that affect trade in services, and to inform other Members promptly of any changes in measures affecting trade in services covered by its specific commitments.
The specific commitments on market access and national treatment, established in Article XVII and XVI respectively, are the core of the GATS.

2.2 Energy within the WTO

Interestingly, the rules of GATT and the GATS do not deal with energy as a distinct sector. The WTO has not usually been immediately associated with energy issues either. By the time the rules of GATT were negotiated, liberalising trade in energy was not considered a political priority, due to the fact that international trade in energy was dominated by a few state-owned multinational companies, performing all energy related economic activities, from the production of energy to its distribution to the final consumers. Important energy actors of today, such as Saudi Arabia, Russia and Iran, were not contracting parties of the GATT and were not represented in the WTO. Moreover, the strategic nature of energy products was feared to politise the negotiations and create unnecessary tensions. What became the consensus is that basic WTO rules apply to all forms of trade, including trade in energy goods and services. Also the WTO dispute settlement mechanism gained the competence in energy-related issues.

Governments have traditionally regulated the energy sector, and in many countries the supply of energy used to be a natural monopoly. Because of the dominating vertically integrated undertakings (VIU’s) have been affecting the market structure, the energy industry has traditionally not distinguished between energy goods and services. In the context of the VIU’s business, energy services would just add value to the energy goods they produce, transport and distribute. This approach has changed after the privatisation

and the emergence of independent producers and distributors. The production of energy goods and commodities falls within the scope of the GATT. Energy transmission, distribution and energy-related services, such as construction, engineering and consulting services, constitute services under the WTO law and when they are provided independently, they fall within the scope of the GATS. As already mentioned, energy services were never negotiated as a separate sector in the WTO. There are however three separate sub-sectors that relate to energy activities: ‘services incidental to mining, rendered on a fee or contract basis at oil and gas fields’ and ‘services incidental to energy distribution’ in ‘business services’. The third one is ‘the pipeline transportation of fuels’, which is a sub-sector of ‘transport services’. Important energy-related services, not exclusive to the energy industry, such as transportation and distribution, are covered by other service sectors.

2.3 Dispute Settlement

For the purposes of this thesis, the rules and procedures governing the settlement of disputes merit some attention. The dispute settlement system of the GATT is considered to be one of the cornerstones of the WTO. It is a central element that provides security and predictability to the multilateral trading order. The EU works as a single actor in disputes and is represented by the Commission, which negotiates agreements and defends the EU’s interests before the DSB on behalf of all 28 Member States.

The ideal way, emphasised by the DSU, is to resolve disputes amicably by diplomatic means at the consultation stage. A Member is required to enter into consultations within 30 days of a request for consultations from another Member. If resolving the dispute is not possible, the complainant may refer the dispute to a panel for adjudication after 60 days. More in about WTO dispute settlement in Van den Bossche & Zdouc (n 4) 156-303.

14 The question on whether the activities closely related to the production of energy are covered by the GATT or the GATT depends on whether the activity is performed independently from the producing company. If the activity is supplied on a fee or contract basis by a company that does not own the raw material, it is classified as service and thus falls within the GATS.


16 DSU, Article 3.2.
days by requesting the establishment of a panel. The panel proceedings last on average approximately fifteen months, depending on the complexity of the case, the need to consult experts, problems with scheduling meetings and the time that is required for translating documents. The general rule is that a panel must conduct its examination within six months, and the period should in no case exceed nine months.\(^{17}\) The burden of proof in WTO dispute settlement proceedings is on the party that asserts the affirmative of a particular claim or defence.\(^{18}\) The end result of the panel proceedings is a panel report, which in turn can be appealed to the appellate body. The last step includes implementing the recommendations in panel/appellate body reports adopted by the DSB, in case the respondent is found to violate WTO law.\(^{19}\)

A principal feature of the dispute settlement is that the proceedings are confidential. In practice that means that from the written submissions of parties, to the meetings of panels and hearings, and even to some extent the reports of panels, everything is confidential. Although the lack of transparency is often criticised by other Members and civil society, companies and the Members consider the confidentiality important.\(^{20}\)

### 2.4 Russia’s Accession to the WTO

Russia became the 156th Member of the WTO on 22 August 2012 under the Protocol on the Accession of the Russian Federation, adopted by the Ministerial Conference on 16 December 2011, being the last major country to join the WTO. Completing the accession negotiations were fraught with disagreements and obstacles and lasted eighteen years.\(^{21}\) Over 60 Member States participated in the Working Party of Russia’s accession negotiations and there seemed to be no unanimous support for Russia’s membership.\(^{22}\)

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\(^{17}\) Van den Bossche & Zdouc (n 4) 246-50.

\(^{18}\) Van den Bossche & Zdouc (n 4) 258.

\(^{19}\) Van den Bossche & Zdouc (n 4) 244.

\(^{20}\) Needless to say, the lack of public documents adds some challenge to legal research, especially at an early stage of the dispute. More about the confidentiality and transparency in Van den Bossche & Zdouc (n 4) 251.

\(^{21}\) Van den Bossche & Zdouc (n 4) 111-12.

The accession has resulted in implementation of reforms in the Russian legislation and to the formation of institutes, including bringing 300 legal acts into conformity with the WTO law and improving market access.\textsuperscript{23} Subsequently tariffs and quotas have been reduced and the membership hopefully leads to modernisation of the Russian economy. Other benefits of the accession include improved quality of goods and a better business climate, with a more open, predictable and transparent investment and trade environment.\textsuperscript{24} The accession made it also finally possible for Russia to lodge complaints and seek reparation with respect the compatibility of the third energy package and its Gazprom clause with the WTO rules. Russia has started to use the available instruments quite actively and is currently a complainant in two cases against the EU (the current dispute on measures related to the energy sector and another one countering the EU’s anti-dumping measures on imports from Russia). Russia may however lack qualified lawyers and specialists in the field of trade policy and experience in WTO’s dispute settlement system.\textsuperscript{25}

\textsuperscript{24} Van den Bossche & Zdouc (n 4) 112, and Hober, 'WTO and Russia’ (n 22) 223.
\textsuperscript{25} Zubacheva Ksenia, 'Being a member of the WTO may not be that easy for Russia’ (Russia Direct, 2015) <www.russia-direct.org/analysis/being-member-wto-may-not-be-easy-russia> accessed 3 August 2016.
3 EU–Russian Gas Trade

3.1 Role of Russian Gas in EU Energy Supply

This section looks at the role of Russian gas and Gazprom in European gas supply. The section aims at brevity, looking at the European dependence on Russian gas and volumes of supply to the end it will be able to understand the importance of the Russian accession to the WTO, which provides with a legal framework for EU-Russia energy relations, and the purpose behind the third energy package.26

Although the EU has some own energy production, 54% of the natural gas consumed is imported. Russia, and especially its state-owned gas company Gazprom, is the main foreign supplier natural gas of the EU. The average volume of Russian natural gas exports to the EU is approximately 24% of the European gas demands. In 2013 Russia supplied 39% of the EU natural gas imports, accounting 27% of the EU gas consumption. Some European Member States, especially countries in the Baltic region, including Finland, Estonia and Lithuania, and South-eastern Europe, depend completely on Russian gas imports and use natural gas for more than a quarter of their energy needs.27 These countries are very vulnerable to interruptions. Most of the Russian gas exports to Europe are based on long-term supply contracts (LTSCs) and long-term transportation contracts (LTTCs), which last from 10 to 35 years. A majority of them were established in the 1970s and will expire during 2025-35. The average annual volumes of these supply contracts are up to 180bcm.28 The LTSCs and LTTCs are legally binding contracts and contain international arbitration clauses with liquidated damages in the event of non-performance. They are also subject to limitations on terminating the contracts before the expiry dates or reducing the volumes. Needless to say, the pressure is on Gazprom, as the company needs to make sure that it will

continue to supply the required volumes as agreed in the supply contracts under the new regime in the third energy package. Otherwise the company will face financial and reputational losses. The contractual obligations and commitments in the LTSCs and LTTCs are expected to be fulfilled by both contracting sides, so not only by Gazprom but also by European companies, irrespective of political circumstances or sanctions.\(^{29}\)

Currently, there is very a limited scope of reducing the European dependence on Russian gas supplies before the expiry of the LTSCs and LTTCs. For the countries considering that Russian gas constitutes a threat to national security and are vulnerable to possible interruptions, one of the options could to be to replace the supplies of gas from Russia with fuels from other countries, *e.g.* with LNG and pipeline gas via Turkey from the Caspian region.\(^{30}\)

Lastly, a few words should be said about Gazprom. It is the biggest Russian public joint stock company focused on geological exploration, production, transportation, storage, processing and sales of gas, gas condensate and oil. The company holds the world’s largest gas transmission system and largest natural gas reserves, up to 17% of the global and 72% of the Russian reserves.\(^{31}\) Over the past decades, Gazprom has been investing in trading, distribution, pipeline and storage activities in Europe.\(^{32}\) Gazprom and its wholly owned local subsidiaries in several European countries have the exclusive right to export gas from Russia, and the company has a *de facto* monopoly on foreign natural gas trade. It should also be noted that since the Russian Federation owns 50.002 % of Gazprom’s shares, the export of gas from Russia is basically under the control of the Russian government.\(^{33}\)

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29 Dickel et al (n 26) 5.
31 More information available at <www.gazprom.com/about> accessed 3 August 2016
32 Holz et al (n 27) 51.
33 Federal law 'On Gas Export' No 117-FZ dated 18 July 2006 (Федеральный закон 'Об экспорте газа'), Article 3.
3.2 Implementation of the Third Energy Package and Russia’s concerns

The reasons behind the third energy package will help to understand why Russia is opposing it. The European geopolitical and security discourse has repeatedly been focusing on the European dependence on Russian natural gas and the possibility of interruptions of gas supplies to Europe. The tense relations in the energy market and gas crises have called for reduction of Russian imports and diversification of European gas supplies.\textsuperscript{34} Liberalising the EU gas market has however been a slow process. Despite the first and second gas directives adopted since the early 1990s, the EU single gas market never made serious progress. The Commission consistently called for the liberalisation of the energy sector in order to increase the efficiency and the competitiveness of the European economy and to facilitate consumers to freely choose their suppliers of gas. Most Member States implemented the first electricity and gas directives, but the Commission considered that further measures would be necessary to address the concerns of transparency, competitiveness and flexibility of the European energy market. In 2007 the EU started developing a third generation of new internal energy market legislative proposals. The Commission highlighted the importance of completing the internal market in natural gas and creating a level playing field for all natural gas undertakings established in the Community.\textsuperscript{35} The third energy package was finally adopted in July 2009 and came into force in March 2011.\textsuperscript{36}

The main areas covered by the third energy package are the effective unbundling of energy production and supply interests from network operators, increased transparency of retail markets, more effective regulatory oversight, the establishment of the Agency for the cooperation of Energy Regulators (ACER) and better cross-border collaboration and investments. Unbundling is the main tool of liberalisation created by the Commission and it is certainly one of the most discussed and controversial products of the Directive. The rules on unbundling aim at preventing companies, who are involved

\textsuperscript{34} Gas crises refer to the disruptions in Ukraine in January 2006, because of price disputes and in the winter of 2008-09, because of unpaid bills, and the confrontation on gas with Belarus in late 2006. The third energy package was released one month after the threat of the gas dispute between Russia and Belarus over increased gas price in August 2007.

\textsuperscript{35} Directive 2009/73/EC, Recital (5).

\textsuperscript{36} Yafimava (n 28) 2-3.
in transmission of energy and production/supply of energy, from not allowing access to the transmission networks to their competitors. Without the unbundling, there is a risk of discrimination in the operation of the network and in the incentives for VIUs to invest in their transmission networks.\textsuperscript{37} As the rules mainly focus on liberalisation, they outstandingly conflict with the energy policies of third countries, including Russia.

Russia has made it clear that it is unhappy with the new obligations, because the European gas market could become problematic for it. The energy sector is important for the Russian economy. Over 70\% of Russia’s total gas exports go to the EU, so it is Russia’s largest gas export market. While the EU seeks to secure its gas supply and gas prices and reduce its dependence on Russia, Russia wants to ensure the security of gas demand in terms of volume and price. As regards to Gazprom, the third energy package will impact its investments and trade relations with EU buyers, because the company will not be able to comply with the unbundling requirements. Moreover, Gazprom has been forced to sell shares in the national transmission system operators in Lithuania and Estonia and abandon the Russian sponsored €32 billion South Stream pipeline project in 2014. At the same time, Russia considers the new regulations as a possible threat to the EU-Russia relations.\textsuperscript{38}

\textsuperscript{37} Directive 2009/73/EC, Recital (6).
4 Legal Analysis of the Dispute *European Union and Its Member States – Certain Measures Relating to the Energy Sector*

4.1 Introduction

This chapter aims to analyse the request for the establishment of a panel by the Russian Federation in *European Union and its Member States – Certain Measures Relating to the Energy Sector* with regard to the first section of the request, which refers to unbundling and third-country certification measures. The chapter will give an insight to Russia’s claims and examine the consistency of the provisions in the third energy package with the WTO disciplines, more specifically with the GATS. With the aim of finding out the likeliness of whether the claims will be accepted or rejected by the panel, the disposition of this chapter is structured as follows. After a brief introduction to the dispute proceedings to date in this first section, the second section discusses the applicability of the GATS. Section three examines the Schedules of Specific Commitments of the EU and its Member States. After that an overview will be given concerning Russia’s claims in the fourth section. Section 5 presents the measures in the third energy package at issue. The main focus of the following sections is to endeavour to analyse Russia’s claims and the consistency of the provisions in the third energy package referred in the claims, by looking at the provisions of the GATS. After analysing Russia’s claims, the applicable justifications of the measures will be examined in section 10. The final section consists of a summary.

As discussed in the previous chapter, since the first draft of the third energy package the unbundling and the third-country certification measures have been a major concern for the Russian Federation and its state-owned gas company Gazprom. The Russia-EU dialogue on the problematic issues of the third energy package began informally with
bilateral consultations already in January 2010 trying to seek for a resolution. Having strongly criticised the third energy package for years, Russia took advantage of its WTO accession and formally initiated a dispute settlement within the WTO framework by requesting for consultations on 30 April, 2014. Two rounds of consultations were held in Brussels on 23-24 June and 10 July, 2014, with a view to reaching a mutually satisfactory solution. Keeping in mind that both the European Union and its 28 Member States are full members of the WTO, the consultations were held with both of them. However, the consultations did not resolve the dispute. Consequently, in a communication dated 11 May, 2015 Russia requested the establishment of a panel. The panel was established at the DSB meeting on 20 July, 2015, where the EU argued that its energy policies are consistent with international trade rules and that Russia’s panel request has expanded the scope of the original complaint by including new measures and claims. Nine WTO members, having a substantial interest in the matter and the energy sector, have reserved their right to participate in the panel proceedings as third parties. The dispute is currently at an early stage. The Director-General composed the panel on 7 March, 2016.

4.2 Applicability of the GATS

Since Russia’s claims are based on the GATT and the GATS, while the emphasis of this thesis lays on the GATS, it is necessary to commence by explaining why the GATS agreement is applicable in the first place. The GATS is a multilateral agreement, which is applicable to measures by Members affecting trade in services. So in order to find out if the GATS is applicable the measure at issue shall affect trade in services. There

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42 The third-parties include Brazil, China, Colombia, India, Japan, Korea, Saudi Arabia, Ukraine and the United States.
43 GATS, Article I:1.
has to exist a transaction between a service seller and buyer, and a service, which actually appears on the market.\textsuperscript{45} The term ‘affecting’ has a broad meaning and implies that the measure has an effect on trade. The general obligations in the GATS are applicable to all WTO Members.\textsuperscript{46} Additionally, WTO Members have identified 12 core service sectors (and sub-sectors) on which Members can individually undertake trade commitments, which are listed in the Members Schedules of Specific Commitments. Some fundamental principles, like the national treatment principle and market access are therefore applicable only in sectors on which the WTO Member has agreed to lower tariffs or decrease non-tariff barriers.\textsuperscript{47}

When transportation and distribution of energy are provided independently by an undertaking, they constitute services according to the GATS.\textsuperscript{48} Classifying energy services is problematic, not only because of the fact that transportation of energy products and services are specific and technically complicated procedures.\textsuperscript{49} Energy services do not constitute a separate core service sector. Instead, important energy services such as transportation and distribution are listed as separate sub-sectors. Consequently ‘pipeline transportation of fuels’ is a sub-sector of ‘transport services’\textsuperscript{50}, and ‘services incidental to energy distribution’ are covered by ‘other business services’\textsuperscript{51}. Pipeline services include the transmission or transport and supply of natural gas, including LNG, and the services related to the transmission and supply of natural gas.\textsuperscript{52} Services incidental to energy distribution refer to transmission and distribution of gas on a fee or contract basis when the service is operated by an independent services

\begin{footnotesize}
\begin{enumerate}
\item For comparison purposes, the GATT is a multilateral agreement, which deals with trade in goods, aiming at eliminating discrimination and liberalizing trade though the reduction of tariffs and other trade barriers.
\item However, particular measures inconsistent with the MFN obligation can be maintained. By now there has been made one exemption to the MFN obligations in pipeline transportation of fuels.
\item Van den Bossche & Zdouc (n 4) 319-23.
\item WTO, Energy Services, Background Note by the Secretariat S/C/W/52 (9 September 1998) para 36.
\item Cottier et al (n 15) 11-12.
\item WTO Services sectoral classification list MTN.GNS/W/130 11(G)
\item WTO Services sectoral classification list MTN.GNS/W/130 1(F)(j)
\end{enumerate}
\end{footnotesize}
supplier and not by a vertically integrated manufacturer.\textsuperscript{53} These subsectors cover the transportation services provided by Gazprom.

The concept of ‘service’ is not defined in the GATS, but the agreement identifies four different ways of providing a service depending on the territorial presence of the supplier and the consumer at the time of the transaction.\textsuperscript{54} These four ‘modes of supply’ include cross-border supply of services (mode 1 – cross-border trade), consumption of a service in the territory of any other Member (mode 2 – consumption abroad), supply through commercial presence in the territory of any other Member (mode 3 – commercial presence), and supply of service through the presence of natural persons in the territory of any other Member (mode 4 – presence of natural persons). ‘Commercial presence’ has been defined in Article XXVIII (d) of the GATS meaning any type of business or professional establishment, including through the constitution, acquisition or maintenance of a juridical person, or the creation or maintenance of a branch or a representative office, within the territory of a Member for the purpose of supplying a service. According to the background note on energy services by the Secretariat, the principal modes for supply of energy services appear to be modes 1, 3 and 4.\textsuperscript{55} Modes 1 and 3 are most relevant for transportation of gas via pipeline. However, third-country undertakings, including Gazprom, manage their gas transmission networks also by having commercial presence, e.g. opening subsidiaries within the EU and Switzerland.\textsuperscript{56} Hence, when the Schedules of Specific Commitments maintained by the European Union and other Members relevant for the case will be examined in section 4.3. The focus will lay on mode 3 on commercial presence.

\textsuperscript{53} Background Note by the Secretariat (n 48) 3-4.
\textsuperscript{55} Background Note by the Secretariat (n 48) 9.
\textsuperscript{56} Van Hoorn Viktor, ‘”Unbundling”, ”Reciprocity” and the European Internal Energy Market: WTO Consistency and Broader Implications for Europe’ (2009) 18 European Energy and Environmental Law Review 51, 63.
4.3 Has the European Union and its Member States Undertaken Specific Commitments on Pipeline Transportation Services?

Russia argues that the prohibition for gas producers and suppliers to provide gas transportation and distribution services is inconsistent with Croatia’s, Hungary’s and Lithuania’s market access obligations under Article XVI:1 of the GATS and that the special ownership unbundling requirements for public transmission system operators and the third-country certification requirement contained in Articles 9 and 11 of the Gas Directive are inconsistent with the national treatment obligation contained in Article XVII of the GATS. Article XX of the GATS provides, in paragraph 1, that each Member shall set out in a schedule the specific commitments it undertakes. The Members’ schedules of specific commitments, pursuant to the same article, are an integral part of the GATS. It is important to note that the obligations Russia refers to, apply only to the extent that specific commitments have been made in the Schedules of Specific Commitments of each Member and therefore it is necessary to examine the commitments made by these countries with regard to pipeline transportation services. Each schedule is interpreted on the basis of Article 31 of the Vienna Convention, which provides the general rules of interpretation.

Under the current Schedule of Specific Commitments, the EU is not bound by the national treatment and market access principles with regard to transport services via pipeline and cannot consequently infringe these principles.\(^57\) Croatia, Hungary and Lithuania undertook market access and national treatment commitments on pipeline transport services on their accession to the WTO.\(^58\) The Commitments of these Members also relate to the applicable mode of supply: the mode 3 on commercial presence. Note also that Hungary has chosen to indicate a limited commitment by describing that services may be provided through a contract of concession granted by the state or the local authority.

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4.4 Claims and Main Arguments of the Russian Federation

This part of the chapter gives an insight to Russia’s requests, which concern several aspects. Overall, Russia claims that the third energy package unjustifiably restricts imports of natural gas originating from Russia and discriminates against Russian natural gas pipeline transport services and service suppliers. It considers that the EU’s third energy package is inconsistent with Articles II, VI, XVI and XVII of the GATS and Articles I, III, X and XI of the GATT. The request for the establishment of a panel consists of three main legal issues, including certain provisions of the third energy package relating to unbundling, the third-country certification requirement and infrastructure exemption measures in the natural gas section, as well as certain capacity allocation measures and projects of common interest measures. There are 17 Russian arguments in total.

In the first section of the request, Russia challenges the consistency of unbundling, third-country certification and infrastructure exemption measures in the natural gas sector with the GATS and the GATT. This section will be further discussed in detail in this thesis but at this stage it is necessary to give an overview of the arguments. Firstly, as regards to the unbundling requirements in the Gas Directive, Russia argues that the unbundling measures, as implemented in the national laws of Croatia, Hungary and Lithuania, are inconsistent with these Members’ market access obligations under Articles XVI:1 and 2 of the GATS. Secondly, Russia considers that the versions of Article 9 (6) of the Gas Directive implemented in the legislations of Croatia, Hungary and Lithuania are de jure inconsistent with these countries’ respective obligations under Article XVII of the GATS (national treatment principle), and that Croatia and Lithuania de facto violate their obligations under the same article, since they both own and control the TSO and production or supply portions of the single VIU supplying pipeline transport services in their territories. Thirdly, Russia challenges the variety of unbundling models among EU Member States amounting to less favourable treatment being accorded to Russian pipeline transport services and service suppliers, and therefore considers that EU is violating Articles II:1 of the GATS and I:1 of the GATT (MFN principle) and Article III:4 of the GATT (national treatment principle), and
considers the exemption of ‘upstream pipeline networks’ from the scope of the unbundling requirements inconsistent with the MFN and national treatment principles.

Another problematic issue challenged by Russia is the third-country certification requirement provided in Article 11 of the Gas Directive, which according to Russia also violates the national treatment and MFN principles in GATS. Furthermore, Russia considers that Croatia, Hungary and Lithuania have administered the third-country certification measures in a non-reasonable, non-objective and partial manner, contrary to their obligations under Articles VI:1 and VI:5 (a) of the GATS. Also, according to Russia, the EU itself has violated the MFN principle in the GATS when the Commission approved some certifications of TSOs without conducting the security of supply assessments. In several instances Russia refers to decisions of EU administrative bodies which have treated Russian gas products and services or service suppliers differently from other WTO Members, (e.g. higher certification requirements, NEL pipeline not qualifying as an interconnector and gas release requirements.)

The two other sections of Russia’s request require less attention for the purposes of this thesis, but will be illuminated briefly. The second legal issue in the request considers the capacity allocation measures in the third energy package. For clarification purposes, access to gas transportation networks is granted by selling rights to gas suppliers for a

59 The Commission required the security of supply assessment from Gaz-System S.A. (section of the Yamal-Europe pipeline, owned by Russian Europolgaz) for the certification as an ISO, when in other cases of TSOs the assessment was not conducted. See further in European Commission Opinion of XXX pursuant to Article 3(1) of Regulation (EC) No 715/2009 and Article 10(6) and 11(6) of Directive 2009/73/EC - Poland - Certification of Gaz-System as the operator of the Polish section of Yamal-Europe Pipeline <ec.europa.eu/energy/sites/ener/files/documents/2014_102_pl_en.pdf> accessed 3 August 2016.
60 The Nordeuropäische Erdgasleitung (NEL) pipeline, whose owners include a Russian service supplier, was intended to transport Russian gas through Germany and requested an exemption from the requirements of the Gas Directive. NEL was not granted an exemption by the German authorities, although similar third country service suppliers or owners of other pipelines also not meeting the definition of an interconnector were. See further Bundesnetzagentur, 'OPAL pipeline: Federal network Agency grants partial exemption for OPAL pipeline' (2009) <www.bundesnetzagentur.de/SharedDocs/Pressemeldungen/EN/2009/090225OPALPipeline.html> accessed 3 August 2016.
61 A 50 per cent cap on the ability of the Russian supplier operating the OPAL pipeline, described as a ‘dominant undertaking’, to acquire exit capacity at the Czech border was imposed by the Commission, which could be exceeded by selling gas at a government-set fixed price, instead of market price.
particular volume of capacity. The third energy package contains a system of regulations, which concern the manner in which capacity allocation may take place, e.g. gas grid operators shall use harmonised auctions when selling access to pipelines. Capacity for natural gas originating in Russia is sold by auctions, since Member States have defined this gas as entering through interconnection points and under the adopted regulations such gas must be sold by auctions, whereas capacity at entry points is sold on a first-come-first-serve basis (domestic gas and other third-country-origin gas.) This has an impact on the tariffs. Russia considers that its gas is accorded less favourable treatment than domestic European natural gas and thus the capacity allocation measures violate Article III:4 of the GATT.

The third legal issue is the consistency of ‘Projects of Common Interest’ (PCIs) measures with the obligations under GATS and GATS. Russia considers that they are contrary to Article II:1 of the GATS as well as Articles I:1 and III:4 of the GATT, since they accord Russian services and service suppliers less favourable treatment than is accorded to like services and service suppliers of other third countries. Projects from third countries are listed as PCIs, contrary to any projects designed to facilitate the importation or transportation of natural gas from Russia, and are accorded priority status, including priority gas corridors. The criteria for PCIs are set forth in the TEN-E regulation.

4.5 The Measures at Issue

4.5.1 The Unbundling Measures

The cornerstone of the third energy package is the unbundling regime, which requires the effective separation (‘unbundling’) of the operation of transmission networks from

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63 National Treatment on Internal Taxation and Regulation.
production/generation and supply operations of vertically integrated energy companies in the EU and in the countries of the European Energy Community. A vertically integrated company is a gas undertaking or a group of undertakings where the same person/persons are entitled, directly or indirectly, to exercise control and the undertaking or the group of undertakings perform transmission and/or distribution and production or supply of natural gas. The unbundling requirement applies also to companies from non-EU countries and is therefore relevant to Russia and companies from other third countries, which invest or hold gas assets in any part of the energy chain in Europe. The measures are believed to increase the competition in the European energy sector, improve the performance of the network, have a positive effect on prices, and separate the grids, in order to support the construction of a common European grid.

The Gas Directive provides three models of unbundling: (i) the full ownership unbundling model; (ii) the independent system operator (ISO) model, and (iii) the independent transmission operator (ITO) model. In the case of full ownership unbundling, set forth in Article 9 of the Gas Directive, the division of the integrated vertical entities of network operations are owned and managed separately. That is to say the ownership of the gas network is transferred to a transmission system operator (TSO). Each undertaking, which owns a transmission network, shall be appointed as a transmission system operator. Furthermore, the same person or persons shall not be entitled to exercise control (including appointing board members or being a board member) over an undertaking performing any of the functions of production or supply, and at the same time exercise control or any right over a TSO or a transmission system; nor exercise control over a TSO, and directly or indirectly to exercise any right over an undertaking performing any of the functions of production or supply. In other words, holding of a majority share is precluded. ‘Control’ means the possibility of exercising decisive influence on an undertaking, in particular by ownership or rights or contracts, which confer decisive influence on an undertaking. In practice these measures mean

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66 Cottier et al (n 15) 3.
that the undertakings need to do some restructuring by splitting up their activities or sell activities to other undertakings.\textsuperscript{71} The European Parliament has referred to the full ownership unbundling model as the most effective tool to promote investments in infrastructure in an non-discriminatory way, fair access to the network for new entrants and transparency in the gas market.\textsuperscript{72} The Directive provides however a derogation from these generally applicable rules. Under Article 9 (6) when the owner of the vertically owned undertaking is a Member State or another public body, two separate public bodies exercising control over a TSO or over a transmission system and over an undertaking performing production or supply functions, shall be deemed not to be the same person or persons. The consistency of this specific provision will be evaluated under the national treatment principle of the GATS in section 4.6.

Under the ISO model the ownership of the gas network assets remain with the vertically integrated company, but the transmission network is managed by an independent system operator, which is an undertaking or an entity separated from the original vertically integrated company that will perform all the functions of a network operator.\textsuperscript{73} Under the ITO model, the supply and generation activities of the vertically integrated companies are operated independently from their network activities through a separate subsidiary.\textsuperscript{74} Also the setting up of an ITO enables the undertaking to maintain ownership of the network assets. The aim is to ensure the neutrality and independence of the transmission operator through detailed conditions such as an independent management, a supervisory board, a compliance officer etc. The option is also called the ‘business as usual’.\textsuperscript{75}

Member States may select from among the alternative unbundling models. All three unbundling models are permitted in the national implementing laws of Croatia and Hungary, whereas Lithuania and Estonia have adopted legislations that permit only the full ownership model, which in each case seems to be the most usual alternative among Member States.

\textsuperscript{72} Directive 2009/73/EC, Recital (8).
\textsuperscript{73} Directive 2009/73/EC, Article 14.
\textsuperscript{74} Directive 2009/73/EC, Article 17.
4.5.2 The Third-Country Certification Measures

This section will provide with an overview of the third-country regime in the Gas Directive. The Gas Directive sets forth provisions for the prevention of control over EU networks by vertically integrated undertakings from third countries, unless they satisfy certain requirements. EU legislators see a threat posed to the security of energy supply, which is considered an essential element of public security and connected to the efficient functioning of the internal market in natural gas.\textsuperscript{76} It is quite obvious, that the clause is also political and may affect the future cooperation between the EU and Russia, since the EU wishes for greater reciprocity from Russia in terms of investment and access to the Russian gas market. Hence the unofficial names the ‘Gazprom clause’ and the ‘Lex Gazprom’.\textsuperscript{77}

Under the Gas Directive proposal persons from third countries were not allowed to control transmission systems or TSOs, unless they came from a country that had concluded an agreement with the Community.\textsuperscript{78} In addition to the prohibition of control, third-country undertakings who control gas networks or TSOs, needed to comply with the same unbundling rules as European undertakings to be certified.\textsuperscript{79} The clause would have effectively excluded foreign investments by state-owned undertakings.\textsuperscript{80} This far-reaching proposal was not included within the final third energy package, since several problems were identified with regard to the negative signal to investors. As a result investments could have been reduced. The exact nature of the agreements and the applicability of the clause to existing investments were unclear and could have jeopardized existing partnerships.\textsuperscript{81} The Council stated instead that the text of the third energy package needs to ensure that the issue of third-country control of networks shall be addressed in a non-protectionist way which guarantees that companies outside the EU respect the same rules that apply to EU undertakings and ‘address concerns about potential implications on Community competence and the handling of existing investment as well as provide the criteria against which investment from third country

\textsuperscript{76} Cottier et al (n 15) 4.
\textsuperscript{77} Talus (n 75) 83.
\textsuperscript{79} Van den Bergh (n 71) 233.
\textsuperscript{80} Van Hoorn (n 56) 57.
\textsuperscript{81} Van Hoorn (n 56) 60.
would be assessed, in particular the EU security of supply. The provisions of the third-country regime are not addressed to the governments of third countries, but to the foreign undertakings, and it does not extend obligations of reciprocity to other regulatory areas.

Under the third-country certification clause, operations and investments by vertically integrated companies from third countries are subject to the requirement of prior EU consent and a certification procedure. Member States have the competence to refuse the certification unless following requirements are fulfilled: (a) the third-country company concerned complies with the unbundling requirements; and (b) granting certification will not put at risk the security of energy supply of the Member State and the Community. In other words, in addition to the unbundling regime, Member States will have to take into consideration the general effect on energy security. Furthermore, before adopting the decision, Member States shall notify the Commission when a transmission system owner or a TSO which is controlled by a person or persons from a third-country or third countries requests a certification, and ask for an opinion on whether the undertaking complies with the unbundling requirements and whether granting a certification will not put at risk the security of the energy supply. The Commission then examines the request referred to it. Although the role of the Commission is consultative, the national regulatory authority must take into account its opinion when adopting the final decision on the certification. The national authority retains the ultimate veto power.

When assessing the level of the security of energy supply, the national regulatory authority shall take into account the rights and obligations addressing the issues of security of energy supply (including agreements concluded) of the Community with respect to the third-country in question under international law; the rights and obligations of the Member State with respect to the third country arising from agreements concluded with one or more third countries to which the Community is a

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82 TTE Council 10310/08 (6 June 2008), 7.
83 Cottier et al (n 15) 6.
84 Directive 2009/73/EC, Article 11.3 (a)-(b).
85 Directive 2009/73/EC, Article 11.4-5.
party and which address the issues of security of supply; and finally other specific facts and circumstances as well as the third country concerned. 

4.6 Claims of Violation of the National Treatment Commitment under Article XVII of the GATS

After the introduction it is now possible to discuss the claims in detail. Russia has challenged various issues to be inconsistent with the national treatment commitment under Article XVII of the GATS, according to which Members shall accord to services and service suppliers of any other Member treatment no less favourable than to its own like services and service suppliers. Treatment is considered less favourable if it modifies the conditions of competition in favour of domestic services or service suppliers. Foreign and domestic services shall be treated equally and Member States shall ensure equal competitive opportunities to like services.

Firstly, as stated above, the Gas Directive contributes to exemptions and derogations from the generally applicable rules on unbundling so that not all vertically integrated companies are going to be forced to sell their network assets. Among them are energy companies, which have close relations to political powers in the Member States and will use the opportunity to derogate from full ownership unbundling. This possibility is opened up in Article 9 (6) of the Gas Directive, which provides that when the owner of the vertically integrated undertaking is a Member State or another public body, two separate public bodies are seen as two distinct persons and are able to control production and supply activities on one hand and TSO or transmission system activities on the other. The measure permits EU Member State governments to own and control both the TSO and the production or supply functions, whereas third-country service suppliers, including Gazprom, are under obligation to divest their transmission assets according to unbundling requirements in the first paragraph of the same Article. Croatia, Hungary and Lithuania have each implemented versions of this measure in their respective national legislations. Russia considers that the implemented legislations

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87 Directive 2009/73/EC, Article 11.3 (b) (i)-(iii).
88 Talus (n 75) 82.
violate *de jure* the national treatment obligation of these Member states. In addition, Russia submits that since Croatia and Lithuania both own and control the TSO and production of supply portions of the single vertically integrated undertakings supplying transport services in their respective territories, the measures are also *de facto* inconsistent with the national treatment obligation of Croatia and Lithuania.\(^89\)

Secondly, with respect to the third-country certification clause, Russia claims the violation of the national treatment principle noting that Croatia, Hungary and Lithuania have each implemented versions of the third-country certification measure, which according to Russia leads to more favourable treatment of the services and service suppliers from the EU Member States than those from outside the EU.\(^90\) TSOs and transmission system owners located and controlled in EU Member States are not subject to the certification measures. As illustrated, several measures could be in violation of Croatia’s, Hungary’s and Lithuania’s national treatment obligation under Article XVII of the GATS, and therefore the question whether the challenged measures are inconsistent with the said obligation will be examined in consolidation in this section, starting with a description on how the principle is applied.

In order to examine the consistency of the challenged measures with the GATS provision on national treatment, a four-tier test of consistency is required. The WTO panel in several cases has followed the same analytical approach.\(^91\) This four-tier test requires examining: (i) whether a national treatment commitment has been made in respect of the relevant subsector and the relevant mode of supply; (ii) whether the measure by the Member at issue ‘affects’ trade in services; (iii) whether the domestic and foreign services or service suppliers are ‘like’; and (iv) whether the foreign services or service suppliers are accorded ‘treatment no less favourable’ than those of domestic origin.\(^92\) These elements will be examined separately below.

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\(^90\) Ibid 3.


\(^92\) Van den Bossche & Zdouc (n 4) 406.
The first element of the analysis is to determine whether Croatia, Hungary and Lithuania have made commitments on national treatment in the relevant sector and modes of supply. As determined above in section 4.3, the European Union itself cannot infringe Article XVII of the GATS, but Hungary, Croatia and Lithuania have each undertaken commitments with respect to supply on commercial presence regarding transport services via pipeline.

The second element of the test of consistency calls for an analysis of whether Croatia’s, Hungary’s and Lithuania’s measures (the special ownership unbundling requirement for public TSOs and the implementation of the third-country certification requirement) affect the trade in services to fall within the scope of GATS. According to the Appellate Body in Canada – Automotive Industry two key legal issues must be examined. Firstly, whether there is “trade in services”, and, secondly, whether the measure at issue “affects” the trade.93 As it has been discussed in section 4.2, the term ‘services’ is not defined in the GATS. The services at issue are supplied in mode 3 through commercial presence. Transmission of gas constitutes a pipeline transport service within the meaning of the GATS. With respect to the second component, it needs to be determined whether the measures ‘affect’ the gas transmission services by service suppliers from other Members. Measures by Members that affect trade in services are defined non-exhaustively in Article XXVIII (c), which include measures in respect of the presence, including commercial presence, of persons of a Member for the supply of a service in the territory of another Member. The term ‘affect’ has a broad scope of application. It covers more than just to ‘regulate’ or ‘govern’. A measure that affects trade in services applies to any measures that bear upon the conditions of competition in supply of a service.94 Both the ownership unbundling requirement for public vertically integrated undertakings and the third-country certification regime, including the security of energy supply assessment, regulate the terms on which gas transportation services may be provided. The unbundling requirements and the third-country certification clause not only regulate the terms on which gas transportation services may be supplied in the European natural gas market, but also prevent any third-country undertaking from

holding an interest in transportation infrastructure activities, unless the company meets the requirements. To conclude, there is no doubt that the measures fall under the scope ‘affect trade in services’ and bear upon conditions of competition.

The next question that needs to be considered is whether the domestic and foreign services or service suppliers at issue are ‘like’, since the national treatment obligation prohibits discrimination only between ‘like services’ or ‘like service suppliers’. According to the Panel in EC – Bananas III and Canada – Automotive Industry, to the extent the service suppliers provide like services, they are considered like service suppliers. Therefore the likeness of services shall be determined before the likeness of the service suppliers. ‘Like’ services include ‘directly competitive or substitutable’ services. The determination of the likeness of services is made on a case-by-case basis. Physical characteristics are irrelevant. The test has generally followed a classification scheme, which is based on the United Nations Central Product Classification; the GATS sub-sector classification in scheduling commitments follows closely the same scheme. Services classified in different sub-sectors in the schedules can be regarded as a sufficient factor for considering them unlike. Gas transportation provided by any service supplier falls within the same sub-sector, namely the ‘pipeline transportation of fuels’. Other factors for the assessment are potential end uses and consumer habits and preferences. End-uses offer an appropriate basis for the likeness test, since this factor shows whether the services are competitive and consumers would treat them as substitutes. The end uses of gas include power generation, metallurgy and agrochemistry. Furthermore gas can be used by household consumers or at the utility sector. When it comes to consumer habits, the supply of gas by a Russian supplier versus for example a German supplier makes basically no difference; the houses will be heated exactly the same way. The only concern that a consumer might have could be the reliability of the energy supply. The starting point in this thesis is thus that the services

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95 GATS, Article XVII:1 and Van den Bossche & Zdouc, 409-12.
97 Mattoo Aaditya, ‘National Treatment in the GATS: Corner Stone or Pandora’s Box?’ (1997) 31 Journal of World Trade 107, 127.
98 Van den Bossche & Zdouc (n 4) 327.
99 Mattoo (n 97) 128.
100 Van den Bergh (n 71) 247.
provided by Russian service suppliers of pipeline services and those of other third countries or of EU Member States are like.

The relevant players that are affected by the measures are third-country service suppliers of natural gas. While the measures seem to be targeted at Gazprom, they affect its competitors also, including for example Naftogaz, which is a Ukrainian fuel and energy complex. The test of ‘like service suppliers’ requires comparing these third-country service suppliers to domestic service suppliers originating in EU Member States. As pointed out above, given that third-country suppliers provide like services, it can be presumed that the third-country supply and transmission providers that provide like services to those from EU Member States, are also like service suppliers. However, the panel could take into account other factors, like the size of the companies, their assets, and their ownership structures.  

The third-country certification clause makes no distinction between private and state owned undertakings; neither does the ‘unbundling’ preclude the possibility of the public ownership of the transmission system operators. It is therefore quite likely that third-country service suppliers, including Gazprom, Naftogaz etc, whether they are state-owned or private, provide like services and are therefore considered to be like service suppliers.

The fourth and the last element that remains to be addressed relates to the question of whether the Croatia’s, Hungary’s and Lithuania’s measures accord foreign services or service suppliers ‘treatment no less favourable’ than to the like services and service suppliers of domestic origin. According to Article XVII:3 the treatment is considered less favourable if it modifies the conditions of competition in favour of domestic services or service suppliers. The obligation is met through formally identical or formally different treatment and covers both de jure and de facto discrimination. The examination of the question involves two elements: firstly, how do the measures provide different treatment between domestic services and service suppliers and like services and service suppliers of other third countries, and secondly, does that different treatment amount to less favourable treatment?

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101 Van den Bossche & Zdouc (n 4) 327.
102 Van Hoorn (n 56) 69.
103 Van Hoorn (n 56) 67.
Some authors argue that the special ownership unbundling requirement for public bodies shall not be interpreted as being inconsistent with the national treatment obligation. Even though it may seem like Croatia, Hungary and Lithuania are according their own like services and service suppliers more favourable treatment, both de jure and de facto by owning and controlling TSOs in their respective territory, the ownership unbundling requirements are nevertheless complied if two separate bodies exercise control over a TSO on one hand and over production and supply portions on the other. Third-country service suppliers can reasonably be expected to comply with the requirement. Furthermore EU Member States are not under obligation to privatize their transmission assets, except in Lithuania where the other two unbundling models are not available.\textsuperscript{105} Even if different treatment can be seen here, it is difficult to argue that it could give a competitive advantage to the service suppliers VIUs owned by Member States. This thesis supports also the conclusion that the provision shall not be interpreted as being inconsistent with the national treatment obligation. To conclude, to the extent that when the owner of the VIU is a Member state or another public body and two separate public bodies are deemed to be the same person or persons, there is no favourable treatment. Hence Croatia, Hungary and Lithuania can not be considered breaching the Article XVII of the GATS.

As regards to the third-country certification clause, it has already been noted that when certification is requested by a TSO controlled by a person or persons from a third country, the Gas Directive requires that the request shall be refused, unless the undertaking passes the security of energy supply assessment. The domestic service suppliers are not subject to similar requirements or assessments. Hungary, Croatia and Lithuania, who have implemented versions of this Article in their national legislations are clearly violating their special commitments regarding the national treatment principle, because there is an additional requirement for third-country undertakings, concerning the security of supply, which makes the treatment accorded to foreign service suppliers formally different. Now, before making any conclusions, the additional requirement calls for an analysis on whether the different treatment gives a competitive advantage to the domestic transmission system owners and TSOs. It is

\textsuperscript{105} Dralle Tillman, 'Guest post: Conflict between EU competition law in the energy sector and WTO law: Russia’s challenge against "unbundling"' (2016) <przegladpm.blogspot.se/2016/02/guest-post-conflict-between-eu.html> accessed 3 August 2016.
probably safe to say, that when third-country undertakings are not granted the certification, they suffer a competitive disadvantage. Not being approved and designated as transmission system operators by Member States means that the companies are not allowed to control transmission systems and supply natural gas to the market. Consequently, not being able to supply gas means that the company is left out of the competition. Other authors, who suggest that it would actually be difficult to demonstrate that the clause and the security assessment would not represent a formally different treatment and that a violation of the national treatment principle is evident, support this same conclusion.\footnote{Cottier et al (n 15) 11.} Therefore it is very likely that the panel will consider that Croatia, Hungary and Lithuania are breaching their special commitments on national treatment obligation in respect of the third-country certification clause. Note however, that the clause in the Gas Directive does not contravene with the EU’s obligations under the said principle.

In conclusion, the likelihood that the Panel will interpret the special ownership unbundling requirements for public system operators not being inconsistent with the NT obligation in the GATS is fairly large, considering that third-country undertakings provide like services and the treatment accorded to public system operators does not affect the conditions of competition to their detriment. With regard to the third-country certification clause, the clause might not withstand the standard required by the NT treatment obligation. The measure would fall within the scope of the GATS and survive the likeness test, but since there is an additional requirement for third-country undertakings which amount to formally different treatment of third-country undertakings being prohibited from controlling the gas networks, they will find themselves in a worse competitive position as the European undertakings. Therefore it is likely that the Panel will find that Article XVII of the GATS is breached.
4.7 Claims of Violation of the MFN Treatment Commitment under Article II:1 of the GATS

Besides the claims based upon the possible violation of the National Treatment obligation of the EU and its Member States, Russia has submitted that several issues in the third energy package are in conflict with the most-favoured-nation treatment obligation, which is one of the basic provisions of the GATS provided in the Article II:1. This section aims to evaluate whether, and to what extent, the issues challenged by Russia will find validation by the WTO panel. The evaluation in this thesis is reduced to concern the following questions identified in the request for the establishment of a panel by Russia: (1) do the three alternative unbundling models result to less favourable treatment under the MFN treatment principle; (2) is the third-country clause inconsistent de jure with the EU Member States obligations; and finally, (3) did the EU accord Russian service and service suppliers less favourable treatment when the Commission refused to approve Poland’s certification of Gaz-System S.A. as ISO for the Polish section of the Yamal pipeline?107

The MFN treatment obligation is the second main non-discrimination provision of the GATS. It aims to ensure all WTO Member States equality of opportunity to supply like services, by prohibiting discrimination between like services and service suppliers from different countries and ensuring that no Member is favoured over other. In other words, a WTO Member may not give services and service suppliers from another WTO Member State treatment less favourable than it gives to like trading partners from any other WTO Member, or other country.108 Unlike the national treatment principle, all Members are bound by the MFN principle regardless of any specific commitments made by them.109 According to Article II:2 of the GATS, derogations from the this general obligation can be made only by listing specific exemptions when becoming a member of the WTO. This is called the ‘negative list’ approach. The EU did not claim any exemptions relevant to the energy sector at the time of its accession. Therefore it has a full obligation to guarantee MFN treatment to all WTO Members.

108 Van den Bossche & Zdouc (n 4) 335.
109 Van den Bergh (n 71) 250.
The test of consistency with Article II:1 consists of examining three questions: (1) does the measure at issue fall within the scope of application of Article II:1 of the GATS; (2) are the services or service suppliers ‘like’; and (3) are like services and service suppliers accorded ‘treatment less favourable’.\textsuperscript{110} The MFN principle is applicable to all scheduled and non-scheduled services.\textsuperscript{111} As stated above, transmission of gas constitutes a service under the WTO law and hence falls within the scope of GATS. The second question calls for the testing of the likeness of services and service suppliers, which has already been addressed in section 4.6 of this thesis. Because the same evaluation affects the consistency test of the MFN treatment obligation, no further elaboration will be needed here. It is sufficient to remind that the services and third-country undertakings are like. Subsequently, the final question that remains to be addressed is whether the measures infringe the MFN obligation? Article II:1 of the GATS provides in relevant part that: “each Member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than that it accords to like services and service suppliers of any other country.”

The Article does not provide any further guidance on what does the concept ‘treatment no less favourable’ mean, but Article XVII of the GATS on the national treatment obligation can be used as guidance. In the context of Article XVII a measure is considered less favourable if it modifies the conditions of competition in favour of services or service suppliers of the domestic service or service supplier. The Appellate Body concluded in \textit{EC – Bananas III} that the scope of the concept is analogous with the one of Article II:1, and hence the MFN treatment obligation applies to both \textit{de jure} and \textit{de facto} discrimination.\textsuperscript{112}

Russia considers that the three alternative unbundling measures result in less favourable treatment being accorded to Russian pipeline transport services and service suppliers, than to like services and service suppliers of other third countries. Certain Member States, like Lithuania and Estonia, have adopted national implementing legislation

\textsuperscript{111} Cottier et al (n 15) 10.
\textsuperscript{112} Van den Bossche & Zdouc (n 4) 344-45.
which allows only the ownership unbundling model, whereas other Member States permit the ISO and/or ITO model besides the ownership unbundling, which allows VIUs in these other states to maintain ownership and varying degrees of control over both the TSO and the production and supply portions. In countries where the ownership unbundling is the only available model, Russia has been required to cede control in the TSO on the basis of the legislation.113 This, according to Russia, grants an advantage to third-country natural gas suppliers.

Two legal problems can be identified with this claim. The first question is whether the variety of unbundling models could violate the MFN clause? The EU Member States were free to choose which system for unbundling they would implement in the national legislation, as long as the system of unbundling is effective in removing conflict of interests between producers, suppliers and TSOs.114 Several authors are of the view that the multi-model Directive is consistent with the MFN treatment obligation, because the MFN treatment obligation could not be used to enforce merely regulatory uniformity among the national legislations of the Member States.115 This thesis supports the same view. It is hard to see how the variety of legislations could modify the conditions of competition between third countries. The variety of unbundling models shall therefore be interpreted as consistent with the MFN treatment obligation.

The second issue in respect with the three alternative models is whether adopting implementing legislation requiring the full ownership unbundling model breaches the MFN treatment obligation? National legislation providing only the full ownership unbundling model does not violate the MFN treatment obligation, since the same treatment will be accorded to all suppliers of natural gas on the market of that particular Member State. Only different treatment of like services and service suppliers constitutes

114 Directive 2009/73/EC, Recital (9).
discrimination within the meaning of Article II:1. Therefore Russia’s claim would most likely not find validation in the WTO panel.

Next, Russia considers that the third-country certification measures are inconsistent *de jure* with the MFN treatment obligation. The extension of the unbundling provisions to external service suppliers is set forth in Article 11 of the Gas Directive. The problem lies in the third paragraph, which imposes third-country undertakings to the additional security of supply assessment. Although it may seem that same conditions apply to all third-country undertakings, certification requests by transmission system owners and TSOs located in one EU Member State and controlled by a person or persons of another EU Member State are not subject to the third-country certification clause, despite the fact that each EU Member State is also a WTO Member. Under the MFN treatment obligation same treatment shall be accorded immediately and unconditionally to like service providers. As an example, a TSO located in Germany but controlled by a Russian undertaking would be accorded different treatment than a hypothetical Finnish TSO on the same market, although Finland is also a WTO Member. A more potential violation is however connected to the fact that the security of supply assessment is made case-by-case and amounts to *de facto* discrimination. In addition to specific facts of the case and the third country concerned, the regulatory authority shall take into account the existence of an agreement between the EU and the third country in question. The assessment may lead to the situation that two like TSOs from third countries satisfy the unbundling requirements of the Directive, but given the subjective assessment and agreements made, only one of them would be certified. This obviously violates the requirement of granting immediate and unconditional advantage to all Members and results to less favourable treatment.

The case of refusal of certification of Gaz-System S.A. as an ISO for the Polish section of the Yamal-Europe Pipeline is also interesting in this context. The transnational Yamal-Europe gas pipeline runs across Russia, Belarus, Poland and Germany, and is owned by a Russian-Polish joint venture Europolgaz. The Commission required Poland to conduct the security of energy supply assessment, though according to Russia’s

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117 European Commission Opinion of XXX pursuant to Article 3(1) of Regulation (EC) No 715/2009 and Article 10(6) and 11(6) of Directive 2009/73/EC - Poland - Certification of Gaz-System as the operator of the Polish section of Yamal-Europe Pipeline.
request, at least two other third-country TSOs, owned by 100 per cent up to third-country persons, were previously approved without the assessment having been made. Russia argues that the EU accorded Russian services and service suppliers less favourable treatment than like services and service suppliers of the third countries that received the certification. Again, if as soon as the EU grants a certification to a third country without the security of supply assessment, all other third countries shall be entitled to the same treatment.

In conclusion, it is unlikely that Russia will succeed with its argument that the multi-model Directive breaches the MFN treatment obligation of the EU or its Member States, because. The outcome of Russia’s claim relating to the third-country clause might instead find validation by the WTO panel, although some authors believe that the panel might be reluctant to interfere in the EU’s discretion.\(^{118}\) The MFN treatment principle could be a legitimate base to denounce the requirement of a security of supply assessment for third-country TSOs, especially in a particular case of two like third-country TSOs both satisfying the unbundling requirements but only one being granted the certification. The factual consideration might violate the requirement of granting any advantage immediately and unconditionally to all Members. As we will see in section 4.10, the EU could however justify the third-country certification measures under general exceptions to the principle present in the GATS.

### 4.8 Claim of Violation of the Market Access Commitment under Article XVI of the GATS

This section will analyse Russia’s argument regarding the violation of the market access commitments. There is no general definition of the term ‘market access’. Instead, it is defined through six types of market access barriers, provided in an exhaustive list in Article XVI:2, that shall not be maintained or adopted, unless otherwise specified in the Members’ Schedules. The first paragraph of Article obliges to accord services and service suppliers of other Members no less favourable treatment than that provided for under the terms, limitations and conditions agreed and specified in its Schedule. The

\(^{118}\) Pradel & Grigorova (n 115).
sub-paragraphs (a)-(d) concern quantitative limitations on market access, sub-paragraph (e) concern measures that restrict or require specific types of legal entity or joint venture, and the last one (f) identifies limitations on the participation of foreign capital. The market access barriers apply equally to discriminatory and non-discriminatory measures.

Russia argues that the unbundling measures, as implemented in the national laws of Croatia, Hungary and Lithuania, are inconsistent with these Members’ market access obligations. Moreover, according to Russia’s request, these countries are maintaining and adopting measures set out in Article XVI:2 of the GATS. Russia does not refer to any specific sub-paragraphs of Article XVI:2 or specify in its arguments in which way exactly the prohibition for gas producers and suppliers to supply gas transmission services amounts to an impermissible market access. However, the unbundling measures could potentially amount to de facto quantitative limitations, such as a limitation on the number of service suppliers, the supply of services by state owned companies or restriction of specific types of legal entities. Since some third-country VIUs will not be able to comply with the unbundling requirements due to their domestic regulations, the unbundling measures will inevitably limit on the number of third-country undertakings operating in the pipeline transportation services and investments could be ruled out.

The GATS does not provide for a general prohibition on the market access barriers – the market access provisions apply only to the extent that the Members have made specific commitments in the Schedules of concessions on the relevant services sector. As noted in section 4.3, the relevant entries of Croatia and Lithuania for mode 3 on commercial presence read "none", which indicates that they have undertaken to provide full market access within the meaning of Article XVI in respect of pipeline transport services and are thus committed not to maintain any of the types of measures listed in the six sub-paragraphs of Article XVI:2. Hungary has also made a market access

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120 Van den Bossche & Zdouc (n 4) 514-18.
122 Van den Bossche & Zdouc (n 4) 517.
commitment for pipeline transport services in mode 3, and has added that services may be provided through a contract of concession granted by the state or the local authority.

Having examined the commitments of the Member States, an analysis of the consistency of the unbundling measures with Article XVI of the GATS is the next step. To date the main dispute dealing with the market access obligation is the US – Gambling, where Antigua claimed that a number of US law on gambling and betting were inconsistent with the market access obligation, since they restricted the ability of companies to provide remote gambling and betting services. The dispute is relevant at the current issue, since the panel took the view that maintaining a ban on a certain method of service supply is covered by Article XVI even if the measure does not specify a numeric quantity but effectively limits the service suppliers and service operations relating to that service to zero. In such case the ban is a ‘zero quota’ and thus constitutes a ‘limitation on the number of service suppliers in the form of numerical quotas within the meaning’ of the provision. An example of such limitation could be a nationality requirement for suppliers of services.123

As it can be concluded from the panel report, a market access barrier in form of a quantitative restriction can be expressed numerically of through the criteria specified in the provisions, such as an economical needs test for example The question is therefore whether the unbundling measures constitute a limitation on the number of service suppliers in the form of numerical quotas and are inconsistent with Article XVI? It has been argued by some scholars that the unbundling measures, including all the alternatives, do not breach the market access obligation of the Croatia, Lithuania and Hungary, since the measures prohibit only specific service providers from supplying transmission services, depending on their supplier-related characteristics.124 Thus the ban never results to ‘zero quota’ because it is not in a general manner.

123 Lester et al (n 119) 664.
124 Dralle (n 105).
4.9 Claims of Violation under Article VI of the GATS

In addition to market access barriers, trade in services can be imposed to other significant barriers, such as unfair and arbitrary application of national trade measures or licensing and qualification requirements and technical standards. Russia has submitted, first, that ‘given the general applicability of the certification requirement, Croatia, Hungary and Lithuania do not administer the third-country certification measure in a reasonable, objective and impartial manner, contrary to these Members’ obligations under GATS Article VI:1’.125 Second, Russia considers that the third-country certification measure is constituting a licensing and qualification requirement that nullifies and impairs the specific commitments of Croatia, Hungary and Lithuania in the pipeline transport services sector, inconsistent with Article VI:5 (a) GATS. Since Russia does not explicitly specify in what way the administration of the third-country certification measure in these Member states it finds to be inconsistent with the GATS, it is fair to focus on only describing the application of the Article, rather than speculating the findings of the panel.

Article VI of the GATS is the domestic regulation provision, which has six subsections, only one of them being generally applicable to all WTO Members (paragraph 2). Four of the paragraphs (1, 3, 5 and 6) apply, without limitation, only to service sectors where Members have made specific commitments. Since Croatia, Hungary and Lithuania have included pipeline transportation of fuels in their Schedules, they will be obligated to comply with paragraphs 1 and 5. By virtue of Article VI:1 of the GATS Member States will have to ensure that their measures of general application are administered in a ‘reasonable, objective, and impartial manner’. Aiming to ensure procedural fairness, these three requirements are limited to apply specifically to the manner of administration of laws, regulations and rulings. Also the administrative processes leading to administrative decisions would fall within the scope of application of the Article. The substantive content of the legal instruments being administered cannot be

challenged under this provision. The three requirements are legally independent, therefore if the panel would find a violation of any of them, that would lead to a violation of Article VI:1. The focus of the assessment lies on the treatment accorded by government authorities to the traders of services from third countries, and not on whether there has been discriminatory treatment in favour of other Members. The panel will have to examine the real effect that a third-country certification measure has on traders of services, involving the possible impact on the competition due to unreasonable, not objective and partial application of a law, regulation, decision or ruling, however it is not required to show any trade damages. Furthermore, in order to find a violation of the provision, Croatia’s, Hungary’s and Lithuania’s actions would have to have a significant impact on the overall administration of the law, and not simply on the outcome in a single case.

As far as the second claim is concerned, under the Article VI:5 Members can adopt measures relating to qualification requirements and procedures, technical standards, and licensing requirements with respect to services for which they have listed specific commitments. If the adopted measures nullify or impair commitments, they must be based on objective and transparent criteria. It should however be borne in mind that the provision is applicable only during the time period in which disciplines for the particular services are pending, and shall not apply licensing and qualification requirements or technical standards that nullify or impair commitments in sectors in which a Member has undertaken specific commitments during the time period in which disciplines for the particular services sector have not yet been developed. In short, as long as disciplines for the pipeline transportation of fuel have not been developed, the paragraph is applicable. The compliance with Article VI:5 at the current issue

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129 Van den Bossche & Zdouc (n 4) 502-07.
130 See further Van den Bossche & Zdouc (n 4) 533.
131 Trachtman (n 126) 212.
involves testing two components: firstly, are the rules relating to the third-country certification considered as licensing or qualification requirements that are subject to the disciplines of the provision, and secondly, do they nullify or impair specific commitments? The provision covers measures that affect the competition if they are adopted after the commitments were made. Needless to say, compliance with the third-country regime contained in the national regulation is a condition for entering the gas market. Such condition creates obstacles to trade in services by complicating the entry into natural gas market in Croatia, Hungary and Lithuania by foreign service suppliers, and in the worst case excludes the third-country undertakings not complying with the requirements or passing the security assessments. Hence, the certification rule is a licensing or a qualification requirement that is subject to the disciplines of Article VI:5.

The next question is then whether the measures by Croatia, Hungary and Lithuania nullify or impair the commitments made by them? Under the provision, licensing and qualification requirements shall be based on objective and transparent criteria, that could have been reasonably expected at the time commitments were made, meaning that they are not more restrictive to trade than old rules, and they shall not be more burdensome than necessary to ensure the quality of the service. Compliance with the necessity requirement involves a process of balancing and weighing several factors, such as the importance of the common interests protected by the law and the accompanying impact of the law. If the third-country certification rules in Croatia, Hungary and Lithuania are more restrictive to trade in services, obviously they could have not been expected by third countries. The panel will also have to do a similar necessity test as it will be discussed in the following section, that is, are there less trade restrictive alternatives reasonably available and are the measures defensible. As can be seen from this brief summary, determining whether the Members comply with the domestic regulation provision is complex and uncertain.

\[ \text{132 Ibid 214.} \]
\[ \text{133 Ibid.} \]
\[ \text{134 Luff David, 'Regulation of Health Services and International Trade Law' in Mattoo Aaditya, Sauvé Pierre (eds) Domestic Regulation & Service Trade Liberalization (World Bank and Oxford University Press 2003) 206.} \]
4.10 Justifications under Article XIV of the GATS

After having examined the measures challenged by the Russian Federation in the context of the GATS and concluded that the claims regarding the inconsistency of the third-country clause could find validation by the WTO Panel, this section discusses the possibility for the violations of the obligations, in particular the third-country clause, being still justifiable. The WTO Members are under specific conditions allowed to adopt and maintain legislation and measures that deviate from the obligations under GATS. The exceptions apply also to the obligations related to specific commitments. The WTO law recognises ‘general exceptions’ and ‘security exceptions’, that allow promoting, protecting and giving priority to certain societal values and interest over trade restrictive legislation, such as market access and non-discrimination rules. These general and security exceptions are slightly different in scope and nature. The relevant articles are provided in Articles XIV (General Exceptions) and XIV bis (Security Exceptions), however the last mentioned are used in very exceptional circumstances and will not be assessed in this context.\textsuperscript{135}

Assuming that the panel would establish that the third-country measure is inconsistent with the principles in the GATS, the burden of the proof shifts to the responding party and the EU would need to invoke the exceptions.\textsuperscript{136} The EU and its Member States could defend the measures from Russian claims by pleading to either the exception under Article XIV paragraph (a) which deals with measures which are necessary to protect public morals or to maintain public order, or paragraph (c) which can justify otherwise GATS-inconsistent measures which are necessary to secure compliance with laws and regulations which are not inconsistent with the provisions of the GATS. In order to examine whether the measure can be justified, Article XIV contemplates a two-tier test. The analysis starts with determining whether the challenged measure falls within the scope of one of the paragraphs of Article XIV – in this case either paragraph (a) or (c). The measure shall address the particular interest and there shall be a sufficient degree of connection between the measure and the interest protected. The next step of the test implies that the measure complies also with the requirement of the \textit{chapeau},

\textsuperscript{135} Van den Bossche & Zdouc (n 4) 544.
\textsuperscript{136} Cottier et al (n 15) 13.
which states that the measure shall not lead to arbitrary or unjustifiable discrimination between countries, or a disguised restriction on trade in services.\(^{137}\)

The paragraph (a) sets forth that measures inconsistent with substantive disciplines imposed by the GATS may be justifiable if they are necessary to protect public morals or to maintain public order.\(^{138}\) So the question is can the third-country regime be justified under this provision? The panel found in \textit{US – Gambling} that Members shall be given some scope to define and apply for themselves the concept of ‘public morals’ and ‘public order’ according to their own systems and scales of values.\(^{139}\) Moreover, the WTO Members have a right to achieve a desired level of protection with respect to the objective pursued in paragraph (a).\(^{140}\) The EU seems to have defined the concept in the recital 22 of the Gas Directive by explaining that the security of energy supply is an essential element of public security and connected to the efficient functioning of the internal gas market. With regard to ‘public order’ the footnote 5 to the paragraph (a) states that the exception may be invoked only if a genuine and sufficiently serious threat is posed to one of the fundamental interests of society. Fundamental interests of society are, just to name some, standards of law, security and moral.\(^{141}\) The recital explains further that the gas transmission system sector is considered being of high importance to the Community and therefore additional safeguards are necessary for avoiding threat to public order and public security and the welfare of the citizens of the EU.\(^{142}\) Keeping in mind that the concept has traditionally been dynamic it can be assumed that the EU’s aim of securing the energy supply could qualify as a matter of public order.\(^{143}\) The level of importance or seriousness of threat required by footnote 5 is a question that will require a balancing assessment by the panel. Given the political sensitivity of the issues and the geopolitical character of the natural gas market, it is possible that the WTO panel would be reluctant to interfere the issues. The European Union might actually be having quite a powerful legal instrument in its hands.

\(^{137}\) Van den Bossche & Zdouc (n 4) 584.
\(^{138}\) GATS, Article XIV(a).
\(^{139}\) Van den Bossche & Zdouc (n 4) 586.
\(^{142}\) Directive 2009/73/EC, Recital (22).
\(^{143}\) Van Hoorn (n 56) 71.
With regard to the necessity of the measure, the Appellate body found in *US – Gambling* that a measure is necessary if there is no reasonably available, WTO-consistent alternative for it. In determining whether the measure is necessary, the panel will assess the importance of the interests and values that the measure protects, the extent to which the measure contributes to the realization of the end pursued, and its impact on trade.\(^{144}\) Keeping in mind that the Commission originally proposed a complete prohibition of the control of transmission systems or TSOs by persons of third countries, the requirement for third parties to obtain certification and going through a security of supply assessment is already a lighter deviation from the obligation of granting market access to all Members under GATS.\(^{145}\) A less restrictive alternative would be only to require similar security of supply test from all undertakings active within the EU; however that could also lead to *de facto* discrimination as we have seen earlier in this thesis. With respect to the impact on trade, the Appellate Body stated in *Korea – Various Measures on Beef* that a measure with a relatively slight impact on international commerce might more easily be considered as necessary than measures that are intense or have broader restrictive effects.\(^{146}\) The third-country certification requirement and the security of supply assessment will affect the execution of the existing contracts and future investments and fundamentally the trade.\(^{147}\)

The paragraph (c) could also be invoked by the EU. A Member invoking this paragraph must show that the measure is designed and necessary for securing compliance with GATS-consistent national laws or regulations. If on the basis of the analysis in the previous chapters it is assumed that the unbundling requirements are consistent with the WTO law, the next question is whether the measures for which justification is sought enforce the obligations contained in the laws and regulations rather than only the attainment of the objectives of laws and regulations. It is sufficient that securing the compliance is part of the reason to put the measure into place.\(^{148}\) Some authors question whether the certification procedure adds any value for functioning gas markets or the

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\(^{144}\) Van den Bossche & Zdouc (n 4) 587.


\(^{147}\) Van den Bergh (n 71) 255.

\(^{148}\) Van den Bossche & Zdouc (n 4) 591.
security of supply, since the undertakings active in the European Union natural gas market are often European subsidies which already satisfy the unbundling requirements anyway, and moreover the clause would lead to an extraterritorial application of unbundling regime.\textsuperscript{149}

The third-country clause must finally also meet the requirements of the \textit{chapeau} of the Article XIV GATS.\textsuperscript{150} The chapeau identifies that any measures are not to be applied in a manner, which constitutes “arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on trade in services”.\textsuperscript{151} Moreover, the chapeau imposes the obligation to undertake negotiations in good faith before taking any unilateral measures. Here the existing agreements and on-going negotiations with Russia must be taken into consideration. The conclusion that can be drawn from this it that even though the justifications are a powerful legal instrument, it is not certain that the third-country measure will benefit from the exception of Article XIV. Other scholars do not either see any possible justifications under the Article.\textsuperscript{152}

Firstly, it is not clear whether the security of energy supply could fall within the scope of paragraphs (a) or the (c). Secondly, the necessity of the measures and the existence of a genuine and sufficiently serious threat posed to one of the fundamental interests of society are questions where the WTO panel will have to apply a balancing test. However, given political sensitivity of the issues involved it will be interesting to see which conclusion the Panel will draw if the justifications are invoked.

\subsection*{4.11 Summary}

The results of the discussion in this chapter are summarised as follows. This chapter has provided an insight to Russia’s claims and evaluated the alleged violations of obligations in the GATS agreement, which covers issues regarding energy transmission, distribution and related services. It has been verified that the EU has made no

\textsuperscript{149} Van Hoorn (n 56) 58.
\textsuperscript{151} GATS, Article XIV.
commitments with regard to pipeline transport services under the current schedule of concession, but some Member States, including Croatia, Hungary and Lithuania have submitted separate GATS Schedules which include market access, national treatment and domestic regulation commitments for pipeline transport services. Having identified the measures in the third energy package that Russia considers discriminatory and contradictory with WTO legal principles, this thesis submits that it is quite likely that many of the claims regarding the unbundling measures will not find validation by the panel. The likelihood that the panel will interpret the special ownership unbundling requirements for public systems operators not being inconsistent with the NT obligation is large. As illustrated, the variety of unbundling models among the EU Member States does neither give rise to a violation of the MFN treatment principle. Lastly, the various unbundling measures do not seem to breach the market access obligation of Croatia, Lithuania and Hungary, because the measures do not result to zero quota.

As regards to the third-country certification regime, the following observations are most important. To begin with, it is possible to conclude that the third-country clause with its additional requirement regarding the security of supply targeted at foreign actors represents formally different treatment under the NT principle, because third-country undertakings will find themselves in a worse competitive position as the European undertakings. Furthermore, there are conditions to report the third-country regime and the requirement of a security of supply assessment for third-country TSOs discriminatory under the MFN principle, especially if two like third-country TSOs both satisfy the unbundling requirements but only one is granted the certification. Lastly, this thesis has demonstrated that there might not be any justifications for deviating from the most-favoured-nation or the national treatment principles at hand, but because the issue is geopolitically very charged, it will be interesting to see how the panel will evaluate the necessity of the measures and the existence of a genuine and sufficiently serious threat to the fundamental interests of society in the European Union.
5 Concluding Remarks

With the aim of evaluating the legitimacy of the claims as regards to unbundling and the third-country regime, raised by the Russian Federation in its request for the establishment of a panel, this thesis has analysed the compatibility of the clauses with the obligations under the current WTO law, more specifically the GATS. In the overall conclusions, the dispute filed by the Russian Federation against the EU over regulations in the energy sector show that the third energy package raises a number of potential concerns regarding the consistency with the WTO law. Returning to the claims submitted by Russia, the assessment made in this thesis demonstrates that some Articles in the Directive 2009/73/EC and the national implementations could potentially breach the EU’s and its Members States obligations imposed by the GATS. It seems that the third-country certification clause will most likely be interpreted as inconsistent with the MFN and NT obligations of the GATS, while the unbundling measures most likely do not give rise to any violation. This conclusion is based on the fact that gas imported from Russia, or any third country, does not appear to have a competitive disadvantage. The dispute is interesting because it shows how the measures in the third energy package may affect the trade between EU and Russia in natural gas. Furthermore the dispute provides the dispute settlement body an opportunity to address issues regarding trade in energy and it will definitely be one of the most important energy disputes in the WTO framework. The dispute may also serve as a further incentive towards the development of a more comprehensive agreement on energy within the WTO framework, but most definitely the result will impact the applicability of WTO law and the future cooperation between the EU and Russia.
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