



The Centre for Polish-Russian Dialogue and Understanding

RETHINKING EU-RUSSIA RELATIONSHIP

Interim Report
of the Polish-Russian Group on Difficult Matters

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Regardless of whether one believes in a polycentric world, the **new global circumstances** will be those of a **more balanced distribution of power**, better reflecting the spread of the world’s population. This new distribution will end the exceptional phenomenon of Western dominance in the last two centuries of world history.

The European Union and Russia should start preparing for a world in which new, emancipated powers, such as China, India, and others, will play a more prominent role while power and responsibility will need to be shared with them. The room for manoeuvre will be more limited but the possibilities for individual and collective success and achievement will be enormous. **We do not know whether this new reality will push the EU and Russia closer together or will lead them to become estranged**, focused on luring others into their fold. We have a joint stake in ensuring that the former becomes a reality.

In practical terms, the “globalisation premium” will apply more selectively to countries that are best-prepared for global competition in a number of areas. These include the mode of governance, economic model and social cohesion. **More than ever, the position of the European Union and Russia in the global order will be decided by developments inside our economies and societies.** We have a strong interest in moving in the same direction together.

This report concentrates on efforts to provide qualitative progress in EU-Russian relations in both the medium- and long-term perspective. It is necessary for both partners to set clear priorities for cooperation that should be focused on the most relevant issues, such as building trade and economic synergies that bolster the institutional foundations of cooperation, strengthening the rule of law, increasing mobility, shared neighbourhood, and wide range of challenges to international security.

The EU-Russian global partnership

The new mode of governance in the world is expressed in a number of ways. These include the **emergence of the G20 as a platform for exchange of views and coordinated action** of the twenty leading global economies. This body includes the four largest EU members and Russia and also EU institutional representation. G20 should not be seen as a rival to the UN Security Council, even if its agenda grows in substance and its status strengthens. It is a locus for

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regular meetings and proceedings based on chairmanship and troika leadership. It may over time turn into an institution on its own– if not prevented from it by questions over its legitimacy coming from the non-participants – with its rules of the game and specific commitments, an *acquis*. The jury is still out on that. However, the G20's contribution to addressing the on-going economic and financial crisis has confirmed its ability to deliver results. This is **an area where the EU and Russia should attempt to find a common denominator with a view toward developing joint initiatives and actions.**

Russia's forthcoming accession to the WTO will reinforce the international trade regime, which is particularly needed in the aftermath of the international financial and fiscal crisis. The EU and Russia are important players in the global market and their engagement can only increase, with the EU trying to identify new opportunities in the emerging countries and Russia having more and more capital at its disposal to earn a stable and solid return. They, therefore, have a stake in a strong global trading and investment regime.

The EU and Russia should build their relations upon two principles: constructive engagement and accountability. Both the EU and Russia should support a strong normative foundation of the international order. The precondition to that is Russian recognition of the specific nature of the EU, which is not a nation-state but a regional and global player functioning as a community of law as well as the EU's recognition of the traditional Russian attachment to the legal order. A proper grounding of the EU – Russia bilateral relations in the principles of the rule of law, democracy, and human rights will have an important impact on other emerging global players and draw them closer to the international normative regime.

Building economic synergies

In the world of ever more intensive rivalry, ensuring a high level of competitiveness and, thus, prosperity will be increasingly challenging. There will be less global liquidity than in the years before the economic crisis and weaker demand in Europe and other key markets. This means that **to unblock potential for growth, countries will need to undertake a lot of structural reforms.** Business environment, the strength of the legal system, and individual freedoms will become more important in assessing prospects for investment and trade.

The economic and social model in the EU is undergoing a profound transformation. The order of the day is managing the substantial debt overhang that accumulated during the crisis as governments took action to reduce the prospect of global stagnation. In parallel, there is an on-going search for new sources of growth to sustain and protect the current levels of prosperity. Russia has now joined the bulk of EU countries as a mature economy with a lower level of growth. The crisis has had a huge impact on its economy, with an 8 per cent fall of the GDP in 2009, spending a third of its foreign currency reserves, and it brought home the truth that **success in the new global economy requires reaching out to partners, diversifying the economy as well as resorting to new sources of growth.**

However, **Russia has an enormous potential to unleash**, comparable to that of the new EU member states, if it improves on its economic fundamentals. Russia has several competitive advantages, in particular, available financial capital, a well-developed educational system, and vast domestic markets - all of these offer excellent opportunities. There are precise niches, the potential of which is underutilized. For example, the EU could learn from Russian experience of prevention and dealing with consequences of emergency situations.

In general, the challenge of economic modernization is vast, which is why it makes sense to define more clearly the key issues in the current programme of cooperation. The priorities of the initiative should meet the internal development priorities of the EU and Russia until 2020. There is a need for a pragmatic approach to this area of cooperation.

With regard to the “Partnership for Modernization”, it is necessary to provide a balance between implementation of specific investment projects and setting up of proper conditions to encourage contacts and enhance business activities in Russia. The following issues should be taken into account: improving investment climate, modernizing legislation, fighting corruption, developing the judicial system as well as the system of commercialization of innovations. Russia could reach for the EU regulatory experience to help with modernizing the country. The EU could offer its well-functioning networks of governance by agencies to open this experience to Russian partners.

Russia is currently the world’s 10th largest economy. **It can become a leading global growth market** and the fifth world economy by 2020 if it undertakes further deregulation, streamlines its administration, scales down corruption and channels more resources into investment, both public and private. Just as EU economies have, the Russian economy can become leaner and more effective.

The Russian **commission on modernisation**, created in 2009, has come up with a number of recommendations, such as improving corporate governance and reducing corruption. Surely the Russian experience points towards avoidance of radical reforms which malfunctioned in the 1990s and led to abuse. Preference for an evolutionary change is entirely understandable as long as the end-result is satisfactory for Russia itself.

There is a lot Russia can benefit from by studying **the experience of Central European transformation** where a **strong emphasis was placed on deregulation and unleashing the entrepreneurial spirit of individuals**. It is no surprise that the Polish-Russian cooperation and trade is that of small and medium-sized enterprises while the German-Russian business dialogue consists of powerful industrial moguls. Importantly, deregulation was carried out in parallel with the **creation of powerful institutions** to oversee competition and respect the level-playing field among both the incumbent and new market actors. **The bottom-up approach** could benefit Russia also in the much cherished objectives of strengthening the innovative capacity of its economy, building up of the middle class, improving the context for innovation and „smart specialisation“

rather than support for the development of arbitrarily selected technologies and skills.

The Russian – EU interdependence is a puzzling issue, responsible for an important chunk of the trade deficit on the EU side (roughly speaking, in value terms, the EU imports from Russia are about twice its exports, at over € 60 billion). The EU's exports to Russia represent up to 6% of its total value exports, while its imports from Russia are around 10%. On the Russian side, the picture looks significantly different. The Russian exports to and imports from the EU are around half of the overall Russian trade. In both cases the EU is by far the most important Russian partner, compared to next-in-line China and the US. About 80% of the accumulated foreign investments into Russian economy come from the EU, which is more than U.S. \$ 200 billion. The volume of the accumulated Russian foreign direct investments into the EU economy is also impressive and equals U.S. \$ 90 billion. More than half of Russian investments are located in the EU.

The general trade imbalances are even more telling in the energy sector. The Russian fuels exported to the EU represent over three quarters of all its exports. Those, on the EU side, constitute a bit less than one third of its total energy import needs, with the remaining part coming mainly from the Middle East, North Africa and Norway. **While the EU as a whole remains fairly well-diversified in its energy imports, the regional discrepancies remain.** There are EU Member States in Central Europe that depend in 100% on their energy imports from Russia, particularly natural gas.

The EU – Russian economic relationship is excessively dominated by the energy issues. They add a strategic dimension to the relationship but often prove to be a poisoned chalice. On inspection they carry seeds of disagreement and, what is more, do not allow for the relationship to improve. Inevitably, as the supplier-nation, Russia tries to solidify its position on the European market. In many parts of the EU, although not in all, this is interpreted as winning an unfair advantage and distorting rules of competition which are fundamental for the single market.

There is **awareness also inside the Russian government that excessive reliance on the production and export of energy resources has a price tag attached** when it comes to the vitality of the Russian economic model. Although oil sales fund about half of the federal budget, this model entails much volatility.

The energy trade discrepancies in a sense correlate to energy efficiency needs. As reported to the Energy Charter Treaty secretariat by the Russian government, its economy remains greatly inefficient with energy intensity three times higher than that of the EU or Japan. There is clearly a lot of room for cooperation in energy matters, specifically within the climate change area.

Russia is trying to maximize the political and economic leverage of its energy assets. Whether the EU partners like it or not, this is **rational from the Russian point of view** to criticize the EU third energy package. The pipeline monopoly is

similar to what the British had done with British Gas and the North Sea fields. Britain gave British Gas a legal monopoly over all gas from the British sector of the North Sea. British Gas also had a monopoly over transmission, distribution and supply. The key word for Russia is control – upstream and downstream. Russia has also been fighting potential competitive transit routes to Europe.

The focus in the European Union is largely **internal** with successive liberalization attempts which have not been entirely successful because of insufficient focus on network capacity development. Interconnections and structural change are still very much needed. **There is not a single market for energy in Europe, yet**; rather there are national markets dominated by national champions, linked only bilaterally.

The external dimension of the EU energy policy is still its weakest part. A new robust, comprehensive agreement with Russia on the basis of the rejected Charter remains on the agenda. The EU continues to work on **the completion of the European networks, improving on strategic gas storage, adopting a single voice in relations with Russia**, including information sharing about contracts, supplies and supply-demand balances need to be shifted.

Rule of law

The basis for contemporary democracy is **the rule of law**. Here, as the past experiences of the European Union's member states suggest, the pathway from authoritarian or semi-democratic regimes needs a beacon of hope and a stable point of orientation. This has been long provided by the European integration project for its prospective member states during their democratisation and transformation. While not aspiring to be a nation-state, **the EU is an embodiment of the rule of law for the participating countries**. This could be of much inspiration to Russia, not as a faultless example to follow, but as the most advanced international legal experiment on cooperation and sharing sovereignty, the only of that kind around to analyse.

It would be useful for both the EU and Russia to look again at their **common basic denominator and ground their mutual relations on the principles of the rule of law**. This would serve a number of objectives. Firstly, it could help fight the virus of corruption. Secondly, it could give a hint at the effectiveness of governance institutions, a timely problem for the final stages of negotiations over the cooperation treaty. Thirdly, it could streamline Russia's participation in the WTO. Finally, it should be used to build a common regulatory framework facilitating mutual investment and diversification of economic ties. It is worth noting that no other Russian partner has this kind of experience to share with. To be sure, **no other EU partner has comparable prospects to develop on the basis of the potential of the rule of law**.

EU-Russia face-to-face

A discussion about democracy is always more difficult in circumstances in which barriers remain to human contacts and interaction. The issue of visas remains

thorny between the EU and Russia. It results from the sensitivity of the migration issue in some EU countries and the nature of the Schengen system. Schengen has been built on a common recognition of external border protection, thus leading to a general increase of the standards of external border management. The compromise for the moment includes a list of steps necessary for the waiving of the visa requirement for Russian citizens in the future. **The easing of requirements for small-border travel between the Kaliningrad area and the adjacent regions of Poland should be seen as one of the first steps** to ensure more convenient travel between Russia and the EU. The progress achieved in this area could be used as an example and an additional argument in favour of the abolition of visas for citizens of both parties. The experiences of the Russian-Polish and the Russian-Finnish cooperation should help to eliminate the existing myths and fears about the implementation of visa-free regulations.

The efforts of the parties to implement visa-free regulations should be complemented by improving the terms for obtaining visas before these regulations become real. In particular, it is urgent to make use of the provisions of the Agreement on visa facilitation and, first of all, the possibility of obtaining longer term visas. Within this context, it makes sense to set officially the provisions of the “Spanish initiative” (the right for a long-term visa automatically to those who were respectable travellers in the past). It is also important to strive for a further simplification of visa regulations for certain categories of people: teachers, students, and entrepreneurs.

Exchange programmes for students or academics are very often the subject of member states’ activity. At the same time, the EU has acquired quite an expertise in the field of supporting these endeavours. Exchange programmes like Comenius, Erasmus, Leonardo da Vinci, Grundtvig, Jean Monnet, Tempus, Erasmus Mundus, etc., have all been widely praised for their effectiveness in stimulating youth, teachers, students and academics to share their expertise and ensure mobility across the borders. **Today, the EU is on an intensive course to build a common space for science and research among the EU Member States.** Clearly, there is much to gain in that area from cooperation with the Russian scientists. Notably, there are a number of EU initiatives already open to worldwide competition in which the Russian citizens can participate fully.

These days culture matters, but **perhaps the most important aspect is the free flow of information coupled with its analysis and servicing.** People working for mass media on both sides should be facilitated in order to communicate better between each other and enhance their understanding of mutual positions. It seems ironic that in a world of abundant information and the Internet, it remains so easy to manipulate public opinion and bring a complex reality to a set of clichés. The image of Russia in the EU becomes that of a parochial state and society, while Europe is often regarded in Russia as irrelevant and irritating. **Societal links and ties cannot operate smoothly and effectively without enhanced understanding between journalists, commentators and public opinion leaders.** This transition will not be achieved overnight, but we should strive to break negative trends, if not to turn them into positive ones.

Open and honest approach to security

In the field of security, there are three sets of issues between Russia and European countries. One is about frozen conflicts and the other concerns the stability of the shared neighbourhood. While largely being a function of the processes initiated by the end of the Cold War, they have, in the meantime, acquired a dynamic of their own. The third set concerns the threat perception in the area from Lisbon to Vladivostok where there is a lot of convergence and hence potential for cooperation. There are institutional implications in all three of these areas. The debate has been dominated by the first two aspects in the last few years but momentum has been steadily growing in the third.

The key concepts are **indivisibility of security, predictability and transparency, mutual respect, and accounting for respective interests.** There is no disagreement at the semantic level when it comes to the relevance of these issues. The differences start when it comes to the steps after that. Russia has argued consistently for the principle of the indivisibility of security—in line with which no country should increase its own security at the expense of the security of others—to be codified and preferably translated into a new legally-binding commitment. The European countries have received Russian suggestions with an open mind but have not shared Moscow's preference for a new European or Euro-Atlantic security treaty.

It goes without saying that the EU is not about hard security, but the vast majority of its members are also NATO allies. Hence the difficulty, not only for the Russians, but also for the Europeans themselves, to properly understand their own security arrangements outside of the NATO framework. The biggest reason for this difficulty is its own greatest success: **in the eyes of many of its founding fathers, European integration has been perceived as a security arrangement in proper sense**, active and effective for the participants and among them. European integration has been and remains the organising device to prevent another war in Europe.

Conceived as a peace-making endeavour, the process of European integration is embodied in its most recent shape as the European Union which acts as a law-based actor in international relations. The EU's international activities should not be mixed with individual EU member states' global actions, and there are many instances of those, as the EU member states do indeed continue to have their own separate foreign and security policies. Whenever the EU acts internationally, it has to find an appropriate treaty-based ground for action, in the post-modern fold. This particularity has been rarely recognized outside of the EU, as **Europe is expected to present a unified front, as if it were a new nation-state, which it is not.**

Security area as a field of cooperation with the EU requires strategic patience, especially from countries like Russia. Nowhere can this be better seen than in opportunities and difficulties of cooperation across the common neighbourhood.

Genuinely shared neighbourhood – not a mission impossible

As seen from the perspective of our joint position on future international political and economic order, there is no question that both Russian and EU interests would be better served if we had prosperous and stable democracies as neighbours. One of the dominant factors in shaping the future of the global economy will be the accessibility of markets. As old sources of growth are increasingly depleted, vibrant economies will need to identify new economic opportunities in their regions and in the wider world. **There is an obvious dividend which both Russia and the EU can draw from a stable shared neighbourhood.** This means that there is ground for a common platform between the Partnership for Modernisation for the EU and Russia and the Eastern Partnership, which the EU has proposed to its six other Eastern neighbours. It is not a question of linking the two initiatives formally together but rather building synergies between activities which have a shared agenda.

The basic precondition for that should be the principle of non-interference in the domestic affairs of neighbours, who should be free to choose both their political future as well as international allegiances. An informal „Code of Conduct“ has to include also, as a non-negotiable principle, the respect for democracy and human rights. Referring to the specific case of Belarus, it is not in the interest of either Russia or the European Union to see the blatant refusal on the part of the Belarusian President to respect his own citizen’s freedom of expression, association and, very often, basic human dignity.

A “no” to left-overs

The means of dealing with the so- called ‘frozen conflicts’ would remain the **litmus test of EU-Russian understanding in the shared neighbourhood.** It does not serve the objective of our long-term understanding to disregard the differences which divide us on these issues. Perhaps the most challenging one is the impasse over the prospects of Abkhazia and South Ossetia.

There are reasons to believe that the relationship between Russia and Georgia is once more becoming fragile. Diplomatic relations have not been restored.

Little or no progress has been achieved on issues such as the return of displaced persons, trade or security. Since the war, agreements have only been signed on transport and energy. **Confidence-building measures are necessary to ensure that tensions do not become explosive.** Still, as the Russia’s WTO accession shows, the conflict does not necessarily have to overshadow other relations.

The return of displaced persons could be facilitated while parties exchange information on their security forces and their movements in areas near the ABLs. Mutual accusations could also be scaled down and an agreement reached to carry out joint investigations or investigations by third parties. In parallel, direct talks could take place on a range of subjects without preconditions.

The idea of setting up an EU-Russian „political and security committee“ has stalled with disagreement between the EU and Russia as to whether progress should be reached in advance on some of the intractable problems in the neighbourhood, especially unblocking the „5+2 talks“ on the settlement between Moldova and Transnistria and withdrawal of Russian forces from the region. **The idea of the committee, however, remains valid.** Both sides would be well advised to note that it is not intended to reach an ultimate solution to any of the ‘frozen conflicts’ but rather to show willingness to engage that is the only precondition for the committee’s usefulness in the context of the EU-Russian relations.

The art of talking to each other

There are fewer differences inside the EU today about the bloc’s policy toward Russia policy. The experience and point of view of the new members have become more closely integrated in the EU thinking, while Russia has gradually come to terms with the NATO and EU enlargements and the more balanced nature of the expanded European Union. **Differences of view are no longer ideological. They relate to specific interests and issues.** This should make them easier to handle and open the way for close EU-Russian engagement on global issues.

The EU and Russia have a number of common interests. However, **their relationship is hostage to a bureaucratic process which is unlikely to yield results.** The talks on the new bilateral treaty are on the back burner, with the 12th round pending to little or no avail. The EU-Russian „work programme“ for implementing the Partnership for Modernisation contains a long list of joint projects and areas of cooperation. A very similar list was adopted in 2005 under the four „common spaces“ programme. They have not been advanced very effectively. There is currently one project which is a flagship of the partnership for modernisation; it focuses on helping Russia set up appellate courts.

The approach on both sides has been more pragmatic than in the past but differences on trade and energy issues run deep and have a systemic character. Still, the trade agreement negotiations might gain more dynamics once Russia has formally joined the WTO. **The EU is interested in a free trade agreement that is of a deep and comprehensive nature, entailing also regulatory harmonisation.** If it is done wisely, **it could give a powerful boost to the Russian economy,** providing more predictable rules of the game to investors on both sides.

Still, Russia fears that just as in the previous rounds of EU-Russian dialogue, when the EU tried to impose its governance framework and democratic principles, it now uses the tool of regulatory harmonisation for the same purpose. The suspicion is magnified by the progress of EU-Ukrainian negotiations on deep and comprehensive trade, about which Russia has become increasingly sceptical. **It seems that the discussion about the regulatory relationship should consider on-going trends as well as those which are likely to take place in the global economy, in which** a race to the top is often

based on regulatory standards. A good example for consideration might be the EU competition policy, widely regarded as the cornerstone of the EU single market success and a set of standards observed by international companies wishing to be active within the EU. The EU and Russia should assess the added value which a joint regulatory relationship between them would create from the point of view of their medium to long-term prospects. This type of clarity on the interests at stake could do a lot to create a better mutual understanding between the EU and Russia.

The EU-Russian network of official contacts is highly segmented with current architecture laid in 2005, after developing “roadmaps” to achieve four common areas (economy; freedom, security and justice; external security; science and education). This ambitious goal required the establishment of dozens of structures and dialogue mechanisms, within which the work to make the relationship between Russia and the EU closer is being done. Almost every day there are meetings at expert level, on a permanent basis between ministers, parliamentarians, representatives of industry and business associations. There are regular meetings held by the Government of the Russian Federation and the European Commission to discuss a whole range of sectorial aspects of cooperation between Russia and the EU. The top of this multi-storied institutional pyramid are the biannual EU-Russia summits, which define the basic trajectory of relations for the long term. No doubt such a dialogue, unprecedentedly saturated both for Russia and the EU, contributes to trust and allows partners to openly discuss any issues.

All in all, it seems **EU-Russia relations need more, not less, institutionalization, but of the kind that would allow both sides to progress.** The new design should allow for getting to know the administrations better, much the way the flexible system of permanent partnership councils (PPCs) works between Russia and the European Commission within the four spaces system. Those arrangements would let both sides broaden their respective interfaces outside traditional ministries of foreign affairs, economy and trade, into domestic affairs, agriculture, environment, and others.

Conclusions – moving on!

The EU and Russia have a joint stake in ensuring that the future global order will be based on a strong normative foundation. It is only in such circumstances that the process of globalisation can continue to bring benefits to our economies and societies, allowing the challenges it creates can be openly addressed. In order to prepare for that, the EU and Russia should place their own relationship on a solid foundation of the rule of law and a joint regulatory framework, both of which can also play an important role in fighting corruption. Commitments on both sides should lead to creation of a legal basis for the new institutional framework.

The approach based on respect for the rule of law will surely be tested first in the context of the current international financial, economic and fiscal crisis. Both the EU and Russia have their own problems to overcome during the crisis. **Their**

consultations and cooperation could well help the emerging global governance system, also the G20. Keeping the flows of finances, trade and services across the globe stable is in everyone's vital interest and needs a continued effort to build mutual trust and understanding.

Economically, the EU and Russia will be faced, in their own ways, with new pressures resulting from the demands of sustainability of public finances and the on-going search for new sources of growth. **Ensuring that the bilateral relationship is more diversified and provides more avenues for mutual economic gain will be of growing importance in this context.** For the EU-Russian relationship to be more balanced, energy should be treated on par with other sectors of the economy, especially in terms of the regulatory approach that is applied to it.

The institutions, if they are to help to break the current deadlock, should be lean, but bold in thinking about solutions to be adopted by political leaders and ways to implement their decisions. The institutions of the new EU-Russian relationship could learn from the long-standing experience of the European Commission, legitimized by its professional authority and ability of policy outputs.

Finally, in the field of security, **the EU and Russia could approach their immediate sensitivities about regional order and stability with an open mind while more actively reaching out to address global problems,** the rank of which will continue to rise. The broad range of security questions, encompassing security of energy supplies, the situation in the neighbourhood, 'frozen conflicts' as well as missile defence will surely remain high on the common EU – Russia agenda. They call for a coordinated approach which could be based on **the common denominator of respect for the rights of all countries to democracy and the protection of human rights,** including, in particular, those in the shared neighbourhood.