



# BULLETIN

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## Old Problems and New Decisions in Lithuania's Energy Policy

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*President of Lithuania Dalia Grybauskaitė supports efforts to strengthen energy cooperation with Norway. She is counting on the development of unconventional gas production and consistently in favour of building a nuclear power plant in Visaginas. However, the actions of the new coalition, which is seeking to lower the price of gas imported from Russia, are contrary to Grybauskaitė's efforts and those of formerly Conservative cabinet. As well, the construction of the Visaginas plant seems to be less likely due to opposition and growing scepticism among the potential co-shareholder countries, Latvia and Estonia. The more Poland should strive for the timely implementation of energy interconnections that integrate the region.*

**Lithuania's Energy Issues.** A priority of the Lithuanian EU presidency, in addition to the Eastern Partnership, is energy security. President Grybauskaitė once again emphasized this during a July meeting with the foreign minister of Norway, Espen Barth Eide, and has consistently advocated measures freeing Lithuania from Russian energy sources. However, in reality, the result of ongoing negotiations with Gazprom and a final decision on the construction of the nuclear power plant in Visaginas, as well as an assessment of shale gas exploration in the country will prove to be crucial in this matter. These circumstances became more important after the government of Social Democrat Algirdas Butkevičius again delayed, this time to October, a decision on the construction of the nuclear power plant, which in 2011 was approved as a priority. Meanwhile, in April 2013, a special working group led by Energy Minister Jaroslav Neverovič presented recommendations regarding the nation's energy policy, according to which the Lithuanian nuclear project is still possible, but only with additional conditions, including changes in funding rules and in the forms of the regional partnerships to minimise the investment risk and move it forward for strategic investor Hitachi Ltd. The financing of the project would be insured by foreign investment companies and export credit agencies (ECAs).

Moreover, the result of last year's referendum on the construction of the nuclear power plant, in which the majority of voters (63%) were against it, is somehow still an unsolved problem. Although these results are not formally binding and have no legal consequences, the plant proposal has become a political issue. Until 2010, Lithuania used nuclear fuel for energy production at the Ignalina power plant, which was cut off as part of the Accession Treaty, but now it is faced with energy shortages, with the state importing more than 70% of its electricity, mainly from Scandinavian countries and Russia. Lithuania produces only 13% of the energy produced in all of the Baltic countries, and the price on the Lithuanian market increased by 30% to 54.8 EUR / MWh year on year. That is why, in real terms, the decision is largely dependent on the political will and determination of Lithuania, Latvia and Estonia.

**The Illusory Interdependence of the Baltic States.** The implementation of the nuclear project partly was supported by its regional scope, including the participation of the three Baltic States. This is especially true if the Visaginas power plant is part of the Baltic Energy Market Interconnection Plan (BEMIP), which would integrate the energy systems of Lithuania, Latvia and Estonia—which together remain an energy island next to Russia and Belarus—with the European electricity and gas infrastructure. However, because of further delays since the Baltic States signed a letter of intent in 2006, as well as the lack of clarity about the costs or financing method, the participation of Latvia and Estonia is even more uncertain. Latvia's hesitance is mainly due to the very high investment costs, but also may cite its relatively secure situation in terms of energy production, including the use of renewable energy sources, and

underground gas storage facilities. However, only Estonia has an electricity connection to Finland. It has started the construction of another one, EstLink2. In addition, Estonian energy companies have made investments in new technologies for energy production from oil shale, and Estonia is now not only self-sufficient in electricity production but also a main exporter (the Narva power plant produces 30% of the energy consumed in the Baltic States). In addition, the Baltic States varying degrees of dependence on Russian gas (Latvia pays the lowest relative price among them, while gas is less than 10% of the Estonian energy mix) and their relations with Gazprom illustrate the importance of considering the differences among the Baltic States and their real situation on the energy markets.

**Negotiations with Gazprom.** At the beginning of August, Minister Neverovič announced the completion of expert negotiations with Gazprom and is waiting for a concrete offer from the Russian company. Lithuania's main goal is to receive a lower price for Russian gas, the more so since Gazprom has been accused of violating the terms of the existing agreement, specifically the accrual rate for gas in recent years. As has been emphasized by Lithuania, the country pays the highest price for gas in Europe (20% more than Germany and up to 35% more than Latvia). The case was assigned to the Court of Arbitration in Stockholm, but according to unofficial information, it is probable that Lithuania would withdraw its application and resign from claims of damages in the amount of LTL 5 billion (€1.45 billion), if it gets favourable financial terms for purchasing gas, including a partial change in the calculation of prices based on a "basket" of oil products. Meanwhile, in response to the EU's Third Energy Package and gas market unbundling, a new company was established—Amber Grid, which was spun off from Lietuvos Dujos, in which Gazprom has a 37% share—leaving uncertainty about the conditions on which the final distribution of ownership would be based or which company in 2014 would own the gas pipelines.

In its negotiations with the Russian company, Lithuania has used as an argument that it will have access to the planned LNG terminal in Klaipėda, scheduled to be launched in late 2014 and through which it will be able to import gas mainly from Norway. Initially, the Lithuanian authorities were counting on the profitable extraction of shale gas, although assessments by experts are increasingly less optimistic, mainly due to different geological conditions than in the U.S. and because of the need to use new technology, which would increase the costs of exploration and test drilling (the American firm Chevron, which holds a 50% stake in Lithuanian LL investicijos—a company engaged in the exploration of oil—is applying for a license). Initially, it was estimated that shale gas would meet the needs of the country for 30 to 50 years. However, public debate on the issue has resulted in increased opposition by the public, supported by ecologists, to shale gas extraction.

**Russian Nuclear Projects in the Region.** In the context of regional energy security, a revision of Rosatom's plans to build a nuclear power plant in Kaliningrad seem significant. However, since a connection to the second block of TEC-2 (Thermal Power Plant) was set up in 2010, a sufficient level of generation capacity for heat and power has been provided, thus Kaliningrad is energy self-sufficient. At the same time, the construction of a nuclear power plant in Ostroveti in Belarus is proceeding, and is still strongly opposed by the Lithuanian authorities. The Committee of the Espoo Convention found shortcomings in the construction plans of the Belarusian nuclear power plant in relation to the standards and safety rules required by the Convention.

**Conclusions and Recommendations.** A possible change in the energy policy of Lithuania, especially with a departure from the nuclear project, a possible end to shale gas exploration, a simultaneously successful Gazprom compromise with a new multi-year contract for gas, or mitigated Third Energy Package, would carry consequences for energy security in the region. Activities on this issue would to a large extent be moved to the national level, requiring them to complete their own projects (though cheaper and smaller), which could speed up implementation of their respective energy policies by increasing the number of private entities participating in them. However, delays in the construction of the Lithuanian nuclear power plant, given its incalculable risk and capital intensity, means that the likelihood of the project is steadily decreasing, especially in view of the growing scepticism among the public in those countries.

Poland, which is considering its own basic energy projects in light of possible energy shortages after 2016, should support the timely development of electricity interconnectors. It is important that a wider range of EU institutions be involved in the monitoring of regional projects and those in its neighbourhood, including a focus on them in the Committee on Industry, Research and Energy. It is in Poland's interest to support the priority on energy security during the Lithuanian presidency, particularly the creation of a single EU energy market (which for technical reasons has already been delayed), primarily at the level of market integration and expansion of electricity connections.