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What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

by Sami Andoura

ABSTRACT

The EU and Turkey are engaged in a long-standing process of negotiation over membership, facing many stumbling blocks and no prospects of successful conclusion in the near future. At the same time, the EU and Turkey have increasingly high energy ambitions, which open the door for potential cooperation in a number of energy areas. The main areas of such cooperation are the diversification of gas supply and transit through the Southern Corridor, and the convergence of regulatory frameworks and markets. While Turkey and the EU have so far have not been able to harness a strong relationship in these fields, their energy cooperation covers a wide range of increasingly complex and sensitive issues which go beyond the gas sector.

Turkey | European Union | Energy | Energy security | Energy supply | Pipelines | Natural gas



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Introduction

The EU and Turkey are engaged in a long-standing process of negotiating their future relationship and their potential integration through the enlargement process. This process is facing huge shortcomings and stumbling blocks, with no prospects of radical change in the near future. At the same time, the EU and Turkey have increasingly high energy ambitions, though not always for the same purposes. These ambitions correspond on a growing number of issues and therefore open the door for potential cooperation in a certain number of energy areas. The main area of potential cooperation addressed in the present analysis is diversification of gas supply and transit mainly through the so-called Southern Corridor, and the convergence of their regulatory frameworks and markets leading to their potential progressive integration. However, Turkey and the EU are facing important challenges in these two fields, and so far have not been able to harness a strong relationship in these fields. However, their energy cooperation covers a wide range of increasingly complex and sensitive issues which are going beyond the gas sector.

In this context, the aim of this contribution is to give a comprehensive overview of Turkey and EU energy profiles (Part I), in order to better identify the potential areas of convergence and cooperation but also the limits of such an approach in the field of gas (Part 2). It then addresses the various frameworks and instruments for cooperation available to EU and Turkey, and makes some recommendations on how they could be used in a more efficient and pragmatic way (Part 3). Finally, it concludes that the main risk facing EU-Turkey energy cooperation is muddling through. Suppliers and market operators might not wait for such rapprochement, and could instead make a decision at the expense of both the EU and Turkey.

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1. Converging energy profiles but at different speed

Economic growth and energy consumption. The EU economy is stagnating, with no real prospects of change in the (near) future. In its context of economic crisis as well as of energy transition, EU energy demand is decreasing. In contrast, even in the context of the economic crisis, Turkey's economy grew annually over the last couple of years. As one of the fastest growing economies in the world, its projected average growth is between 3 and 5 percent in the years to come. As a result, Turkey saw an increase of almost 90 percent of electricity demand between 2001 and 2010.¹ Consumption will also expand at a fast pace (4.5 percent per annum till 2030) in order to satisfy both its economic expansion and the increasing living standards of its population.

Energy policies and markets. The EU and Turkey are engaging in their respective energy transition. However, energy transition is a "concept valise" with different priorities for every country (EU member states and Turkey) or region (EU). Both energy policies are structured around the same three key objectives of competitiveness, security of supply and sustainable development, but with different priorities in respect to time (the hierarchy in the priorities is changing much faster in the EU, and not always in very rational way), and with different ambitions. Both actors are in the process of liberalization, engaging with deep market reforms mainly related to the role of national regulator, competition authority, unbundling of utilities, access to the grid, transparency, etc. Turkey has started the restructuring of its electricity and gas sectors in 2001, with the Electricity and Natural Gas Market Laws and the establishment of the Energy Market Regulatory Authority.

However, these processes of market restructuring are taking place at different paces and with different modalities. The EU is at the stage of (trying to) finalizing the liberalisation and integration of its electricity and gas markets. As regards the market players, there is a mix of publicly owned and private companies for electricity production, transportation, distribution, as well as for natural resources exploration and exploitation in both the EU and Turkey. The role of international companies (EU and non-EU) is key to both actors and markets. But again, there is not the same degree of market openness, as a consequence of which foreign involvement in exploration and production activity in Turkey have to be subject to forming a joint-venture with TPAO, the Turkish national oil company. The community of private market players and international companies also have a key role to play in their diversification strategy, including the Southern Corridor: EU companies are directly involved in the region, including in Turkey, in exploration of natural resources, production, transit, distribution, and technologies. Foreign companies from the regions (i.e. SOCAR) are increasingly active in EU markets.

¹ Energy Information Administration (EIA), *Turkey Energy Profile*, <http://www.eia.gov/beta/international/country.cfm?iso=TUR>.

The role of natural gas. Conventional thermal power (mainly gas and coal) is a key power generation source in both Turkey and the EU. In 2011, the EU generated about 726 TWh (or 22 percent) of electricity from natural gas.² Gas use increased compared to 2000 from 17 to 22 percent. Fossil fuels are Turkey's main energy sources as well (43 percent for gas). However, indigenous energy production is almost negligible and Turkey's reserves are fast depleting. Natural gas, used mainly in power generation and heating systems, is playing an increasing role in Turkey's energy profile. It is one of the fastest growing gas markets in the world (127 percent increase of natural gas supplies between 2000 and 2009). The Oxford Energy Institute estimates that this trend will continue with the projected rise in gas demand from 45 bcm in 2012 to 70 bcm in 2030.³ By 2023, the Turkish government aims to reduce 12 billion dollars' worth of natural gas replacing this with domestic resources, and to increase gas storage capacity to 5 bcm.

Import dependency. Both the EU and Turkey are highly dependent on energy imports for their internal needs, a trend which will only amplify in the near future. In 2011, the EU's import dependency stood at 54 percent with gas import dependency being particularly elevated standing at 67 percent.⁴ Russia is the EU's main import partner, providing 36 percent of its gas, and Norway is the second (34 percent). Overall, the EU remains to a large extent dependent on external fossil fuels suppliers and will continue to be so because of decreasing indigenous resources. Turkey has to import almost all its gas (98 percent). Its gas comes mainly from Russia (56 percent) followed by Iran (18 percent), Azerbaijan (8 percent), Algeria, and Nigeria. Turkey also imports Liquefied Natural Gas (LNG was 15 percent of the total gas supply in 2011, 17 percent in 2012 according to EIA⁵) from five countries: Algeria, Nigeria, Qatar, Egypt and Norway. Most of Turkish gas supply relies on long-term contracts. Moreover, one of Turkey's principal energy "weaknesses" is its lack of adequate storage capacity (around 3 bcm), which is a security weakness in case of shortage, but also an economic weakness due to onerous take-or-pay clauses it is facing.

The EU is increasingly concerned by the too high level of dependency of some of its member states on one supplier, particularly Russia. In contrast, Turkey has fewer concerns than the EU over Russia, as illustrated recently with the deal on the "Turkish stream," which is seen as an alternative to the cancelled South Stream pipeline in the Southern Gas Corridor.⁶ Turkey has nevertheless decided not to have

² European Commission, *Trends and Developments in European Energy Markets 2014* (SWD(2014)310), 13 October 2014, p. 10, <http://eur-lex.europa.eu/legal-content/en/TXT/?uri=celex:52014SC0310>.

³ Gulmira Rzayeva, "Natural Gas in the Turkish Domestic Energy Market: Policies and Challenges", in *OIES Papers*, No. NG 82 (February 2014), p. 1, <http://www.oxfordenergy.org/?p=4160>.

⁴ European Commission, *On the exploration and production of hydrocarbons (such as shale gas) using high volume hydraulic fracturing in the EU* (COM(2014)23), 22 January 2014, <http://eur-lex.europa.eu/legal-content/en/TXT/?uri=celex:52014DC0023>.

⁵ Energy Information Administration (EIA), *Turkey Energy Profile*, cit.

⁶ For more information on Turkish stream, see <http://www.gazpromexport.ru/en/projects/6>.

more than 50 percent of its imports from one source. This is one of the reasons why it has recently concluded several deals with countries like Algeria, Azerbaijan, and Iran over additional gas supply. Furthermore, both have fears about the impact their increasing dependency currently has – and will continue to have – on their foreign policy, as well as on the relations they are developing with energy foreign suppliers in order to guarantee their security of supply in the (near) future.

2. Potential cooperation for diversification of supply: same appetite for diversification but for different purposes

2.1 EU's perspective: security of external supply and transit routes

EU diversification of sources' strategy has been launched with the "new energy policy for Europe" adopted in 2007⁷ in the context of growing tensions between the EU, Ukraine and Russia over gas transit and supply disruptions in 2006 (and again in 2009) which directly affected EU countries. By ensuring greater diversification of supply sources – mainly of natural gas –, and transport routes at European level, the European strategy is seeking to limit the EU's exposure to its imports, and particularly for member states that depend on a single supplier. To this end, the EU has committed to speaking more often "with a single voice" on the international energy stage and more coherently by reinforcing energy partnerships and dialogues with the main transit and supplier countries. The Southern Energy Corridor (with Nabucco being the flagship project), has officially been (on paper) the key external component of this new EU's diversification strategy.

Nevertheless, the EU is still seeking to define a coherent and collective diversification strategy for supplies and international partnerships. Most EU member states are now engaged in unprecedented diversification strategies of energy sources and resources, which have at times undermined the principle of energy solidarity within the EU. Various competing and controversial projects for oil and gas pipelines to diversify the supply routes have emerged as a result. Examples include Nord Stream, Nabucco and South Stream.

In practice, the lion's share of EU diversification for gas has come through market developments rather than the above "policy" developments. It is mainly the increase of LNG supplies (and infrastructures) that have brought real diversification through additional volumes and new suppliers and transit regions/countries to the EU. However, success of diversification of gas supplies using LNG has more recently been mixed because of stagnating (and even decreasing) LNG volumes marketed in Europe from 24 percent in 2011 to 18 percent in 2012.⁸

⁷ European Commission, *An energy policy for Europe* (COM(2007)1), 10 January 2007, <http://eur-lex.europa.eu/legal-content/en/TXT/?uri=celex:52007DC0001>.

⁸ International Energy Agency (IEA), *World Energy Outlook 2014*, November 2014, <http://www.>

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

In the current context of low EU natural gas demand, the competitiveness of its economy (related *inter alia* to energy demand and energy intensive industry) is not the priority factor driving its strategy of diversification. It is indeed in the name of its security of supply rather than its competitiveness that the EU has developed such a strategy. If new/additional gas is to come to the EU (including from/through Turkey), it is mainly in order to diversify from its traditional supplier and transit countries in the context of growing tensions (even conflict) between the EU and Russia over Ukraine rather than to cope with additional gas demand.

Most recently, the feeling of insecurity in the EU over gas supply and transit has again seriously increased, mainly due to the current state of crisis between the EU and Russia over Ukraine. The EU is facing historically high tensions with Russia following the eruption of the Ukrainian crisis, from the annexation of Crimea to today's escalating state of war, which lead to the EU's adoption of several rounds (not finished) of sanctions on Russia. High level of tensions have further increased with the cancellation of the projected South Stream pipeline by Russia, and the antitrust case launched in May 2015 by the European Commission *vis-à-vis* Gazprom. The EU and its member states, once again shaken up by the course of (external) events, have adopted at the European Council in June 2014 a new EU energy security strategy proposed by the European Commission, which clearly aims to diversify energy gas imports from Russia.⁹ The Southern Energy Corridor is thus again under the spotlight, and in particular the future energy relationship between the EU and Russia, as well between Russia and Turkey through the ambitious Turkish Stream pipeline bringing Russian gas supply to the EU (Greece) and transiting only through Turkey.

2.2 Turkey's perspective: economic competitiveness and gas demand

Turkey is strategically located at a crossroads between gas rich regions (proximity to around 70 percent of the world's proven gas reserves – i.e. Russia, Caspian region, and the Middle East) and consumer energy markets. As such, it has the potential to play the role of an energy bridge between the supplier countries and consumer markets (the EU mainly), and to enjoy the huge benefits that this role implies. In its comprehensive strategy of diversification of gas supplies and transit routes, Turkey is engaging in several projects in order to expand additional capacity of gas – mainly from Iraq, Iran and Turkmenistan, but also potentially from Russia – for both internal consumption and export/transit to the EU markets. At the same time, this energy strategy of diversification, which renders Turkey a central player amongst energy suppliers in a vast zone at the intersection of key regions – including the EU, the Middle East, the Caucasus, Central Asia, Russia, and even the Gulf – mirrors Turkey's foreign policy ambitions to be a central political

worldenergyoutlook.org/publications/weo-2014.

⁹ European Commission, *European Energy Security Strategy* (COM(2014)330), 28 May 2014, <http://eur-lex.europa.eu/legal-content/en/TXT/?uri=celex:52014DC0330>.

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

actor in the same zone. Turkey is willing to become a key transportation source for hydrocarbons to Europe, and is portraying itself as both a future transit country and energy hub. While these two goals have common features, they are different in essence (and in view of all conditions to be met in order to become one and/or another).

A transit country is a country connecting supplier and consumer regions/countries/markets through (a network of) pipeline or other (LNG, tankers, etc.) infrastructures. It can act as a mediator/honest broker between supplier and consumer countries/operators or be a source of tension between the two. It is a lucrative activity for the transit country in terms of transit fees, and also in light of the possibility to get gas from the transit itself (lift off) through contractual arrangement in a transparent way. The availability of alternative routes for transit, or the lack thereof, gives more or less central role and leverage to the transit country *vis-à-vis* the supplier and consumer countries. A safe, reliable and uninterrupted flow of energy from the supplier zone to the consumer one is the key role/obligation of the transit country. Such a transit "system" requires the necessary infrastructure to be in place, political stability, transparency of the decision making process, and the adequate regulatory framework to attract investments for building the necessary infrastructures and to operate them in an open/non-discriminatory and efficient way. Last but not least, getting sufficient supply of gas is another obvious key precondition.

An energy hub is a market location where (important) amounts of resources (natural gas in this case) are going to through a network of available (gas) infrastructures – i.e. pipelines, storages, LNGs, etc. These multiple energy carriers meet at the hub, which plays a role of interface where the energy can be sold, and/or converted, conditioned, and stored. It is a point of access to several markets, connecting intrastate and interstate (gas) infrastructures. Beyond this role of exchange, the energy hub can also play a role of a pricing point for natural gas, sold on the so-called "spot markets". In this case, the hub can also play a role in setting prices for natural gas that can be used to a certain extent as benchmarks for other natural gas markets and/or contracts/arrangements. The condition for an energy hub to be in place are mostly the same as for a transit country, but reinforced in many ways (sufficient infrastructures and gas available, the adequate regulatory framework and liberalized market allowing free competition in a transparent way, etc.).

Turkey is already a reliable transit country for oil. It plays an important role in international transit (the Bosphorus is one of the busiest chokepoints worldwide), and is deriving significant revenues/fees for its transit role. In so far as the gas sector is concerned, Turkey's network (9 entry points: 4 through international pipelines, 2 LNG terminals, 2 domestic production areas and a storage facility) is in the process of being expanded.

However, Turkey's strategy of diversification is above all aimed at attracting more gas in order to satisfy its domestic energy consumption/demand and to guarantee its competitiveness. Gas is increasingly expanding in Turkey's energy mix: from 2000 to 2012 alone, gas demand rose from 14.8 bcm to 45.2 bcm and is set to reach

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

59.6 bcm by 2018 according to IEA estimates.¹⁰ As a consequence, past and current excess capacity of its main pipelines – Russia-Turkey West Gas pipeline (16 bcm capacity), Russia-Turkey Blue Stream pipeline (14 bcm), Iran-Turkey pipeline (10 bcm), Baku-Tbilisi-Erzurum pipeline (6,6 bcm) – are decreasing. Turkey's gas demand is also highly seasonal, with high peaks during winter. Turkey also has little storage capacity. It will therefore undoubtedly need to import more gas for satisfying its demand. However, estimations regarding its internal consumption differ, with some arguing that it is over-estimated.¹¹ Furthermore, the fees it is receiving as a transit country are important economic revenues. Another advantage it derives from its role as transit country is its increased attractiveness for foreign suppliers and international companies to supply gas through Turkey, but also to Turkey – as its role as transit state strengthens its aims to get additional supply as a consumer country –, and making the necessary investments (and joint ventures) in the Turkish energy sector. Finally, as an energy hub, Turkey would have the benefits of a transit country (fees), coupled with further room for maneuver in terms of internal consumption, and price setting. Gas sold on spot markets might in the long term lower the price of gas. Additional gas flows and liquidity of Turkish gas market can also mean more room of maneuver for Turkey to get lower prices for its imported gas – and renegotiate with Russia and others over long-term contracts.

2.3 State of play of EU-Turkey energy relations in the Southern Energy Corridor

In the case of EU-Turkey relations, Turkey is an almost unavoidable transit country for importing resources from the Caspian and Middle East regions, through the Southern Corridor as a central piece of its strategy of diversification. "Cooperation" with the EU has already started in the Southern Corridor, but with mixed success so far.

The EU has taken a high profile stance when it exerted its full weight behind developing the so-called Southern Corridor (the Nabucco pipeline initially) that it conceived of as a genuine European interest. However the project has encountered a number of obstacles since its inception: delays, rising costs, supply that is not yet secure, fierce competition from other European projects, including those promoted by the Russians (i.e. South Stream). Nabucco will never come on line in the form initially promoted by European institutions. It was first scaled as Nabucco West (supported by private operators Austrian OMV, Hungarian MOL, Romanian Transgaz, Turkish BOTAS and Bulgarian Bulgargaz) supposed to transport gas from the Caspian to the EU from Turkish border, as an extension of the Trans Anatolian Pipeline (TANAP) and then through Bulgaria and Romania to Austria and gas hub Baumgarten. Nabucco West was finally eliminated from the competition by Azeri suppliers and other developers of the consortium for the Shah Deniz II gas field

¹⁰ International Energy Agency (IEA), *World Energy Outlook 2014*, cit.

¹¹ Gulmira Rzayeva, "Natural Gas in the Turkish Domestic Energy Market", cit.

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

(supported by the companies BP, Statoil, Total and SOCAR) for the benefit of its direct competitor, the Trans Adriatic Pipeline (TAP, supported by Statoil and E.ON Ruhrgas AXPO) – which will deliver gas up to 10 bcm per year, from the Turkish border to the EU (by extending the TANAP) through Greece and Albania to Italy.

A number of lessons can be learned from the Nabucco experience. Above all, it is difficult to develop a gas transit system without sufficient insurance about the volumes of gas available for such a pipeline. Concretely, this project was not sufficiently based on the existence of adequate quantities of available gas. Gas resources from Azerbaijan were quickly proven inadequate and it was never clear how much Turkmenistan or other suppliers would engage in this European project of diversification. This explains why today's EU strategy on the (potential) Trans-Caspian pipeline is first and foremost targeting the supply from Turkmenistan, and then only if there are real prospects of getting gas from it (and potentially from Iran and Iraq at a later stage). Both the proposed building of a Trans-Caspian pipeline, and the expansion of TANAP transport capacities (even building a second line) will be considered.

Moreover, it is more difficult to develop a project of this magnitude when companies and private operators involved are small or medium sized, and not among the largest in Europe, especially as it turned out after the withdrawal from Nabucco of German operator RWE. Other factors have also played a role, such as the Russian lobby *vis-à-vis* the countries of Central Asia but also the price differences between gas markets targeted by TAP and those covered by Nabucco West, and the (in) direct interest of Azeri (SOCAR) in the Greek energy infrastructure. The difficulties encountered in developing the Southern Corridor have to a certain extent played down the interest of energy utilities and gas suppliers, except for Azerbaijan so far, to invest and commit in the Southern Corridor endeavour.

Last but not least, Turkey's role in the recent developments (TANAP and TAP) has not always been totally clear. Some observers are wondering whether Turkey ultimately played in its own interest only or if it has also taken into consideration EU's interest in its strategy *vis-à-vis* Azerbaijan. Some also question Turkey's demand and ambitions regarding the transit of gas directed to the EU (both in terms of transit fee and gas supply available to Turkey). The fact that all the projects are out of the hands of the EU is worrying, as it is particularly the case for TANAP, owned by SOCAR and BOTAS. There is an interesting parallel with Naftogaz and Gazprom in Ukraine, and a powerless EU regarding transit issues.

All these questions will need to be clarified in the future. From now on, if the EU and Turkey want to further develop and expand the Southern corridor concept, there are many key challenges and obstacles ahead that will need to be addressed. In this context, it is worth identifying whether Turkey and the EU could cooperate on each of the main challenges ahead.

2.4 Future challenges in the Southern gas corridors as vectors of cooperation

Finding enough suppliers. It is key to find potential sources of gas to fill the Southern Corridor. In an “ideal world”, it is in the interest of all parties that the gas would come from politically reliable countries with enough gas and at competitive prices. However, the Southern Corridor is operating in a fragile and complex geopolitical context. The Middle East holds great potential, but some of its key players are in state of civil war (Syria, Iraq) while there are tensions over energy supplies among them. In the Eastern Mediterranean region, which also holds great potential, both the EU and Turkey are involved as well. But EU has a low profile so far and Turkey is both part of the solution and part of the problem/obstacle for the development of those resources. Turkey has adopted a rather conflicting approaches so far regarding Cyprus, Israel, Greece, and so on. Iran has also a key potential but its relations with the EU (and to a much less extent with Turkey) have been complicated. The EU is much more concerned by political and military developments in Iran, especially related to its nuclear development plan, and has adopted several rounds of sanctions and embargos, including on the latter’s energy sector. The Caspian Region, at the heart of both countries’ strategies of diversification also has a huge potential. Turkey is closer (and more involved) than the EU in energy relations with its neighbours from the Caspian – above all Azerbaijan, followed by Turkmenistan. But tensions between countries around the Caspian over energy resources are a source of uncertainty. Political relations between Turkey, the EU and the countries from the Caucasus remain fragile.

Securing the transit. Military conflicts and terrorist threats are high in several key places where the supply originates or could originate and/or passes through in order to reach EU markets through Turkey. This threatens the uninterrupted flows of gas and makes the area less “appealing” for potential investors who build the required infrastructures to expand the network. Turkey borders unstable countries, such as Iraq and Iran, and has already experienced terrorist attacks on its pipelines, which caused supply disruptions. Turkey has therefore a key role to play in securing the region, in conformity with the great role it (want to) plays in the region in terms of foreign and security policy, as Turkey is also a member of NATO.

Designing the adequate regulatory framework. The insufficient regulatory framework for gas transit regulation in Turkey (no market approach such as TPA, transparency, tariffs, nondiscrimination, etc.), which does not meet EU standards (third package and others), is worrying. In this respect, one should note that while Turkey is already a transit country, it is far from being an energy hub that it aspires to be. Many issues remain to be addressed (where to do it, when, how, infra, storage, etc.). Market conditions are not ready either (they need new regulation, new infra, new investments, new market players, etc.). The EU and Turkey therefore have real potential for cooperation in the field regulation and market conditions.

Struggling with other actors. The EU and Turkey might have to increasingly struggle with other suppliers and consumers over access to natural resources – and also between energy sources themselves (i.e. gas vs. coal, etc.) – in a context of increasing global competition. The impact of emerging global gas markets on the development of the Southern Corridor might rise in the mid to long term: rising LNG markets, shale gas revolution in North America, etc. There is a risk for Turkey of losing its importance for the EU as an energy bridge with respect to these developments in the global energy markets. The EU and Turkey might also have to face growing competition from external actors in the region, mainly Russia.

Confidence building between the EU and Turkey. A common strategy between the EU and Turkey to share and spread risk, and to make the best use of their combined weight in global and regional affairs will always be more effective than dispersed or even conflicting actions. As a large trading bloc, the EU and Turkey would have a lot to offer to energy suppliers. However, EU-Turkey political relations remain a key obstacle to such an endeavour. Foreign policy issues might also negatively impact the entire project. Moreover, it is not clear whether the “hub” concept is a real vector for cooperation or competition between the EU and Turkey. If Turkey is able to attract additional supply of gas in the future either as a transit country or an energy hub, it might want to consume most of the resources coming on stream. Playing the EU markets as end consumers for the resources it wants to attract is reinforcing its hand and attractiveness *vis-à-vis* the supplier countries and international investors.

3. Potential frameworks for cooperation

Beyond the various parameters that are not directly in the hands of the EU and Turkey (supply side), the main question is how to frame their bilateral cooperation over the diversification and the integration of their electricity systems with the adequate tools of governance and the right mix of policies and instruments. The EU and Turkey, if they are willing to do so, can already cooperate on their energy projects through a wide range of other EU policies which are either dealing with the issue of energy diversification *per se*, with the region where this diversification should occur. There are also several competent EU institutions and instruments involved.

3.1 Enlargement policy: a difficult process

The main vector for EU-Turkey relationship so far has been the enlargement process, but this process has achieved little to date, and encountered significant obstacles. The bilateral relations between the EU and Turkey are at a very low level at the moment – and has been so for some time now. It also seems that there might be very little new sign of trust and progress in the near future. The main stumbling block to the rapprochement between the EU and Turkey is the unresolved status of Cyprus. But there are also other obstacles within the EU block: Turkish accession

is without common measure in EU history, it would massively impact the EU, and the way it is operating, both internally and externally.

Support from EU actors to Turkish accession is diminishing. Bilateral relations between Turkey and EU member states are very fragile with a growing majority of countries opposed to Turkish accession. The European Parliament is divided over Turkey. Public opinions in the EU are increasingly against it. All in all, the enlargement fatigue, and Turkey as a *sui generis* issue/model, pose a challenge for EU enlargement. Other recent EU factors pose additional obstacles to Turkish accession: the results of the last EU elections saw a breakthrough for extreme right parties. With no clear portfolios in new EU Commission on enlargement policy, the EU might be tempted to look inward and thus not prioritize the accession process with Turkey.

There are four main conditions to be met by the EU and Turkey in order to bring their relationship to a higher level, and thereby to ease the accession negotiations:

1. Both actors need to make new (and much bigger) concessions;
2. Turkey must adopt a less confrontational standing *vis-à-vis* EU countries and therefore the EU as a whole;
3. The EU must respect its commitment over negotiations of Turkish accession, pursuing them to their end, and then only make a choice whether Turkey can or cannot integrate into the EU block;
4. To be ready on both sides to make progress on a wide range of pending issues, including the energy file, without linking all issues to the enlargement process.

Finally, they have to find their proper *modus vivendi* and *operandi*, based on a balanced equilibrium between cooperation/trust and competition. They will never agree on all terms, and remain to a certain extent competitors on certain issues, including in the energy field. It should come as no surprise that even within the EU, member states are to a very large extent co-operators but also competitors. This is particularly the case in the field of energy and the diversification of supply – Nabucco vs. South Stream, bilateral relations with Russia, nuclear vs. RES, gas vs. coal, interconnections, etc.

3.2 The role and status of energy in the enlargement process

As an EU candidate country, Turkey makes concerted efforts to align its energy policy with the EU *acquis communautaire*. However, according to the 2012 Commission Staff Working document on Turkey's progress regarding the enlargement procedure, Turkey is at a moderately advanced stage of alignment.¹² Progress

¹² European Commission, *Turkey 2012 Progress Report* (SWD(2012)336), 10 October 2012, <http://eur-lex.europa.eu/legal-content/en/TXT/?uri=celex:52012SC0336>. For 2013 and 2014 2013 Progress Report conclusions on Chapter 15 (Energy) see Sohbet Karbuz, "EU-Turkey Energy Cooperation: Challenges and Opportunities", in *IAI Working Papers*, No. 14|12 (November 2014), p. 8, <http://www.iai.it/en/node/2362>.

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

has been recorded within the realm of renewable energy and energy efficiency. According to the Commission's document, some progress can be recorded in terms of security of supply with reference to the intergovernmental agreement and the Memorandum of Understanding between Turkey and Azerbaijan, in 2011, on the sale and transit of Azeri natural gas to EU through Turkey (TANAP).

At this stage, the EU is tempted to concentrate on practical and pragmatic cooperation through the "positive agenda" with Turkey, with energy as part of it. In the context of the "positive agenda" – launched by Commissioner for Enlargement and European Neighbourhood Policy Štefan Füle and the Turkish Minister for European Affairs and Chief EU negotiator Egemen Bağış in Ankara in 2012,¹³ with a view to bringing fresh dynamics and a new momentum into the EU-Turkish relations – energy issues have also been part of the overall agenda.¹⁴ It is mainly about the following key topics: (i) long-term perspectives on energy scenarios and mix; (ii) market integration and development of infrastructures of common interest; (iii) global and regional cooperation; (iv) promotion of renewable, efficiency and clean technologies; (v) nuclear safety and radiation protection. More precisely, a working group has been established and is tasked the preparation of a roadmap which will contribute positively to the cooperation enhancement of EU-Turkey energy relations. So far, the "positive agenda" is a dead end. Turkey is only willing to use it to a full extent on energy issues, privileging the enlargement process and the opening of the energy chapter. The EU itself is also not really devoting the adequate (political, economic and administrative) resources necessary to make it happen.

It seems clear that closer ties with Europe in the field of energy – and European interest over diversification of its Southern Corridor and its need of Turkey to achieve it – will not pave the way for reopening negotiations on a new spirit leading to full membership for Turkey. Obstacles, above all the political ones, are too high. One can draw a parallel with Cyprus settlement issue, and the energy part of this equation. It is not clear at all whether the discovery of natural gas resources offshore the island is about facilitating a rapprochement between the two sides of the island, or whether it could even complicate an already fragile relationship. New discoveries of gas will not be a game changer for the resolution of the conflict as long as a compromise has not been found on the overall political status of the island. In both cases, solutions will come only when all parties have accepted that the main answer is political in essence, and are ready for a comprehensive deal.

¹³ European Commission, *Positive EU-Turkey agenda launched in Ankara*, 17 May 2012, <http://europa.eu/!kF67WC>.

¹⁴ European Commission, *Turkey-EU Positive agenda, Enhanced EU-Turkey Energy Cooperation*, Outcome of the meeting of Commissioners Oettinger and Füle and Ministers Yildiz and Bağış, Stuttgart, 14 June 2012, http://ec.europa.eu/energy/international/bilateral_cooperation/doc/turkey/20120622_outline_of_enhanced_cooperation.pdf.

3.3 Turkey's place and priority in European energy policy (external dimension)

Energy affairs at EU level are almost exclusively addressed at the level of European energy policy, and therefore the Directorate General for Energy within the European Commission, which is in the driving seat. Other dimensions are much more accessory, such as foreign policy, trade, development, neighbourhood, enlargement, etc. This means that all important decisions and issues to be addressed in the field of energy – both internally and externally to the EU – are to be dealt with the DG Energy portfolio, and the relevant EU Commissioner for energy – and not, for instance, the DG for enlargement, or even the European External Action Service (EEAS) and the High Representative for Foreign and Security Policy. This state of affairs, specific to the EU, has to be clearly understood by external actors, including Turkey, when addressing issues or developing projects with the EU in the energy field. If Turkey wants to make progress on the energy front with the EU (especially in the short term), it is therefore in the framework of its European energy policy that it must engage with, and not only through the framework of enlargement. Projects such as diversification of supply (including the Southern Corridor) or integration of energy markets (including in the EU neighbourhood) are driven by the EU energy policy.

At the same time, the question is then whether the EU is able to deliver on these issues. EU energy policy is still half way between integration (a common EU energy policy) and full sovereignty of member states over their energy mix and supply structure. The external dimension, including access to supply (and transit routes), is one of the key battlefields in terms of competence between the member states and the EU. It has been years now that the EU is trying to develop its external dimension of energy policy, without huge breakthrough so far. Things are however moving in the right direction, as highlighted again recently at the March and June 2014 European Council, together with the new EU strategy for energy security.¹⁵ The EU is also getting more assertive *vis-à-vis* external actors, including Russia (South Stream re-negotiation, sanctions, etc.) and its operator Gazprom (antitrust case, compliance with EU regulations/3rd package, etc.). It is more and more in the interest of external actors to better understand this evolution, and to “play” the EU card rather than the divide and rule one with individual member states.

As concerns EU-Turkey relations, one can regret two shortcomings from the EU. First, when dealing with Turkey over energy issues, the EU is still far from bringing the necessary coherence and consistency between its various policy frameworks (energy, enlargement, ENP, trade, foreign policy, etc.) and the related instruments (PCI, financial support, infrastructures, EU institutions – Commission, EEAS, EU missions, etc.). Second, Turkey is clearly not the priority of EU energy policy, and this is reflected in EU institutional capacity devoted to EU-Turkey energy relations (and the role of Turkey in the region). However, there are some key factors that

¹⁵ European Commission, *European Energy Security Strategy*, cit.

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

could indirectly increase the EU interest in and involvement over Turkey in the field of energy:

- the new concept of “Energy Union” as a key priority for the new EU institutions;
- the ambition that the external dimension of such a policy should be better addressed (including speaking with one voice, EU bargaining power, etc.);
- the ambitioned further coherence between various policies and instruments within the European Commission (new Commissioner for better regulation, European Parliament scrutiny, etc.);
- and potentially a more strategic EU role and action on the global and regional stage.

Beyond European energy policy’s “borders”, the EU and Turkey could therefore undertake other important steps to make progress in the energy area by making a greater use of their external action policies and instruments. It is in their interest to pursue the systematic inclusion, where necessary and justified, of energy objectives in their external policies and instruments and other financial and economic means to attain them. While energy is already a key component of Turkish foreign policy, the EU itself is far less advanced. This approach would require giving the European Commission clear, coherent and ambitious negotiating mandates. Moreover, the EEAS would have a special role in coordinating the different instruments and the multiple geographic areas concerned, as well as in the overall contact with foreign countries (including supplier and transit ones). The two main areas where EU and Turkey could further cooperate in supporting their common interest are their neighbourhood policies and their trade instruments.

3.4 Common EU-Turkey trade strategies

Having a common strategy of diversification of energy sources *vis-à-vis* external partners, whether producer or transit countries, and pursuing their common interests with regard to these states and other trade entities could also mean, when necessary, that the EU and Turkey could negotiate directly with suppliers and transit countries the conditions of energy supply, while leaving companies to negotiate and conclude the final contracts over volumes and prices with suppliers. Moreover, EU (members states) and Turkey are in some cases not able to consume alone the large quantities of gas that the supplier countries are ready to sell on their markets (30 bcm from Turkmenistan for instance).

Beyond the current case-by-case *ad hoc* approach, the EU and Turkey could negotiate trilateral framework agreements with these countries to establish the rules of the game for energy relations, on an equal footing and in line with the principles of free competition, inter-dependence, and reciprocity. Such a (highly ambitious) step would be consistent with their respective objectives and agenda for energy security. The negotiations of such energy frameworks agreements could for instance have the objectives of: (i) negotiating framework supply agreements; (ii) establishing the right legal and economic framework for investment consortiums with supplier and transit countries and companies; (iii) using transport and storage

infrastructures (EU, Turkey and others), but also potentially to prevent supply disruptions and to improve energy crisis management (common definitions and joint emergency mechanisms), etc. Establishing a stable legal framework with partner countries would also promote trade relations among industry players involved on all sides. Transparent and reliable framework conditions are likewise essential for operators/utilities to take advantage of new investment possibilities. This would eventually open up their respective energy markets to the foreign companies concerned, according to the rules and parameters negotiated in the framework agreements (in compliance with common regulations established at EU-Turkey level).

However, in general, such an approach does not appear within the realm of the realizable. On the EU side, this consideration is still too often absent in bi- or multilateral agreements signed with supplier and/or transit countries. The mandate of the European Commission to negotiate a framework agreement with supplier and transit countries in Central Asia (Azerbaijan and Turkmenistan) is a first step in this direction. However, it has taken nearly a decade since the launch of the Nabucco project for the EU Council to finally give the European Commission a clear mandate to negotiate. As we have seen, the problem is that the markets, operators, and producer and transit countries are moving faster, and not necessarily in the direction set by the EU. As far as Turkey is concerned, it prefers to negotiate directly on bilateral basis with supplier and transit countries, without the involvement of the EU.

3.5 Strategic partners in their common neighbourhood

Energy cooperation within the "European" neighbouring area, including Turkey and Central Asia countries, is part of a far-reaching project to create a pan-European area of security and prosperity, be it in the name of overall political, economic and social cooperation within the EU neighbourhood, or for energy security and diversification of supply purposes. However, this strategy cannot be limited on the EU side to transferring the Community energy *acquis* to neighbouring countries. Whether it is in the framework of the European Neighbourhood Policy, the Eastern Partnership or the Union for the Mediterranean (UfM), the EU and its neighbours must gradually open up their respective energy markets on a reciprocal basis, and develop concrete co-development projects in the energy sector with its partners. In this context, two key frameworks for cooperation are the Energy Community Treaty and the UfM, where both the EU and Turkey can play a major role.

The Energy Community Treaty. This is a very good concept, with the right objectives, (some) of the right players, and with an interesting institutional setting. However, it is clearly not sufficiently equipped (in both administrative and financial terms), not sufficiently supported (commitments), and there are issues of compliance and monitoring that need to be more effectively addressed. Turkey currently only holds an observer status. The energy community is going through a revision process, addressing its main shortcomings but also raising its ambitions.

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

But it is not certain whether this process, highly political and intergovernmental, will be supported by its member countries. And it is not certain whether this revision process will change the prospects of Turkey's membership. Furthermore, Turkey has thus far not expressed any interest in becoming a full member of the Energy Community for two main reasons. First, Turkey fears that its full membership to the Energy Community would serve the same purpose as the enlargement process. It wants to prioritise the enlargement process and does not want to see the Energy Community as an alternative to it. Second, Turkey is a large market and wants to keep flexibility in running it rather than binding itself through the Energy Charter Treaty (ECT), while the benefits that the ECT can offer are too limited in comparison.

Mediterranean Energy Community. The UfM and its Mediterranean Solar Plan as its flagship project, is potentially a key element and vector for cooperation on energy issues in the broader Mediterranean area. However, conditions are far from being in place for such a cooperation to emerge. There is a need to develop closer legal, economic, regulatory and financial relationships amongst the Southern Mediterranean neighbours. The EU and Turkey have a big role to play in this respect. They are both by far the biggest markets and foreign actors in the region. They have also important know-how to export. Beyond that, one of the best instruments to achieve cooperation is to bring closer network regulators and operators in the region. The MEDREG/MEDTSO initiative actively supported by the European Commission, and duplicating to a certain extent in the south what was started with Balkan countries in the South East European Energy Community can play a key role in this process. EU and Turkey can again be leading actors in that field. EMRA is part of ERRA (Energy Regulators Regional Association) and MEDREG (Association of Mediterranean Energy Regulators). However, the UfM is not in a very good shape at the moment. Decision between top/down vs. bottom/up approach has not been taken. In the field of energy, the UfM has growing ambitions, even talking about a future Mediterranean Energy Community. But the last UfM Ministerial conference on energy in December 2013 was a failure, with some antagonism between (some) EU member states vs. Turkey (with European Commission) as part of the main reason for the failure.

Conclusion: Muddling through a fast changing energy landscape

EU and Turkey's energy profiles, markets and systems are progressively converging. It offers a good basis for common interests and enhanced cooperation. There are two main areas where cooperation has clear potential, and also where it would be in the interest of both parties: diversification of gas supplies and convergence of energy systems and regulatory framework, leading to a future integration of their energy markets (gas and electricity).

However, their energy policies priorities and interests do not completely match. It is particularly the case in the field of diversification of gas resources and with its concrete project of opening the Southern Corridor. It is therefore not completely

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

clear to what extent Turkey and the EU are partners and competitors in this area.

Their (potential) cooperation in the field is further impeded by other (more) fundamental issues related to the overall future of the relation between the EU and Turkey, mainly through the enlargement process that has been initiated between the two partners. The relations under this vehicle are mostly frozen, and the expectations for a thaw are very low at the moment, with only a few signs of rapprochement. This inevitably has a negative impact on all aspects of EU-Turkey relations, including energy. Vice versa, the fact that the EU and Turkey are not able to cooperate on a number of important issues, including energy, is impeding progress on the enlargement process. Turkey should understand that the first priority, from the EU's perspective, is to bring "Europe" to Turkey, rather than Turkey to the EU.

In this relationship, energy will not be the game changer, and should not be perceived as such. Closer ties with Europe in the field of energy will not pave the way for reopening negotiations on a new spirit leading to full membership for Turkey. In the respect, there is an interesting parallel to be made with the Cyprus settlement issue, and the energy part of this complex *equation*. It is not certain that the discovery of natural gas resources offshore the island is about facilitating a rapprochement between the two sides of the island, or whether it could even complicate an already fragile relationship. New discoveries of gas will not be a game changer for the resolution of the conflict as long as a compromise has not been found on the overall political status of the island. Both regarding Turkish enlargement process and Cyprus settlement, solutions will come only when all parties will accept that the main answer is political in essence, and be ready for a comprehensive deal. It is only through strong political leadership, concessions and commitments on both side on a wide range of issues that the enlargement process will evolve in the right direction.

It becomes obvious that cooperation between the EU and Turkey in the field of energy will be critical if both actors want to develop their projects and ambitions in this area, irrespective of the enlargement process. It is therefore in their interest to cooperate on energy issues in a concrete, pragmatic and non-politicized way. Indeed, there are still many political, economic, industrial, regulatory, financial (etc.) challenges and obstacles to be addressed in the Southern Corridor. There are also external factors that are out of their hands (supply side, etc.), and where a common approach would be essential. This means a rapprochement of respective EU and Turkey's foreign policies in the targeted regions.

Fortunately, there are a wide range of potential policies, instruments and institutions that can serve such a purpose. Several frameworks for cooperation between the EU and Turkey, or including other external actors do exist in principle but they do not fully cover all aspects of energy nexus between EU and Turkey, they are not fully effective in practice, and they are not necessarily supported by Turkey and/or some EU member states. However, these obstacles and challenges will have to be addressed in the near future if both actors want to move ahead together in the field of energy.

What Potential for Cooperation between the EU and Turkey on Diversification of Gas Supply?

Both partners have their work to do. The EU needs to further engage with Turkey and allow the necessary resources matching its ambition in the Southern Corridor and its aim to set a pan-European energy market in the future, including Turkey. Signs of further openness and political appeasement should come from Turkey as well.

They have to find their proper *modus vivendi* (and *operandi*), based on a balanced equilibrium between cooperation/trust and competition. They will never agree on all terms, and remain to a certain extent competitors on certain issues, including in the energy field. This is no surprise, as even within the EU itself, member states are to a very large extent cooperating, but also competitors. This is particularly the case in the field of energy, and the diversification of supply (Nabucco vs. South Stream, and in the future the ambitious Turkish Stream, bilateral relations with Russia, nuclear vs. RES, gas vs. coal, interconnections, etc.).

At the end, the real risk for the two partners in the field of energy is one of muddling through in their relationship. Meanwhile, energy markets are moving fast and operators will not wait for a comprehensive agreement between EU and Turkey on their future relationship, including energy, before taking a decision over the Southern Corridor, the supply, the transit and the consumption of natural gas in the broader region. The price to pay for these mistrust, misunderstandings, and hesitations might increase over time.

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