

THE TENSION BETWEEN TRADE LIBERALIZATION AND RESOURCE SOVEREIGNTY: RUSSIA-EU ENERGY RELATIONS AND THE PROBLEM OF NATURAL GAS DUAL PRICING

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ABSTRACT

In this paper, we explore the underlying legal principles that influence and guide the current energy relationship between the European Union (EU) and the Russian Federation (Russia). Global economic integration in the twenty-first century is premised primarily on legal governance structures, such as the World Trade Organization (WTO), that promote liberalized markets and free trade among nations. Energy governance on the other hand, which is surprisingly weak at the global level, appears to be premised on the principle of permanent state sovereignty over its natural resources (PSNR). This principle allows states to turn inward by giving them exclusive authority over all decisions concerning the disposition of their resource endowment. So, while principles of free trade require global cooperation and transboundary economic integration, principles of resource sovereignty encourage the opposite. While liberalized economies, such as the EU, look to open markets in emerging or transitional economies, Russia has chosen to focus on domination of its resource sector as its primary policy for economic development. This contradiction between trade liberalization on one hand, and principles of resource sovereignty on the other, has created considerable tension between the fundamental policies of Russia and the EU. One example of this tension is that of Russia's gas dual pricing practices. While the practice is less important today than it has been in the recent past, this practice provides a good example of the disagreement that can exist between countries as they work towards creating new principles on the global governance of energy.

I. Introduction

In the context of economic globalization, energy and natural resource governance remains largely undeveloped at the global level.¹ Hardly an oversight on the part of global trade regimes, the lack of sophisticated, specific legal rules on the transboundary trade in energy and natural resources appears to be the result of an inherent tension: between the principles of trade liberalization on one hand,² and the principle of permanent sovereignty over natural resources (PSNR) on the other.³ In terms of economic development, theories abound on the potential benefits that a state can derive from both the liberalization of trade⁴ and the exploitation of its natural resources.⁵ Yet, for a resource-endowed state such as the Russian Federation (Russia), trade liberalization must not come at the cost of sovereign control over its natural resource sector, especially when this sector is the primary

¹ “Energy was not specifically addressed by international agreements for a long time, and was mostly treated in a political context as a special case. It is now commonly accepted that the existing WTO rules apply equally to energy products. These rules are not, however, well designed to address some trade-related issues in the energy sector.” Y. Selivanova, *The WTO and Energy: WTO Rule and Agreements of Relevance to the Energy Sector*, ICTSD Trade and Sustainable Energy Series Issue Paper No. 1, International Centre for Trade and Sustainable Development (2007), vii.

² The international trade regimes that have developed in the past fifty years are premised on the idea that reductions in excessive tariffs and trade barriers (the liberalization of trade) create mutual economic advantages and benefits to states. The fundamental principles of the WTO and the GATT embody this approach and have been embraced by a vast majority of the world’s states. *Marrakesh Agreement Establishing the World Trade Organization*, April 15, 1994, 1867 U.N.T.S. 154, 33 I.L.M. 1144 (1994) [hereinafter *WTO Agreement*]; *General Agreement on Tariffs and Trade*, October 30, 1947, 61 Stat. A-11, T.I.A.S. 1700, 55 U.N.T.S. 194 [hereinafter *GATT*].

³ The principle of PSNR states that every state has the full and inherent sovereign right to control and exploit its own natural resources in accordance with the United Nations Charter and the principles of international law.

⁴ According to free trade theories, the greatest benefits of trade among nations can be derived when policies include little or no governmental restrictions on trade from tariffs and other types of trade barriers. Under a free, or fully liberalized trade regime, prices would be a reflection of true supply and demand, and would be the sole determinant of resource allocation (*laissez-faire* economic theory). As such, free trade policies differ from other forms of trade policy where the allocation of goods and services amongst trading countries are determined by artificial prices that may or may not reflect the true nature of supply and demand (command or non-market economies).

⁵ The benefits that a state can gain from resource exploitation are well-documented. However, a state’s complete reliance on natural resources often limits its ability to integrate fully into the global economy (and to enjoy the benefits of trade liberalization). Likewise, a fully liberalized state will often regulate its resource sector in a manner that limits the maximum benefit that could be derived from the exploitation of its natural resource endowment.

source of state revenue.⁶ This means that Russia's accession to the World Trade Organization (WTO) will likely occur only if its fundamental policies in regard to natural resource exploitation remain unaffected.⁷ From an economic perspective, Russia is not unique in this outlook, as most resource-endowed countries view their path to economic prosperity directly tied to the exploitation of their domestic resources.⁸ While such a strategy often results in the emergence of the so-called resource curse, sovereign states have been reluctant to take heed.⁹ From an international legal perspective, a state's ability to use its resource endowment as a tool of economic development has been declared repeatedly as the principle of PSNR.¹⁰ Likewise, principles of trade liberalization are hallmarks of modern economic globalization and are enshrined as international legal rules in the WTO and the multitude of regional trade agreements it endorses.¹¹ While decisions and policies about global trade necessitate collective and multilateral cooperation, natural resource exploitation decisions remain within the exclusive purview of the resource-endowed state. With much of global trade reliant on energy and natural resource inputs, these potentially contradictory principles can create problems for

⁶ The first paragraph of the *Energy Strategy of Russia in the Period to 2020* states that Russia's "mighty energy sector" is "an instrument for the conduct of internal and external policy" and that "the role of the country in world energy markets to a large extent determines its geopolitical influence" *The Summary of the Energy Strategy of Russia for the Period of up to 2020*, Ministry of Energy of the Russian Federation (2003), available at: http://ec.europa.eu/energy/russia/events/doc/2003_strategy_2020_en.pdf.

⁷ See for example, H. Balzer, *Russia Opts for State Power over Free Markets, or Why is Khodorkovsky in Jail?*, Johnson's Russia List, October 31, 2003, reprinted online at: www.gateway2russia.com/st/art_161898.php.

⁸ "The aim of energy policy is to make most effective use of the natural fuel and energy resources and of the potential of energy sector for economic growth and improvement of life quality." *The Summary of the Energy Strategy of Russia*, supra note 6.

⁹ The resource curse refers to the paradox that countries and regions with an abundance of natural resources, specifically point-source non-renewable resources like minerals and fuels, tend to have less economic growth and worse development outcomes than countries with fewer natural resources. This is hypothesized to happen for many different reasons, including a decline in the competitiveness of other economic sectors (caused by appreciation of the real exchange rate as resource revenues enter an economy), volatility of revenues from the natural resource sector due to exposure to global commodity market swings, government mismanagement of resources, or weak, ineffectual, unstable or corrupt institutions (possibly due to the easily diverted actual or anticipated revenue stream from extractive activities).

¹⁰ See section III below.

¹¹ See generally, *WTO Agreement*.

resource-endowed states as they seek to be integrated into global trading regimes.¹² In the context of the energy relationship between the European Union (EU) and Russia, this tension plays a fundamental role. This article will explore issues relating to energy and natural resource governance between the EU and Russia with emphasis on Russia's WTO accession bid, the principle of PSNR, and the particular problem of natural gas dual pricing.

II. Dual Pricing and the Russia-EU Energy Relationship

The energy relationship between the EU and Russia is complex and strife with potential conflict. At the heart of this relationship is a co-dependent reliance on Russian natural gas supplies.¹³ Russia is endowed with the world's largest known reserves of natural gas.¹⁴ It is a major gas-exporting country and the EU is a major importer of Russian gas.¹⁵ This reliance on Russian gas supplies has led the EU to become increasingly alarmed at the potential energy security issues such reliance creates.¹⁶ This problem is exacerbated by seemingly divergent agendas relating to market and trade liberalization. The EU has for decades been at the forefront of supra-national governance relating to the creation of common markets and reductions in internal trade barriers, particularly in the area of energy.¹⁷ Russia on the other hand has pursued policies focusing on the state's monopolization of its

¹² Energy subsidization by resource-endowed states can give unfair advantage to particular industries. For example, a state that provides cheap energy inputs to energy-intensive industries, such as steel or fertilizer producers, gives those industries the ability to produce their products at a price lower than the true cost of production.

¹³ P. Noel, *Beyond Dependence: How to Deal with Russian Gas*, ECFR Policy Brief, European Council on Foreign Relations (2008).

¹⁴ BP, *BP Statistical Review of World Energy 2008*, British Petroleum (2008); IEA, *World Energy Outlook 2008*, International Energy Agency (2008).

¹⁵ Noel, *supra* note 13.

¹⁶ Commission of the EC, *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: An EU Energy Security and Solidarity Action Plan*, Second Strategic Energy Review, COM(2008) 781 Final, Brussels, 13 November 2008; A. Monaghan, *Russia-EU Relations: An Emerging Energy Security Dilemma*, Carnegie Endowment for International Peace (2003), available at: <http://www.carnegieendowment.org/files/EmergingDilemma1.pdf>.

¹⁷ See for example, Directive 2009/73/EC of the European Parliament and of the Council of 13 July 2009 Concerning Common Rules for the Internal Market in Natural Gas and Repealing Directive 2003/55/EC (Text with EEA relevance).

natural resource sector.¹⁸ These resource utilization policies have played a large role in Russia's delayed entrance in to the WTO. As such, Russia remains the largest economy still outside the multilateral trade governance of the WTO.¹⁹ Although Russia began the accession process in 1993, some issues remain unresolved.²⁰ One of the impediments to its WTO accession related to its gas pricing policies.²¹ Labelled as gas dual pricing, Russia has pursued policies that price natural gas exports distinctly from prices for domestic use.²² Opponents of Russian dual pricing, such as the EU and the United States (US), hold that such a practice can provide energy so inexpensively to the industrial and manufacturing sector that the export price of certain goods produced can be sold in export markets at prices significantly lower than end-user products produced in countries that do not suppress the domestic price of its energy inputs.²³ Likewise, domestic products that have benefited from cheap energy inputs may have the ability to make like goods imported into that market less able to compete with products that have benefited from the suppressed domestic gas prices.²⁴ However, when a resource-endowed country, such as Russia, is merely using its natural comparative advantage in a non-discriminatory manner to promote the development of its domestic industry, the

¹⁸ S. Pirani (ed.), *Russian and CIS Gas Markets and Their Impact on Europe*, (New York: Oxford University Press, 2009).

¹⁹ D. Tarr, *Russian WTO Accession: Achievements, Impacts, Challenges*, OECD (2008), 1, available at: <http://www.oecd.org/dataoecd/28/4/40747249.pdf>.

²⁰ "Many energy-endowed countries [including Russia] still remain outside the WTO system. Energy policies of these countries have become a concern for industrialized WTO Members. They try thus to use the accession negotiations to address energy issues. Energy-importing states are interested to address issues such as pricing practices, natural resource development policies, procurement in the energy sector, and restrictive practices of incumbent energy companies. Some acceding countries have faced demands to fully liberalize their energy services sector, to eliminate export taxes and dual price systems, and even unbundle energy monopolies. Whereas some of the applicants conceded to WTO Members' demands and changed their regulations [such as Saudi Arabia and China], some others [including Russia] insist that these demands go beyond the standard WTO provisions and represent so-called 'WTO-plus' requirements." Selivanova, *supra* note 1, x.

²¹ D. Tarr, *Political Economy of Russian Trade Policy: Early Transition, Customs Unions, WTO Accession and Protection for Industrial Diversification*, Paper Prepared for the Conference on 'The Political Economy of Trade Policy in the BRICs,' New Orleans, Louisiana, 27-28 March 2009.

²² *Id.*

²³ W. Cooper, *Russia's Accession to the WTO*, Congressional Research Service Report for Congress, RL31979, 17 July 2006, 10-11.

²⁴ D. Dudek et al., *Should Russia Increase Domestic Prices for Natural Gas?* 34 *Energy Policy* 1659, 1668-1669 (2006).

practice of dual pricing would be neither prohibited nor actionable under the WTO. In fact, such a practice is theoretically encouraged under the Ricardian economic theory of comparative advantage:²⁵ a theory that lies at the heart of liberal trading system such as the WTO.²⁶ While the practice of dual pricing in Russia has been shown to be implemented in a non-discriminatory manner with limited trade distorting effects²⁷ – and thus was dropped from the EU agenda on Russia’s WTO accession bid²⁸ – dual pricing still persists in Russia (at least in the short-term)²⁹ and therefore provides a good example of the tension between the principle of PSNR on one hand and principles of trade liberalization on the other. In the case of Russia, resource sovereignty has been pursued in the last decade as the primary policy for economic development and national security.³⁰ In his 1999 PhD dissertation, Vladimir Putin laid out the Russian strategy for regaining its title as a global superpower.³¹ His proposal, which happens to closely mirror the current reality in Russia, calls for state monopolization of its natural resource sector as the primary

²⁵ However, it must be noted that Ricardo’s theory of comparative advantage applied only in the context of market economics. That is, for a state-controlled economy such as Russia, the theory of comparative advantage does not necessarily apply. If a country uses state power to derive monopolistic control over its resource base, then any application of Ricardo’s theory would actually distort trade.

²⁶ The law of comparative advantage states that each member in a group of trading partners should specialize in and produce the goods in which they possess lowest opportunity costs relative to other trading partners.

²⁷ While the practice of dual pricing of natural gas was a highly controversial issue in the bilateral WTO accession negotiations between the EU and the US, the practice of suppressed domestic gas supplies in Russia is implemented equally to all sectors of the Russian economy and thus has been shown to have fewer trade distorting effects than if the practice gave specific price reductions to particular industries. Tarr, *supra* note 19.

²⁸ In the Russia-EU bilateral agreement on Russia’s WTO accession, Russia reportedly was not required to unify its domestic and export price of natural gas. Russia, however, was expected to raise its domestic price to the long run marginal costs of Gazprom. *Russia-EU Bilateral Market Access Agreement*, 21 May 2004.

²⁹ While dual pricing practices still exist in Russia, Russia decided to raise its domestic prices in parity with export costs beginning in 2011. Later, however, this target was changed for 2014. According to Gazprom, “the government will stop subsidizing domestic gas prices by 2014 as Gazprom seeks to profit from sales at home to help fund new fields and pipelines.” *The Moscow Times, Domestic Gas to Lose Subsidies*, 26 March 2010, available at: <http://www.themoscowtimes.com/business/article/domestic-gas-to-lose-subsidies/402584.html>.

³⁰ H. Balzer, *The Putin Thesis and Russian Energy Policy* 21 *Post-Soviet Affairs* 210 (2005).

³¹ V. V. Putin, *Mineral’no-Syr’evyye Resursy v Strategii Razvitiya Rossiyskoy Ekonomiki (Mineral Natural Resources in the Strategy for Development of the Russian Economy)*, *Zapiski Gornogo Instituta*, 144, 3 - 9, 1999.

means of building a strong, central state.³² This monopolization and tight state control of the natural gas sector, primarily through the state-controlled enterprise Gazprom, has permitted Russia to set pricing policies on its natural gas endowment in a manner not fully consistent with market forces, but rather in line with natural resource pricing policies consistent with what Russia believes to be in its national interest.³³ However, the ability of a state to set domestic and export prices unilaterally is usually a symptom of anti-competitive behaviour.³⁴ As such, natural resource monopolies generally, and state-controlled natural resource monopolies specifically, are considered to be antithetical to the achievement of liberalized global trading regimes because of their high potential to distort markets and trade.³⁵ These are the main reasons why most industrialized, as well as some developing countries, have abolished energy dual pricing as being inconsistent with their new liberalized energy and competition policies.³⁶ Russia has gone the opposite direction however. It continues to regard its energy policy as a tool for regaining its title as a global superpower.³⁷

The EU, and those countries that have embraced the logic of the GATT and the WTO, hold that liberalized trade and free markets are the best policy for

³² Putin's "general conclusion" in his dissertation is that "the existing socio-economic conditions and also the strategy for Russia's exit from the deep crisis and restoration of its former power on a qualitatively new basis demonstrate that the condition of the natural resource complex remains the most important factor in the state's development in the near term." *Id.*, 9.

³³ Putin asserts in his dissertation that rational resource use, environmental protection, and ensuring long-term economic security are beyond the capacity of market mechanisms. "In Russia, as a consequence, it is necessary to implement this principle of rational resource use by an organic combination of market mechanisms of self-regulation and support for rational resource use and conservation." *Id.*, 7.

³⁴ In addition to Russian energy policies based on the exploitation of its natural resource endowment, Russia further exacerbates the tension between resource sovereignty and trade liberalization by pursuing economic policies that do not allow market mechanisms (as theoretically embraced by the WTO and the EU) to operate freely.

³⁵ While there is no multilateral set of rules on competition under the WTO regime, anti-competitive behaviour through state-controlled monopolies creates many opportunities for trade distorting practices. State-controlled natural resource monopolies have the specific capacity to subsidize energy to its domestic population in a manner that can give industries a competitive export advantage as goods produced with cheap energy inputs do not reflect the true cost of production.

³⁶ Selivanova, *supra* note 1, x.

³⁷ A. Tsygankov, *Vladimir Putin's Vision of Russia as a Normal Great Power*, 21 *Post Soviet Affairs* 132 (2005).

economic development and global integration.³⁸ This approach may be true for the majority of developed countries in the world, but it can work to the disadvantage of resource-endowed states that have yet to fully enjoy the fruits of industrialization.³⁹ While the Russian policy of state-controlled natural resource domination does not mesh cleanly with EU energy liberalization policies, it is substantively similar to the economic policies pursued by EU member countries during their periods of industrialization.⁴⁰ Therefore, a practice such as dual pricing is actually just a smaller debate encapsulated in the broader trade policy debate currently being hashed out under the Doha Development Round between developing and developed countries.⁴¹ While developing countries argue that absolute control over their resource endowment is critical for their economic development, developed countries argue that opening borders and liberalizing trade (including trade in their resources) is a better means of achieving economic growth. However, as Putin's PhD dissertation attests, Russia has chosen to pursue policies whereby resource control trumps market liberalization.⁴²

Russia has practiced a system of dual pricing from 1990 to the present, providing natural gas domestically at prices well below the export market price.⁴³ Natural gas is provided at suppressed prices equally to all sectors of the economy.⁴⁴

³⁸ These principles of free trade that are embraced by the WTO hold that reductions in trans-national barriers to trade will result in mutual benefit for all countries involved. By embracing cooperation in trade, countries can achieve long-term economic gains even if in the short-term free trade measures appear to harm particular industries that are exposed to international competition through reductions in protective measures taken by the state within which these industries operate.

³⁹ In the case of developing or transitional economies, arguments for complete trade liberalization are difficult to embrace from an economic development perspective if they require developing states to give up some control of their natural resources or reduce measures that protect domestic industries from exposure to competition from more developed global industries.

⁴⁰ Almost every developed country in the EU industrialized in the 18th and 19th centuries as a result of inexpensive natural resource inputs from their colonies.

⁴¹ Under the current Doha Development Round of trade negotiations, developing countries argue that trade policies must conform to their right to economic development. This right to development includes the ability of industrializing developing countries to exploit their natural resources in a manner that promotes its economic well-being – even if such permissions are contrary to developed country agendas on trade liberalization and environmental protection.

⁴² Putin, *supra* note 31.

⁴³ D. Dudek et al., *Environmental Aspects of Dual Pricing for Natural Gas in Russia*, Environmental Defence, Moscow (2004), 4.

⁴⁴ *Id.*

Dual pricing practices are thought to have a number of positive developmental benefits, and are thus pursued in resource-endowed states as part of a broader economic policy. Developing and transitional economies argue that the practice of dual pricing is one that can be used to foster economic development, while at the same time providing inexpensive energy (for cooking, heating, electricity) to the poorest strata of society.⁴⁵ On the other hand, developed countries hold that such practices are determinately; they accelerate the exhaustion of natural resources, pollute the environment, and contribute to global climate change.⁴⁶ While these potential environmental costs and social benefits are important to the debate, additional economic concerns often arise when a resource-endowed state provides resources domestically at subsidized rates.⁴⁷ In the case of Russian practice, natural gas is not just subsidized, it was subsidized at prices below the long-term marginal cost of production.⁴⁸ That is, the Russian government was providing natural gas so inexpensively that it had to directly subsidize the natural gas industry in order to sustain the practice.⁴⁹ The World Bank has proposed that at a minimum, Russia raise domestic natural gas prices to the long-term marginal cost of production level.⁵⁰ Following this suggestion, Russia has been increasing the domestic price of natural gas in recent years in consideration of its marginal costs of production. Moreover, recent developments show that Gazprom's internal policies are now embracing a strategy that will continue to increase natural gas prices whereby domestic prices will reach parity with export prices (excluding transport costs) by 2014.⁵¹ This strategy does not appear to be the result of external pressure, but rather reflects internal decision-making as Russia realizes that long-term costs of major capital investments (pipelines, etcetera) will require a rise in domestic gas prices.⁵²

⁴⁵ *Reforming Energy Subsidies: An Explanatory Summary of the Issues and Challenges in Removing or Modifying Subsidies on Energy that Undermine the Pursuit of Sustainable Development*, United Nations Environment Programme, Division of Technology, Industry, and Economics (2002), 6.

⁴⁶ Dudek, *supra* note, 4.

⁴⁷ *Id.*

⁴⁸ D. Tarr and P. Thomson, *The Merits of Dual Pricing of Russian Natural Gas*, 27 *The World Economy* 1173 (2004).

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ *See supra* note 29.

⁵² *Id.*

Overall, the Russia-EU energy relationship is governed by a co-dependent reliance on Russian gas supplies. This reliance is placed within the context of substantively distinct energy policies in the EU and Russia. The difference in these policies is the result of a number of complex issues that relate to each political entity's place in history, stage of development, and resource endowments. The EU would like to see Russia embrace energy policies that are driven by market forces whereby natural gas supplies to Europe would be the product of competitive, open markets. In addition, the EU is concerned about the distortive effect of energy dual pricing in Russia on the Russia-EU trade in energy-intensive products. Russia, on the other hand, believes that the market liberalization of its resource sector would constrain its economic development and prevent it from re-emerging as a global superpower. And as such, a tension persists.

III. PSNR and the WTO

Since the 1950's, developing countries have repeatedly reiterated that a state retains full sovereignty over the use of its natural resources.⁵³ United Nations (UN) General Assembly (GA) Resolution 1803 on the principle of PSNR expressly recognizes that the *"right of peoples and nations to permanent sovereignty over their natural wealth and resources must be exercised in the interest of their national development and of the well-being of the people of the State concerned."*⁵⁴ This concept developed at the end of the colonial period as a means for newly recognized states to shed themselves from not only their political oppression, but economic oppression as well.⁵⁵ From a public international law perspective, the result has

⁵³ *"The motives for formulating the principle of permanent sovereignty and the objectives to be pursued by it are obvious. The principle was developed during the 1950s, as part of an effort both to secure the benefits arising from exploiting natural resources for peoples living under colonial rule and to provide newly-independent States with a shield against infringements upon their sovereignty by foreign States or companies."* N. Schrijver, *Sovereignty over Natural Resources: Balancing Rights and Duties in an Interdependent World*, PhD Thesis, Rijksuniversiteit Groningen (1995), 24, available at: <http://dissertations.ub.rug.nl/FILES/faculties/jur/1995/n.j.schrijver/thesis.pdf>.

⁵⁴ *Permanent Sovereignty over Natural Resources*, G.A. res. 1803 (XVII), U.N. Doc. A/5217 (1962).

⁵⁵ According to Nico Schrijver, one of the reasons for the development of the PSNR was the end of colonial rule and the increasing demand by newly formed states calling for the *"demand for economic independence and strengthening of sovereignty. The decolonization process entailed a claim to economic self-determination."* N. Schrijver, *supra* note 53.

been the development of a general principle of international law that appears to be an obvious truism of sovereignty:⁵⁶ resource-endowed states have the sovereign right to the exclusive control over decisions on how their natural resource endowments are exploited.⁵⁷ The right of Russia to use its energy resources for economic development and wealth is based on this general principle of PSNR.⁵⁸

In the most recent statement by the UN on the principle of PSNR, the Security Council declared PSNR as a general principle of international law: “*every state has the full and inherent sovereign right to control and exploit its own natural resources in accordance with the both the UN Charter and general principles of international law.*”⁵⁹ In addition to resolutions and declarations made by the UN GA and Security Council, the principle of PSNR has been acknowledged in the treaty law as well. For example, in the Energy Charter Treaty (ECT) of 1994, Article 18 provides that “[t]he Contracting Parties recognize state sovereignty and sovereign rights over energy resources. They reaffirm that these must be exercised in accordance with and subject to the rules of international law.”⁶⁰

⁵⁶ As Rosalyn Higgins clarifies, this principle has emerged as a customary rule of general public international law, developing through UN resolutions and acknowledgement in international tribunals and writings. See R. Higgins, *Problems and Process: International Law and How We Use It* (New York: Clarendon Press, 1994).

⁵⁷ For the most recent UN declaration on PSNR, see *Statement by the President of the Security Council*, 25 June 2007, UN Doc. S/PRST/20-07/22 [hereinafter *Security Council Statement*].

⁵⁸ Along these lines, UN GA Resolution 626 recommends all member states “to refrain from acts direct and indirect, designed to impede the exercise of the sovereignty of any state over its natural resources.” *The Right to Exploit Freely Natural Wealth and Resources*, United Nations General Assembly Resolution 626 (VII) (1952), available at: http://www.un.org/documents/ga/_res/7/ares7.htm; Later, UN GA Resolution 2158 confirmed the above right in the context of developing countries’ needs. On the latter resolution Nico Schrijver observed as follows: “the General Assembly recognizes in this resolution that ‘the natural resources of the developing countries constitute a basis of their economic development in general and of their industrial progress in particular’, that ‘it is essential that their exploitation and marketing should be aimed at securing the highest possible rate of growth of the developing countries’, and that ‘this aim can better be achieved if the developing countries are in a position to undertake themselves the exploitation and marketing of their natural resources.’” N. Schrijver, *Sovereignty over natural resources: Balancing rights and duties*, (New York: Cambridge University Press, 1997), 270; See also *Permanent Sovereignty over Natural Resources*, United Nations General Assembly Resolution 2158 (XXI) (1966), available at: <http://www.un.org/documents/ga/res/21/ares21.htm>.

⁵⁹ *Security Council Statement*

⁶⁰ *The Energy Charter Treaty* (1994), available at: http://www.encharter.org/fileadmin/user_upload/document/EN.pdf.

Despite these iterations of the principle of PSNR by developing and transitional economies over the past fifty years, Russia's natural gas pricing does not appear to be in line with the underlying principles of free trade and economic integration as endorsed by the WTO. This is noteworthy because under international law a state, although has the sovereign right to decisions over its national energy policies, it also has a sovereign right to contract out from general rules of international law, such as the principle of PSNR, by entering into treaties.⁶¹ In other words, treaties may impose certain limitations on general public international law that reduce a sovereign states ability to pursue their domestic energy pricing policies in accordance with the principle of PSNR. One example of this type of treaty is the Agreement Establishing the WTO (WTO Agreement). According to professor Pauwelyn, the WTO Agreement is a treaty that places some restrictions on the application of general principles of international law.⁶² Yet, these restrictions are limited to the specific rules thereof. This is because the WTO regime constitutes a *lex specialis* that provides specific rules that will prevail over more general rules of international law: *lex generalis*.⁶³ In the WTO there are a few rules – mostly relating to state-trading enterprises (STEs), subsidies, and anti-dumping measures– that have the potential to place some limitations on a countries ability to freely exploit their natural resources.⁶⁴ These potential limitations will be explored in the next section.⁶⁵

IV. Dual Pricing in Russia and Its Consistency with WTO Law

When addressing the issue of the consistency of gas dual pricing with WTO law, the most relevant rules in this respect appear to be the GATT Article XVII (WTO

⁶¹ This right is based on the concepts of the state sovereign consent to treaties and *pacta sunt servanda*. These both concepts represent customary international law and are codified in the Vienna Convention on the Law of Treaties 1969, available at: http://untreaty.un.org/ilc/texts/instruments/english/conventions/1_1_1969.pdf; See also J. Pauwelyn, *Conflict of Norms in Public International Law: How WTO Law Relates to Other Rules of International Law* (New York: Cambridge University Press, 2003).

⁶² *Id.*

⁶³ *Id.*

⁶⁴ These are the primary rules that have the potential to interfere with Russia's absolute application of the principle of PSNR if it were to become a Member of the WTO.

⁶⁵ See section IV *below*.

rules on STEs), WTO Subsidies, and Anti-Dumping rules. This category of rules have constituted the major basis for anti-dual pricing claims made by net energy-importing countries vis-à-vis Russia as well as other energy-endowed developing countries. In a similar context, some scholars have also referred to the GATT Article III:9 (a soft-law provisions recognizing that internal maximum price control measures can negatively affect exporting countries), Article XI:1 thereof (General Elimination of Quantitative Restrictions), and the Agreement on Trade-Related Investment Measures (TRIMs)⁶⁶ (such as when a government provides low-cost energy inputs on the condition that foreign investors comply with the local content requirement).⁶⁷ Regarding the GATT Article XI:1, it has been argued that energy dual pricing has a *de facto* effect equivalent to an imposition of export restrictions.⁶⁸

Nevertheless, the latter category of rules appears to be of little relevance to gas dual pricing in Russia. For instance, the GATT Article III:9 does not establish any hard-law obligation and has merely a declaratory nature. Article XI:1 appears to prohibit the export restrictions only on those natural resources that have been already extracted from the ground (such as not covering energy development projects).⁶⁹ In addition, considering that in practice exports of natural gas from Russia to the EU are executed through long-term agreements, energy dual pricing in Russia cannot have any impact on the volumes of gas export to this market. Regarding the TRIMs Agreement, the Russian government has never been accused of tying its low-cost gas to a local content requirement. On the basis of the above

⁶⁶ *Agreement on Trade-Related Investment Measures*, April 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, The Legal Texts: The Results of the Uruguay Round of Multilateral Trade Negotiations 143 (1999), 1868 U.N.T.S. 186 [hereinafter *TRIMs Agreement*].

⁶⁷ See Y. Selivanova, *Energy Dual Pricing in the WTO: Analysis and Prospects in the Context of Russia's Accession to the World Trade Organization* (UK: Cameron May, 2008); D. Behn, *The Effect of Dual Pricing Practices on Trade, the Environment, and Economic Development: Identifying the Winners and the Losers under the Current WTO Disciplines*, SSRN, 17 December 2007, available at: <http://ssrn.com/abstract=1151553>; S. Zarrilli, *Dual Pricing Practice and WTO Law*, Oil, Gas, and Energy Law Intelligence, Vol. 3, Issue 3 (October 2005).

⁶⁸ The argument holds that by keeping domestic energy prices low, a state artificially inflates its energy demand, which, in turn, results in the diversion of energy development or supply projects from export to domestic market. See Selivanova, *supra* note 67.

⁶⁹ See M. Desta, *Challenging OPEC Countries before the WTO: A Legal Analysis* in A. Reinisch (ed.), *OPEC and International Law*, (The Netherlands: Eleven International Publishing, 2010), 177.

considerations, this section will analyze the consistency of gas dual pricing in Russia with the GATT Article XVII, WTO Subsidies, and Anti-Dumping rules. It has a particular focus on the latter, since it has been already established by other researchers that energy dual pricing in Russia does not constitute a subsidy incompatible with WTO law and does not trigger the GATT Article XVII.⁷⁰

A. The GATT Article XVII

Energy dual pricing in Russia complies with the requirements of the GATT Article XVII. Article XVII:1 (a) provides that if a Member establishes or maintains an STE or grants to any enterprise exclusive or special privileges, such an enterprise, in its purchases or sales involving imports or exports, must act in a manner consistent with the general principle of non-discrimination.⁷¹ The following provision (Article XVII:1 (b)) clarifies that the obligation established by Article XVII:1 (a) shall be understood to require that STEs or the enterprises granted exclusive or special privileges must make any purchases or sales involving imports or exports solely in accordance with commercial considerations.⁷² It should be noted that the latter requirement does not constitute a separate obligation, but merely defines the obligation set out in Article XVII:1 (a).⁷³

The key questions that have been addressed when deciding on the compatibility of gas dual pricing in Russia with the GATT Article XVII:1 are whether Gazprom qualifies as an STE or an enterprise granted exclusive or special privileges, and whether its different pricing for domestic and foreign consumers amounts to unlawful discrimination? Concerning the first question, it should be noted from the outset that WTO law does not define either the terms “STE” or “an enterprise granted exclusive or special privileges.” It provides only a limited guidance in the WTO Background Paper on STEs and the Uruguay Round Understanding on the

⁷⁰ See Selivanova, *supra* note 67; S. Ripinsky, *The System of Gas Dual Pricing in Russia: Compatibility with WTO Rules*, 3 *World Trade Review* 463 (2004).

⁷¹ GATT, Article XVII:1.

⁷² *Id.*

⁷³ See *Canada – Administration of the Foreign Investment Review Act (FIRA)*, GATT Panel Report, BISD 30S/140, adopted on 7 February 1984, para 5.16; *Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain*, Appellate Body Report, WT/DS276/AB/R, adopted on 27 September 2004, para 145.

Interpretation of the GATT Article XVII regarding relevant criteria for making decisions.⁷⁴ For instance, although the Background Paper on STEs states that the degree of the government's ownership and the ability to exercise control over a given enterprise should be those necessary criteria for determining whether it is an STE or not, this paper does not provide specific determinants or establish a percentage of necessary control. Considering that Gazprom exercises control over the gas pipeline network and major processing plants in Russia, as well as negotiates and administers bilateral contracts for the supply of gas from Russia to Europe and the CIS, the mainstream view is that it possesses exclusive or special privileges and constitutes an STE in the sense of the GATT Article XVII.⁷⁵ It should be noted that in 2003 during the accession negotiations of Russia to the WTO, Russia's representatives acknowledged the status of Gazprom as an STE.⁷⁶

Concerning the second question, it is effectively about whether the obligation of "non-discrimination" in Article XVII:1 covers only the most-favoured nation (MFN) provisions, or both the MFN and the national treatment (NT) requirement? In *Korea – Various Measures on Beef* the Panel stated that "*general principle of non-discrimination [in the GATT Article XVII:1 (a)] includes at least the provisions of Articles I and III of GATT [such as both the MFN and NT requirement]*".⁷⁷ It should be noted, however, that this interpretation of Article XVII:1 (a) does not reflect the language of the provision itself and appears to contradict its negotiating history. The wording of Article XVII:1, when establishing the obligation for STEs and the enterprises granted exclusive or special privileges to comply with the principle of non-discrimination, refers only to purchases or sales involving either "imports or exports" without addressing the issue of domestic sales. Moreover, as the negotiating history of Article XVII:1 (a) suggests, this provision intended to cover only

⁷⁴ See WTO, *Operations of State Trading Enterprises as They Relate to International Trade*, Background Paper by the Secretariat, G/STR/2, 26 October 1995, para. 95; *The Understanding on the Interpretation of Article XVII of the GATT*, available at: http://www.wto.org/english/docs_e/legal_e/legal_e.htm.

⁷⁵ See Selivanova, *supra* note 67.

⁷⁶ See *Draft Report of the Working Party on the Accession of the Russian Federation to the World Trade Organization*, Working Party on the Accession of the Russian Federation, WT/ACC/SPEC/RUS/25/Rev.2, 26 May 2003, p. 120.

⁷⁷ *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, Panel Report, WT/DS161/R, WT/DS169/R, adopted on 10 January 2001, para 753.

the MFN and not the NT obligation.⁷⁸ In light of these arguments, the very general interpretation of Article XVII:1 given in *Korea – Various Measures on Beef* cannot provide sufficient means to read the NT requirement into this provision. Therefore, using different prices for domestic and national consumers does not appear to constitute discrimination in the sense of the GATT Article XVII:1 (a).

The last issue to be clarified in relation to the GATT Article XVII:1 is that the practice of Gazprom to charge different prices in different foreign markets is also in line with WTO law. The Ad note to the GATT Article XVII:1 (such as Ad Article XVII) establishes that the GATT Article XVII:1 does not preclude the STEs of WTO Members from charging different prices in different markets, provided that such different prices are charged for commercial reasons, and to meet conditions of supply and demand in export markets.⁷⁹ Consequently, gas dual pricing in Russia is compatible with the GATT Article XVII:1.

B. Subsidies Rules

Dual pricing in Russia does not constitute a subsidy incompatible with WTO law. In the WTO, the rules on subsidies are set out in the Agreement on Subsidies and Countervailing Measures (ASCM).⁸⁰ This Agreement controls the use of specific subsidies and regulates the actions that WTO Members can take to counteract the effects of another Member's trade-distorting subsidies.⁸¹ According to the ASCM, three elements must be present for a subsidy to exist: (1) a financial contribution by a government or any public body within the territory of a WTO Member, or when a government or a public body entrusts or directs a private body to carry out this function; (2) benefit resulting from this financial contribution; and (3) specificity.⁸² The ASCM tackles two main categories of subsidies: (1) the so-called "prohibited subsidies", which are *de jure* or *de facto* tied to export performance or are

⁷⁸ See the negotiating history of the GATT Article XVII:1 quoted from Selivanova, *supra* note 67, 104.

⁷⁹ GATT.

⁸⁰ *Agreement on Subsidies and Countervailing Measures*, April 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, The Legal Texts: The Results of the Uruguay Round of Multilateral Trade Negotiations 275 (1999), 1867 U.N.T.S. 14. [hereinafter *ASCM*].

⁸¹ See P. Van den Bossche, *The Law and Policy of the World Trade Organization: Text, Cases, and Materials*, (Cambridge: Cambridge University Press, 2005), 551.

⁸² *ASCM* Article 1.

contingent upon the use of domestic over imported goods (such as a local content requirement); and (2) the so-called “actionable subsidies,” which cause adverse effect to the interests of other WTO Members either in the form of injury to their domestic industry, or nullification or impairment of their benefits accruing due to their membership in the WTO, or a serious prejudice to their interests.⁸³ The former category of subsidies is considered to be specific automatically and when the financial contribution, benefit and the contingency upon export performance or local content requirement are proven, they are regarded as WTO-inconsistent.⁸⁴ The latter category of subsidies requires the proof of specificity.⁸⁵ For the purposes of the analysis of gas dual pricing in Russia, the key questions that have puzzled trade negotiators and scholars are whether the provision of low-priced gas inputs by Gazprom to domestic consumers, firstly, confers the benefit, and, secondly whether it confers that on the specific recipients in the sense of the ASCM? This analysis concerns the category of “actionable subsidies,” since the use of “prohibited subsidies” does not appear to be an issue in Russia.

The main difficulty in proving benefit lies in the absence of a commonly accepted benchmark applicable to trade in energy resources. In WTO jurisprudence the panels and the Appellate Body (AB) clarified that the notion of benefit implies that after the financial contribution occurred the recipient receives an advantage relative to applicable commercial benchmarks reflecting its situation on the marketplace before and after the financial contribution, and hence it becomes “better off.”⁸⁶ In the case of gas trade, however, it remains unclear whether international market or domestic market in Russia should be used for the calculation of benefit conferred on Russian domestic consumers. These two marketplaces obviously imply the use of different gas prices as benchmarks. Whereas in the first case, the benefit will be derived from the difference between international and Russian domestic gas prices, in the second case, the benefit does not seem to exist at all. It should be noted that although, in principle, WTO jurisprudence allows

⁸³ ASCM Article 3 and 5.

⁸⁴ ASCM Article 2.3 and 3.

⁸⁵ ASCM Article 1.2.

⁸⁶ See *Canada – Measures Affecting the Export of Civilian Aircraft*, Appellate Body Report, WT/DS70/AB/R, 2 August 1999.

referring to other benchmarks than domestic market, for instance, when prices are distorted by the government, in the case of natural gas the alternative reference points appear to be limited.⁸⁷ Currently, international market for natural gas does not exist as yet; and natural gas is mainly traded on a regional level with varying prices between different regions.⁸⁸ It is noteworthy also that even if other benchmarks than domestic gas prices in Russia are established for calculating benefits conferred on Russia's energy-intensive industries, the WTO law requires this benchmark to reflect the prevailing market conditions in Russia, and to take into account any relevant comparative advantage of Russia in regard to gas production.⁸⁹

Another stumbling block in proving that gas dual pricing in Russia allegedly constitutes a WTO-inconsistent subsidy is the lack of specificity. Under the ASCM, a specific actionable subsidy can be provided in a *de jure* (such as through a legislative or regulative act) or *de facto* form (such as an actually specific subsidy). Regarding the latter form, the ASCM Article 2.1 (c) reads: “[i]f, notwithstanding any appearance of non-specificity. . . there are reasons to believe that the subsidy may in fact be specific, other factors may be considered.”⁹⁰ According to the ASCM, these factors include: (1) the use of a subsidy program by a limited number of certain enterprises; (2) predominant use of a subsidy by certain enterprises; (3) the granting of disproportionately large amounts of subsidy to certain enterprises; and (4) the manner in which discretion has been exercised by the granting authority in the decision to grant the subsidy.⁹¹ The most likely cases when gas dual pricing could constitute a *de facto* specific actionable subsidy in Russia would be either where a government deliberately provides a disguised advantage to certain energy-intensive enterprises or industries, or if there is only one or a few predominant users of a gas input within Russia. However, so far, neither these two cases of *de facto* specificity, nor the case of a *de jure* specific subsidy have been proven to exist. In Russia, there

⁸⁷ See *United States – Final Countervailing Duty Determination with respect to certain Softwood Lumber from Canada*, Appellate Body Report, WT/DS257/AB/R, adopted 17 February 2004.

⁸⁸ See The Energy Charter Secretariat, *Putting a Price on Energy: International Pricing Mechanisms for Oil and Gas* (The Energy Charter Secretariat, 2007).

⁸⁹ *US-Softwood Lumber IV*, AB Report, *supra* note 87.

⁹⁰ ASCM Article 2.1 (c).

⁹¹ *Id.*

is no discrimination regarding the access to energy inputs at reduced domestic rates between foreign and Russian companies, which equally benefit from national dual pricing policy.⁹² Consequently, gas dual pricing in Russia appears to be in line with the ASCM.

C. Anti-Dumping Rules

Regardless of whether gas dual pricing is considered to be consistent with WTO rules, or not, the EU Commission has regarded it as a trade distortive practice, affecting the competition on the EU market between gas-intensive products from Russia and local producers, and allegedly resulting in input dumping. Taking this position, the EU Commission has levied anti-dumping duties on imports of energy-intensive products from Russia (such as petrochemical products and steel) to offset the effect of gas dual pricing in Russia on their prices on the EU market. These measures have been based on the adjustment to the Russian exporters' gas costs by using the so-called "market price" in a range of surrogate countries, including the EU itself. Because of essential economic differences between the surrogate countries and Russia, such practices have systematically yielded the determination of high dumping margins and consequent losses for Russian economy, estimated in hundreds of millions Euro annually.⁹³

In legal terms, input dumping refers to a situation where inputs, including gas inputs, used in manufacturing an exported product, are purchased internationally or domestically at dumped or below-cost prices, regardless of whether the end product is exported at dumped prices or not.⁹⁴ In the context of gas dual pricing, the discipline of input dumping overlaps with the discipline of subsidies, which allows analyzing dual pricing from both perspectives and apply to a product either an anti-dumping or an anti-subsidy remedy. In the WTO, the concept of dumping and anti-

⁹² For details, see Selivanova, *supra* note 67.

⁹³ See V. Pogoretsky, *The System of Energy Dual Pricing in Russia and Ukraine: The Consistency of the Energy Dual Pricing System with the WTO Agreement on Anti-dumping*, 4 (10) *Global Trade and Customs Journal* (2009), 313.

⁹⁴ *Id.*

dumping rules are covered by the Agreement on Anti-Dumping (ADA).⁹⁵ In the ADA, dumping is defined as the introduction of a product into the commerce of another country at less than its normal value (such as the price of a product in the exporter country in the ordinary course of trade).⁹⁶ However, if the investigating authority has grounds to believe that the price of a product in the exporter country was formed not in the ordinary course of trade (such as if it was affected by the government's intervention or gas inputs were sold below costs or a market price),⁹⁷ then it can refer only to the following two alternative solutions for determining the product's normal value.⁹⁸ According to the ADA Article 2.2, in this case dumping must be determined either by comparison with a comparable price of the like product when exported to an appropriate third country, provided that this price is representative; or with the production costs in the country of origin (such as Russia) plus a reasonable amount for selling, general, and administrative costs and for profits (such as the method of "constructed normal value").⁹⁹

Despite the above strict rules and the exhaustive benchmarks provided by the ADA for determining dumping, the EU Commission in the case of imports from Russia of energy-intensive products has regularly referred to the so-called "non-market economy" technique, which is allowed under Article 2.7 of the Council Regulation (EC) No. 384/96 and appears to be based on Article 2.7 of the ADA. The latter provision provides that the rules of the ADA Article 2 (such as a Determination of Dumping) are without prejudice to the Ad Note to the GATT Article VI, which, in its turn, sets out that in the case of imports from a country that has a complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the state, the importing Members in the determination of dumping may deviate from a strict comparison with domestic prices. The EU Commission has regarded the

⁹⁵ *Anti-Dumping Agreement*, available at: http://www.wto.org/english/docs_e/legal_e/legal_e.htm [hereinafter *ADA*].

⁹⁶ *ADA* Article 2.

⁹⁷ In light of the ADA, the concept "in the ordinary course of trade" has a broad meaning relying primarily on the discretion of the WTO Members' investigating authorities. Such a situation implies that dual pricing and input dumping can technically be regarded as practices not reflecting the ordinary course of trade.

⁹⁸ For details, see Pogoretsky, *supra* note 93.

⁹⁹ *ADA* Article 2.

above provision as that referring to a non-market economy environment where domestic energy prices cannot represent the normal value of a product and therefore must be disregarded for the purposes of dumping determination. On the basis of the above rules, the EU Commission has substituted gas costs of Russian exporters for an average price of Russian gas when sold for export at the German/Czech border (such as the Waidhaus hub), net of transport costs (such as a surrogate country method).¹⁰⁰ This has led to a systematic finding of dumping in the EU anti-dumping investigations against imports of energy-intensive products from Russia, due to a significant difference between gas prices in Russia and at the Waidhaus hub.¹⁰¹

The “non-market economy” anti-dumping methodology of the EU Commission has faced a lot of criticism in developing energy-endowed countries, which believe that this approach encroaches on their permanent sovereignty over domestic natural resources and is not in line with the ADA requirements. This appears to be true. The Ad Note to the GATT Article VI is outdated and cannot disable anymore the requirements of the ADA that only two possible benchmarks are used for the determination of dumping, excluding the “surrogate technique” applied by the EU Commission from the permitted anti-dumping instruments. It has to be recalled that this provision was introduced in the mid-fifties of the XXth century to integrate the so-called “state-trading countries” into the GATT market economy system.¹⁰² Currently, it is hardly possible to find any country that has complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the state, with few exceptions of self-isolated states, such as North Korea. In addition, as far as Russia is concerned, the EU has recognized it as a market economy, which makes it politically inconsistent and WTO-illegal for the EU

¹⁰⁰ Pogoretsky, *supra* note 93.

¹⁰¹ See the discussion of the EU anti-dumping investigations against imports of energy-intensive products from Russia in Pogoretsky, *supra* note 93.

¹⁰² A. Polouektov, *Non-Market Economy Issues in the WTO Anti-Dumping Law and Accession Negotiations: Revival of a Two-tier Membership?* 36 (1) *Journal of World Trade* (2002), 1.

institutions to impose on Russian exporters of energy-intensive products anti-dumping duties based on a non-market economy methodology.¹⁰³

V. Conclusion

This paper has analyzed the political and legal tensions that exist between the contradictory principles of trade liberalization and PSNR in the context of the Russia-EU energy relationship. Whereas the principle of trade liberalization envisages a free or fully liberalized trade regime where prices are the reflection of true supply and demand and are the sole determinant of resources allocation, the principle of resource sovereignty allows every state to exercise control over the disposition of its natural resources exploitation even if it is based on the government-control measures. This inherent conflict involves different agendas, related to environment and climate change, energy security, power politics, economic development, and trade in energy-intensive products. In light of Russia-EU relations, the key issue appears to be a co-dependent reliance on Russia's natural gas supply, which in economic terms feeds the EU industrial sector, but at the same time distorts trade by providing cheap energy inputs in Russia that increase the competitiveness of Russian producers of energy-intensive products vis-à-vis their EU competitors. This issue emphasizes the contradiction between the principles of trade liberalization and resources sovereignty, and demonstrates its critical relevance to the WTO agenda.

In the bilateral negotiations between Russia and the EU on the accession of Russia to the WTO, the EU has pushed for the liberalization of Russia's domestic energy market and relaxing government control over natural resources. Through such an external policy, the EU has for many years attempted to export its domestic energy *aquis* and energy governance principles to neighbours and major trading partners. Russia, however, has opposed these endeavours, regarding national energy strategy as a tool for boosting its economic development and regaining the title as a global superpower. In its WTO accession bid, Russia has taken the view that its national energy policy is fully consistent with WTO rules. Therefore, it has been

¹⁰³ See Pogoretsky, *supra* note 93.

reluctant to accept any 'WTO-plus' commitments contradicting its national energy strategy.

In international law terms, the Russia-EU relationship provides an illustrative example of how the general principle of PSNR – the legal basis for resource sovereignty – interacts with WTO treaty law. The key task of this paper was to explore this interaction and to see whether the *lex specialis* of WTO law precludes the application of the *lex generalis* principle of PSNR. To explore this interaction, gas dual pricing in Russia was chosen as an illustrative example. Although the Russian government has recently decided to gradually converge Russian domestic and export gas prices by 2014, the relevance of this analysis will not be undermined because energy dual pricing remains a domestic policy choice of many energy-endowed Members of the WTO.

The analysis in this paper shows that in the context of gas dual pricing, there are no WTO rules that would be violated if Russia were to become a WTO Member. While the overarching concepts that guide global free trade (transnational trade liberalization) and natural resources exploitation (PSNR) are contradictory in nature, the specific rules of the WTO are likely to only place limited restrictions on the sovereign state's natural resources exploitation decisions. Even though Gazprom appears to fall under the definition of an STE, its practice to price gas differently for domestic and different categories of foreign consumers does not constitute discrimination within the meaning of the GATT. Regarding the ASCM rules, Russia's gas dual pricing is not a prohibited subsidy, since it is neither tied to export performance, nor is it contingent on a local content requirement. It does not amount to an actionable subsidy because of its lack of specificity. From the ADA perspective, it is the EU that appears to fall afoul of WTO law by resorting to anti-dumping methods not allowed under the ADA. Although, in general, dual pricing can be regarded as input dumping in the sense of WTO anti-dumping rules, the ADA does not provide effective instruments to tackle it.

The above findings indicate that WTO law does not contract out of the principle of PSNR and, therefore, both rules do not exclude each other. In fact, the WTO legal framework appears to be designed in such a way that it takes a neutral position with regard to the states' sovereign right to explore and exploit their natural

resources. Nevertheless, while the basic legal principles of the WTO do not extend to the domain of natural resources governance, the neutrality of WTO law does not contribute to resolving or alleviating the inherent tension between the principles of trade liberalization and resources sovereignty. In the era of energy-dependency, this tension will continue to have relevance as resource-endowed states seek to maximize benefit from their resource endowment. However, one positive aspect to this debate relates to the nature of the global economy: resource-endowed states can only benefit from their resource endowment if they participate in global trade and commerce. While the principle of PSNR permits states to control their natural resources, governance of natural resources also requires global rules that permit the efficient trade in these resources and resources-intensive products. Without markets to sell one's resources/resources-intensive products, the principle of PSNR has little meaning in terms of economic development. Therefore, as the world moves through the twenty-first century, the global governance of energy will become more, not less, important as both resource-exporting and resource-importing states struggle to derive economic benefits by balancing principles of resource sovereignty with those of trade liberalization.