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COMMUNICATION FROM THE COMMISSION

The European Union and Russia: the future relationship

The European Union and Russia: the future relationship

Commission Communication

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Accompanying document: draft Common Position on European Union-Russia relations

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The European Union and Russia: the future relationship

Commission Communication

Introduction

1.1. The ties that bind Russia and the countries of the European Union are centuries old. In matters political, cultural and commercial, the history of Russia is closely intertwined with that of her European partners. Cooperation has been a fact long taken for granted, yet it has never been fully exploited, for reasons essentially linked to the gulf that, in Soviet times, divided the Western democracies from a totalitarian state.

1.2. In the short space of a decade, Russia has undergone a far-reaching process of economic and political transformation. Reforms have been put in place, though their integration and acceptance into post-Soviet society present considerable challenges. It will take many years for Russia to overcome the Soviet legacy, and no certain prediction can be made about the road Russia will follow towards political and economic reform. The key question is whether she turns inward upon herself, seeking to implement reform and develop her economy with limited input of foreign expertise and investment, or whether she takes her place in the world economy in full and responsible partnership with the European Union and others.

1.3. For the European Union, the relationship with Russia is of high significance, because:

(i) Russia is a key player on the world scene, being permanent member of the UN Security Council and nuclear power;

(ii) In addition Russia is a key contributor to stability on the European continent as a whole;

(iii) Russia represents a considerable economic, commercial and scientific potential;

(iv) Moreover, the European Union is today Russia's main trading partner and, with Finland's accession, immediate neighbour.

1.4. It is time that the European Union and Russia recognized their historical vocation

as the two principal European powers and, in the common interest, sought to develop the close and mutually enriching partnership which will reflect their political, social and economic significance, while at the same time demonstrating the responsiveness and respect for human rights without which cooperation will remain unfulfilled and void of substance.

In this context the recent events in Chechnya have placed a considerable burden on current relations which are being hampered by Russia's insufficient fulfilment of frequently discussed conditions seeking to remedy the situation.

1.5. This Communication, which was announced at the informal meeting of European Union Foreign Ministers in Carcassonne on 18-19 March, develops a strategy governing European Union/Russia relations for the coming years. Realization of this strategy must be achieved in joint endeavour with Russia and in close cooperation with the European Union's principal partners, particularly the transatlantic partners, on the basis of the following objectives:

- the reinforcement of political, social and economic stability in Russia and the countries of the region;
- sustained development leading to improved living standards for the population of Russia;
- enhanced cooperation in addressing the major regional and global issues of concern.

In this respect the European Union recognizes the territorial integrity of the Russian Federation while supporting its development as a state where minority rights are respected in accordance with internationally recognized principles.

The Communication proposes the adoption of a Common Position (see attached document) on relations between the European Union and Russia.

Russia: the present situation

2.1. The process of change in Russia over the past decade has been fundamental, but a sustainable equilibrium has not yet been achieved.

2.1.1. On the political side, democratic institutions are being built up, but these are fragile and the rule of law is often uncertain; indeed, a tradition of authoritarian, secretive rule reminiscent of earlier times seems to have gained ground in recent months. The construction of a civic society has begun, but still has far to go as a vital basis necessary for the success of political democracy. The military continues, as in Soviet times, to be of major importance to Russia's political life and absorbs economic resources out of proportion to what Russia can currently afford (an estimated 20-25% of the 1995 budget). Organized crime and corruption are rampant, and indeed could undermine democracy and economic development if not dealt with effectively.

As a heritage of the Soviet empire, some 25 million people of Russian origin live outside the borders of Russia - a highly sensitive aspect of Russian foreign policy - and some 150 ethnic groups live within Russia's borders. Central government had made progress in improving relations with the diverse peoples of the Russian Federation, but its actions in Chechnya have been a serious setback to prospects of the Federation's managing its

regional and ethnic diversity in a democratic and civilized way.

Against that background there are some positive elements. The menace of nuclear confrontation has been removed, even though tens of thousands of nuclear weapons still remain, often in uncertain conditions of safety and storage, posing the threat of nuclear dissemination which would be difficult to control. Political debate is open and lively, and an independent press freely criticises government policies. Russian public opinion, now able to inform and express itself, is a new and important factor in Russian politics.

2.1.2. The Russian economy remains in a precarious situation. The new Russia inherited from the Soviet Union a decrepit industrial base that has wasted resources and produced a string of environmental disasters, and a heavily subsidised and startlingly inefficient agricultural system that has failed to meet basic needs. Almost three years after the onset of reforms, progress has been achieved in many areas of structural reform, including price liberalisation, sustained currency convertibility and privatisation.

These reforms have changed the economic environment. Market forces are playing a key role in significant parts of economic life. The underdeveloped services sector is expanding at a rapid pace, which is positive, even if the explosive growth in areas such as banking causes concern in view of a lack of regulation and prudential supervision. On the other hand, the manufacturing sector has contracted sharply, which causes serious social dislocation, but is also an inevitable correction of Russia's bias towards heavy industry.

Yet, for three years, macroeconomic stabilization has proved elusive. Inflation has remained much too high, fuelled by an excessive budget deficit which in turn was caused by a collapse in tax revenues and strong spending pressures. Several attempts at stabilization failed in a fragmented and divided policy-making environment with many competing centres of power. This has led to repeated policy reversals, and to the granting of costly privileges to sectoral or regional lobbies.

The high level of capital flight is evidence of the low level of confidence that Russian economic operators have in their own economy and indeed in the economic reform process. Foreign investors can scarcely be expected to enter where Russian investors themselves fear to tread.

The immediate and overriding economic policy priority is to end inflation. A virtuous circle must be launched, of restored confidence, a return of flight capital, investment and restructuring. The recent stabilization programme, supported for the first time by an IMF stand-by arrangement, provides a serious chance to achieve this. Yet it will be a formidable challenge for the government to remain united and committed to this programme as its initial contractionary effects will begin to be felt especially in the run-up to the end-1995 and mid-1996 elections. (See also Annex A)

European Union/Russia: the current state of the relationship

3.1. To date, the European Union has sought to develop its relationship with Russia through a wide variety of linkages, instruments and programmes:

Contractual links

The 1989 Trade and Cooperation Agreement with the USSR, offering MFN treatment for tariffs and duties and dialogue through a Joint Committee, still constitutes the formal framework for European Community/Russia relations. The Partnership and Cooperation Agreement signed at Corfu in June 1994 ("the PCA") is much more ambitious in scope, covering a wide range of European Community/Russia trade, commercial and economic relations, instituting political dialogue at various levels up to that of Heads of Government, and placing respect for human rights and the democratic process at the centre of the relationship. The human rights clause, to be found in both the Interim Agreement and the PCA, is an important instrument. It serves as a reminder of the fundamentals on which the relationship between the European Union and Russia is built, and, if necessary, enables either party to enforce those principles. Pending ratification of the PCA by the European Parliament and the national parliaments of the Member States - a process now delayed because of the events in Chechnya - it is intended that an Interim Agreement would bring the trade provisions of the PCA into force. Signature of the Interim Agreement is now also postponed, again in view of the human rights situation in Chechnya.

Further progress with respect to the signing of the Interim Agreement has been made conditional on sufficient fulfilment of a number of criteria: conclusion of a cease-fire, progress towards a political solution, unhindered access for humanitarian assistance and establishment of an OSCE assistance group in Chechnya.

De facto, even though the contractual framework constituted by the PCA is lacking, the political dialogue has been sustained, from the time of the signature of the Political Declaration signed by the Presidents of Russia, the European Council and the European Commission at Brussels in December 1993. This looked forward to establishment of "a permanent political dialogue and a system of regular consultations at different levels on the whole spectrum of political, economic and other issues of mutual interest".

Trade and commerce

In the economic field, the European Community has become by far the largest trading partner of Russia, accounting, in the first half of 1994, for 37% of the total of Russia's foreign trade, as compared with 24% for trade with the other CIS states, 6% for trade with China, 4% for trade with the USA and 3% for trade with Japan. In 1993 exports from Russia to the European Community reached 15.5 billion ECU and imports rose to 11.5 billion ECU, leaving a balance in Russia's favour of almost 4 billion ECU. However there is concern over the low level of the European Community's tariffs on imports from Russia (average weighted tariff of less than 1 %) as against the continued increase in tariffs imposed on Russia's imports from the European Community (average weighted tariff currently estimated at more than 18 %). As the majority of this trade balance is energy related, the European Community is already encouraging Russia to implement the European Energy Charter Treaty, its purpose being to create a legally binding framework to foster trade and to encourage foreign investment in the energy sector.

The inflow of foreign investment continues to be low (around one billion US Dollars per annum) in relation to Russia's size and potential.

A number of trade issues and commercial issues between the European Community and Russia are currently outstanding. These include: anti-dumping, where a systematic dialogue between experts has been initiated; procedures for testing and certification, where a task force has been set up to propose solutions to problems resulting from excessive Russian requirements for testing and certification procedures; the effects of enlargement, where the Russian side takes a positive view in principle of the present and future European Union enlargement but seeks to alleviate as much as possible the negative consequences on their exports to the new Member States; trade in nuclear products, although the conclusion of the Energy Charter Treaty in Lisbon on 17 December 1994 has contributed to solve a long-standing dispute between Russia and the European Community over the role of the Supply Agency and the interpretation of the Euratom Treaty as regards nuclear trade; Siberia over-flying rights.

Other forms of cooperation

European Community/Russia cooperation has been built up through the implementation of numerous actions and programmes, including Tacis, Pan-European networks in the fields of transport, energy and telecommunications and on other issues, including education and training, the environment, energy, humanitarian assistance, industrial cooperation, research and development, as summarized in Annex B.

European Union/Russia relations: further considerations

Looking to future European Union/Russia relations, a number of considerations should be borne in mind:

4.1. Given the uncertainty of predicting, with any degree of reliability, even the mid-term fortunes of a country such as Russia, it is difficult to define with confidence the European Union's medium-term strategy towards this country. An important factor will be the identity and persuasion of Russia's government and president after the next elections. Making due allowance for the weakness of Russia's democratic structures, it seems likely that the tensions will remain between governance in Russia and observance of human rights, between the centre and the regions, between maintenance of political control and the growth of criminality.

4.2. In the security, political and economic contexts, this implies an intensification of effort on the part of the European Union in order to take greater account of the specificities of the European Union/Russia relationship, and to ensure that the Russian government and public opinion give due weight to Russia's relationship with the European Union.

4.2.1. Security

It is important that the European Union's economic strategy towards Russia be coordinated with a political strategy that takes account of Russian security interests.

Now that NATO enlargement in favour of Central and East European countries is clearly envisaged, it is necessary to take account of the concerns of the Russian government. If

NATO enlargement, however, were to lead to Russia's standing opposition and, ultimately, to a build-up of her military capabilities, the aim of greater European Union stability would clearly not be achieved. There is accordingly a need to intensify the dialogue concerning the development of Europe's future security architecture, comprising such aspects as NATO enlargement, Partnership for Peace, OSCE strengthening and the development of relations between Russia and the Western European Union.

The OSCE continues to establish itself as an important organ of European security. Its comprehensive approach to security, broad membership and high standards make it the appropriate forum for managing change and preventing the reemergence of new divisions. The ongoing discussions on the "security model" are based on this comprehensive definition of security. The European Union should continue to work to strengthen the OSCE framework in which the rôle of Russia in European security is recognized.

4.2.2. Political

It seems likely that, in the coming months, the European Union's political relationship with Russia will be overshadowed by the tragedy of Chechnya, just as Russia's political scene is likely to be dominated by Chechnya in the run-up to two crucial events: the legislative elections in December 1995 and the presidential elections in June 1996. During this period the European Union must strike a balance between giving expression to its concern over Russia's breach of human rights in Chechnya, and the need to facilitate the process of reform in Russia.

In order to be able to raise issues of political concern in a timely fashion and in a manner which will have due influence, European Union-Russia relations will be best served by consolidation of the political dialogue. There is a need for the European Union to strengthen its ties with a much wider range of Russian leaders, opinion formers and institutions both inside and outside government, both at the centre and in the regions of Russia, and to involve a greater number of European Union and national institutions. The European Parliament has a special rôle to play, to build up contact with both the Duma and the Federal Chamber, and thus to deepen the relationship with national and regional politicians.

The issue of ethnic Russians living outside the borders of the Russian Federation is a deeply sensitive matter for Russian public opinion, and one which is easily played upon by nationalist politicians. Here the European Union can play a moderating role in the resolution of conflict through the exercise of its political influence, as it has in the area of Russia-Baltic State relations through its promotion of the Stability Pact, and as it continues to do through its declarations and démarches, based on close monitoring of the situation. Direct support might also be provided by the European Community and the Member States, for example through the financing of language-training to encourage integration and the acquisition of nationality.

The advance towards further European Union enlargement will prompt, with increasing urgency in the coming years, questions over the weight and content of the European Union's relationship with all the CIS countries, and particularly Russia. As the effects

of the process leading to enlargement begin to be felt by the Central and East European countries, it may be expected that the CIS countries will, for their part, intensify their search for closer links with the European Union. Since accession is not, in the European Union's view, an option for those countries, the network of Partnership and Cooperation Agreements (currently signed with Belarus, Kazakhstan, Kyrgyzstan, Moldova, Russia and Ukraine) must provide the framework which will allow the bridging of the political and economic gap between those countries acceding to the European Union and their neighbours to the East. Participation in a wider European zone of prosperity can also be encouraged through regional organisations such as the Baltic and Barents Sea regional bodies.

4.2.3. Economic

4.2.3.1. European Union-Russia economic relations:

The potential for the future growth of European Community/Russia economic relations is great. To realize that potential will require the building up of strong mutual confidence, so that investment of money and effort in the Russian economy can be seen by both European Community and Russian business partners to be worthwhile. Industrial cooperation between the European Community and Russia will be increasingly important to support the micro-economic pillar of reform. Russia will have to increase its efforts to provide stable, transparent and predictable framework conditions for foreign direct investors. The Tacis programme facilitates the development of industrial cooperation through its contribution to enterprise privatisation, restructuring and modernisation in Russia.

Both for Russia and the European Community, the PCA, once ratified, will be the framework within which mutual confidence will be nurtured. As trade grows and diversifies from its present narrow base, it is inevitable that differences will arise in the way issues are perceived. It will be necessary for both parties to make full use of the provisions of the Interim Agreement and the PCA to ensure that problems are addressed promptly, in ways which meet the interests of the European Community and Russian economies.

It is worth noting that the two parties to the PCA are due to hold a joint examination in 1998, to see whether circumstances allow for the beginning of negotiations on the establishment of a free trade area.

As bilateral trade builds up between the European Community on the one side and the Central and East European countries and the CIS countries on the other, it will be important not to lose sight of the trade potential that exists between the CIS countries themselves, and between them and the Central and East European countries. It will be in the European Union's interest to encourage the resumption, in a manner appropriate to a market economy, of those links ruptured when the Soviet Union collapsed, in particular through encouragement of regional and cross-border cooperation.

4.2.3.2. Russia's participation in the global economic system:

As regards the institutional framework regulating Russia's international trade links, the main challenge facing Russia in the short to medium term is its accession to the WTO, a process which is still in its early stages. The European Community has started a systematic dialogue with the Russian side to prepare the accession negotiations, which will offer an additional opportunity to remove barriers limiting the access of European Community goods and services to the Russian market. It is politically committed to the process, both as a means of firmly integrating Russia into the world trading system and because accession to the WTO will further underpin the domestic reform process. Nonetheless, it has to be recognized that the path to membership may be difficult at times. A rapid accession may imply Russia being asked to undertake a large number of specific obligations as part of the accession package. Over time, and as the reform process matures, the need for such specific disciplines will diminish.

Russia has a cooperation agreement with the OECD, which through its expertise in economic and trade matters can do useful work in helping Russia insert itself into the world economic system. Full membership could be envisaged once Russia has completed the process of accession to the WTO.

The G7 has been an important forum for discussing Western economic policy towards Russia. It has played a useful role, particularly in strengthening coordination between bilateral and multilateral donors, especially since the Tokyo Summit. Russia has expressed keen interest in taking an increasing part in G7 economic activity. This will however be dependent on Russia's achievement in the development of a market economy.

The European Union's objectives and priorities for the future European Union/Russia relationship

5.1. There is consensus, as was demonstrated at the informal meeting of the Foreign Ministers of the European Union at Carcassonne, that, in the interest of the European continent as a whole, the European Union must conduct its relations vis-à-vis Russia so as to contribute to its evolution as a democratic and progressive nation.

To this end, in joint endeavour with Russia and in close cooperation with its principal world partners, particularly the transatlantic partners, the European Union should work towards achievement of the following interrelated objectives:

- reinforcement of political, social and economic stability in the Russian Federation and the countries of the region;
- sustained development leading to improved living standards for the population of the Russian Federation;
- enhanced cooperation in addressing the major regional and global issues of concern.

These are objectives of which the European Union must not lose sight, in the face of shorter-term difficulties in the European Union-Russia relationship.

5.2. Certain priorities follow from the above objectives :

- the further involvement of the Russian Federation in the development of the European security architecture, the overriding aim being to avoid new divisions in Europe;
- the further development of democratic norms, institutions and practices, and the respect of human rights, individual liberties and the rule of law;
- further progress towards economic reform and encouragement of European Community/Russia economic interaction in order to ensure Russia's economic liberalisation and establishment of the market economy; and its growing participation in a wider European economic zone of prosperity, and the world economic system;
- the intensification of bilateral and multilateral cooperation in other fields, inter alia justice, home affairs and crime prevention, and crisis prevention and management.
- the extension of open and constructive dialogue at different levels and in various fora, covering all matters of common interest, in particular security, support for political and economic reform in the Russian Federation and the prevention and resolution of crises so that the views of the European Union and the Russian Federation are heard in time and at appropriate level; in this context, seek to develop the political dialogue with the Russian Federation, pursuant to the political declaration signed by the Presidents of Russia, the European Council and European Commission in Brussels on 9 December 1993.

5.3. A number of further steps are put forward as a means of implementing the above objectives and priorities in respect of European Union/Russia relations for the coming years.

5.3.1 Security

The European Union should deepen discussions with Russia concerning the development of Europe's future security architecture, comprising such questions as NATO enlargement, Partnership for Peace, OSCE strengthening and the development of relations between the Russian Federation and the Western European Union. Russian hesitations over ratifying START II and implementing the CFE Treaty, indeed any retreat from internationally agreed undertakings particularly in the field of disarmament, should be met with a firm response. Other actions in the security field include cooperation with Russia against nuclear smuggling, greater involvement of Russia in the multilateral regimes on nuclear, biological, chemical and ballistic proliferation, as well as its membership of the 'New Forum' (post-COCOM regime on export controls).

Following the discussions at Carcassonne the European Union should work towards intensification of the dialogue between Russia and NATO, notably in the context of the Partnership for Peace and the North Atlantic Cooperation Council. In this context it is worth examining further the idea of a specific arrangement between Russia and the Atlantic Alliance which would set up regular ad hoc procedures of consultation and dialogue.

5.3.2. Political

Because of the length of national ratification procedures, the Partnership and Cooperation Agreement could not, in the most optimistic of scenarios, come into force before 1997. The European Community's short term concern therefore limits itself to the question of the Interim Agreement and its signature. The purpose of the Interim Agreement is to bring into force the trade provisions of the PCA, in the absence of which the 1989 Agreement with the Soviet Union continues to apply. It is therefore of fundamental importance, as has been made clear on several occasions to the Russian authorities, that the conditions for signature of the Interim Agreement should be met; for this, responsibility rests squarely with the Russian Government.

However, in the meantime, the European Community could take the necessary procedural steps to ensure that the Interim Agreement can be signed promptly and the European and national Parliaments can at once take up formal debate on ratification of the PCA, once these conditions have been met.

In the context of support to the democratic process and the establishment of human rights in Russia, the European Commission will continue to refine the implementation of the Tacis Democracy Programme (amounting to 11 MECU for 1995, of which 55-60 % will be spent on actions in Russia). The programme is of particular importance in the lead up to the forthcoming parliamentary and presidential elections. In coordination with the Member States' own programmes, it will also support cooperation between Russian and European opinion-leaders, parliamentarians and representatives of governmental and non-governmental organizations, both at the centre and in the regions. Equally, new information actions will be implemented to ensure among Russian opinion-leaders and the public a deeper knowledge of the European Union's involvement and concerns.

The European Union has in the past supported Russian accession to the Council of Europe, though at a time and in accordance with criteria to be decided by the Council itself. The events of Chechnya have halted the accession procedure. The Council is already engaged in assisting Russia in order to improve mechanisms of democracy and human rights, in cooperation with the European Union. Once the Chechnya issue has been resolved, the European Union should again advocate Russia's accession.

5.3.3. Economic

As regards economic issues, Russia has adopted a positive attitude in principle to current and future European Union enlargement. For its part, the European Community should examine to what extent the increase of certain customs tariffs in the three new Member States reduces market access. This should be part of an overall analysis of trade issues including those arising from enlargement. One should also bear in mind that the European Community is concerned by a number of specific problems, notably the significant increase in tariff protection decided in 1994 and 1995 by Russia, the cost of which will have to be borne by European Community exporters, as well as by excessive Russian requirements in the field of testing and certification which hinder trade.

Should signature of the Interim Agreement be substantially delayed due to lack of progress on the criteria laid down by the European Union, consideration should be given to certain deadlines laid down in the PCA :

- the agreement to consider, in the course of 1996, the possibility of granting MFN treatment for mobile satellite services;
- negotiations on the stage-by-stage opening of inland waterways for international sea-river services should commence by the end of 1996;
- nuclear trade agreement: a specific nuclear trade agreement should be in place by 1 January 1997, the provisions of the 1989 Trade and Cooperation Agreement continuing to apply in the meantime.

The Commission will make specific proposals to the Council and the European Parliament to meet these contingencies in due time before expiry of the deadlines.

The new Tacis regulation should be adopted by the end of 1995, in order to give new impetus to the programme. For the future, the sectoral and regional priorities of the Tacis programme and types of project can be expected to evolve continuously, as experience accumulates and Russia's transition progresses. These developments cannot be identified in advance with any confidence, but certain trends can already be noted:

- The implantation of the private market economy has taken place relatively quickly, with large-scale privatisation. Particular attention must however be paid to the establishment of effective social policies mitigating the serious consequences of economic restructuring.
- There has been rapid emergence of new enterprises, notably in the banking services sector. In many sectors know-how is now required at a higher level of sophistication, for example that of financial markets. However the future development of the manufacturing sector continues to raise serious concern.
- Within the food and agricultural chain, food distribution has now much improved, but the restructuring of the former collective and state farms has hardly begun.
- A continuing priority must be the education and training systems and scientific research, which has been gravely weakened by the lack of budgetary resources. Also regarding the institutional basis for civic society and democracy there are major needs, which are now being identified more clearly.

Regionally, Tacis is progressively opening up annual programmes in different important regions and this approach should be confirmed. There are grounds also to facilitate the work of the Baltic and Barents Sea Regional organisations, and the development of certain Trans-European Networks.

Regarding types of project, the emphasis should continue to shift in favour of projects leading later to investment or actions that directly benefit Russian citizens, and away from surveys and studies that do not have lasting impact.

Through Tacis assistance the European Community will continue to support Russia in the area of economic policy advice, in harmony with the work of the IMF, the EBRD and the other International Financial Institutions.

The reinforcement of cooperation across the new common border between the European Union and Russia becomes a priority for Tacis, and will involve joint programming of the Tacis and INTERREG programmes, and the promotion of pilot projects for cooperation between local and regional authorities of the European Union within the framework of an ECOS-Tacis programme.

Monitoring and evaluation of Tacis projects will be reinforced with a view to improving project preparation in the future and, more immediately, to obtain value for money.

5.3.4. Other forms of cooperation

The European Community is continuing its cooperation in many sectors with Russia. Such forms of cooperation (inter alia, environmental protection and nuclear safety, development of human resources, information technology and telecommunications, transport, science and research) are of common interest to both parties. Telecommunications networks in particular serve as a vital underpinning of Russia's economic relations between the European Community and the rest of the world. Such cooperation should continue, as a clear signal of support for the ongoing political and economic reform process in Russia. Equally, fresh consideration should be given to the question of Russia's eventual access to certain of the European Community's financial instruments, particularly in the context of the Trans-European Networks.

Close cooperation between the European Community, the CIS states and Russia in particular on energy issues is of prime importance. The European Energy Charter Treaty is an important instrument in this respect; all opportunities to make use of Charter mechanisms, including resumption of negotiations for the so-called Second Stage of the Charter, should be fully utilized in order to ensure the rational and equitable exploitation of energy resources. To improve the flows of investment into the vital Russian energy sector, all efforts should be made by the European Community to arrive at liberal provisions on investment opportunities.

Equally there is a need for further cooperation between the European Community, the Central and East European countries and all the CIS countries, in order to combat the growing threat posed by nuclear trafficking and to pursue the fight against organised crime and drug smuggling. The European Community's own interests are also involved in working with Russia to improve her catastrophic environmental situation, thus to avert ecological threat in the event of military or civil accident, and to avoid spillover from internal strife and economic deprivation in the form of large-scale emigration.

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Accompanying document: draft Common Position on European Union-Russia relations

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Annex A: Economic situation and economic reform in Russia

Annex B: TACIS and other specific instruments

**Draft Common Position
on the objectives and priorities of the European Union
towards the Russian Federation**

The Commission, in forwarding to the Council the Communication on the European Union's relations with the Russian Federation, considers it necessary, in parallel, to propose that the Council adopt a Common Position by virtue of Article J.2 of the Treaty on European Union.

Common Position

defined by the Council on the basis of article J.2 of the Treaty on European Union on the objectives and priorities of the European Union towards the Russian Federation.

(95/...CFSP)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on European Union, and in particular article J.2. thereof,

SETS OUT THIS COMMON POSITION :

A. The European Union will pursue the following objectives and priorities in its relations with the Russian Federation :

I. Objectives

1. The European Union will continue to pursue the objective of deepening and expanding its relationship with the Russian Federation, with the aim to achieve partnership while respecting democratic principles and human rights;

2. In joint endeavour with the Russian Federation and in close cooperation with its principal partners, particularly the transatlantic partners, the European Union will work towards:

- reinforcement of political, social and economic stability in the Russian Federation and the countries of the region;
- sustained development leading to improved living standards for the population of the Russian Federation;
- enhanced cooperation in addressing the major regional and global issues of concern.

3. The European Union recognizes thereby the territorial integrity of the Russian Federation while supporting its development as a state where minority rights are respected in accordance with internationally recognized principles.

II. Priorities

The European Union lays down the following priorities and calls upon the Russian Federation to work closely with it to achieve their realization :

1. the further involvement of the Russian Federation in the development of the European security architecture, the overriding aim being to avoid new divisions in Europe;

To this end, it will seek to intensify the dialogue between Russia and NATO, notably in the context of Partnership for Peace and the North Atlantic Cooperation Council, and promote OSCE strengthening, and the development of relations between the Russian Federation and WEU; and contribute, in this context, to the further examination of the idea of a specific arrangement between the Russian Federation and the Atlantic Alliance which would set up regular ad hoc procedures of consultation and dialogue;

2. the further development of democratic norms, institutions and practices, and the respect of human rights, individual liberties and the rule of law;

To this end, it will

- support forms of cooperation at various levels between Russian and European opinion-leaders, parliamentarians and representatives of governmental and non-governmental organizations, both at the centre and in the regions;
- promote and encourage fulfilment of conditions that will allow the Russian Federation's accession to the Council of Europe;

3. further progress towards economic reform and encouragement of European Union/Russia economic interaction in order to ensure Russia's economic liberalisation and establishment of the market economy, while taking account of the need to mitigate the social consequences of economic reform; and its gradual participation into a wider European economic zone of prosperity, and the world economic system;

To this end, it will

- support the Russian Federation in the planning and implementation of its agreements with the IMF and the other international financial institutions; on the basis of its achievement in macro-economic stabilisation and economic reform reassess Russia's membership of international groupings such as G7;
- support the Russian Federation in its application for membership of organizations such as WTO;

4. the intensification of cooperation in other fields, inter alia the field of crisis prevention and management;

To this end, it will

- explore the possibility of a moderating rôle for the European Union in the resolution of regional conflicts within the framework of the Stability Pact;
- encourage regional cooperation between Russia and its neighbours, where each party freely recognises the mutual benefit of cooperation;
- try to develop further cooperation with the Russian Federation in matters such as the prevention of ecological disasters, and questions relating to migration, and the prevention of illegal activities, in particular the fight against organised crime, the illegal traffic of nuclear materials and drugs, illegal immigration and other offenses;
- ensure the supply of humanitarian assistance to the population in need through the specialist agencies where this is deemed necessary, in addition to Community operations in these areas.

5. the extension of open and constructive dialogue at different levels and in various fora, covering all matters of common interest, in particular security, European integration, support for political and economic reform in the Russian Federation and the prevention and resolution of crises so that the views of the European Union and the Russian Federation are heard in due time and at appropriate level; in this context, seek to develop the political dialogue with the Russian Federation, pursuant to the political declaration signed by the Presidents of Russia, the European Council and European Commission in Brussels on 9 December 1993.

B. The Member States shall ensure that their national policies shall conform to this common position.

C. THE COUNCIL notes that the Community on the basis of the Commission's initiatives will contribute to the above objectives and priorities in particular through :

1. the taking of all necessary steps to ensure, at such time as the criteria laid down by the European Union have been substantially fulfilled, the prompt signature of the Interim Agreement and early ratification of the Partnership and Cooperation Agreement signed at Corfu on 24 June 1994;
2. the pursuit of its dialogue with the Russian Federation concerning its application for membership of international organizations, including the current application to WTO;
3. implementation of programmes in support of the democratic process and establishment of human rights in the Russian Federation, on the basis of among others the EU's Democracy Programme and in cooperation with the relevant programmes of the Member States; and support other forms of cooperation at various levels between Russian and European opinion-leaders, parliamentarians and

representatives of governmental and non-governmental organizations, both at the centre and in the regions;

4. continuing to refine and develop its technical assistance programmes, while working towards more effective coordination between donor organisations implementing programmes with the Russian Federation, and in particular to ensure that the new TACIS regulation is adopted in due time, before the end of 1995;
5. working with the Russian Federation to promote European cooperation aimed at ensuring the rational and equitable exploitation of energy resources, within the framework of the European Energy Charter;
6. reconsidering the question of the Russian Federation's eventual access to certain of the European Union's financial instruments, particularly in the context of the Trans-European Networks;
7. continuing to provide humanitarian assistance where necessary;
8. continuing to cooperate with the Russian Federation in the fields of education and training, environmental protection and nuclear safety, industrial cooperation, information technology and telecommunications, transport, science and research;
9. implementation of new information actions to ensure among opinion-leaders and public in the Russian Federation a deeper knowledge of the European Union and its concerns;

THE COUNCIL will undertake the necessary measures to promote the above-mentioned objectives and priorities, where appropriate on the basis of Commission proposals.

C. This Common Position shall be published in the Official Journal.

Done at Brussels,

For the Council,

The President.

The European Union and Russia: the future relationship

Commission Communication

ANNEX A

Economic situation and economic reform in Russia

During the past three years Russia has undergone major economic changes. Yet it is far from certain that it has found a sustainable path to a market economy. Liberalization has been only partial, and restructuring has not really started in any coherent sense. The lack of a clear division of power among various decision-making centres has led on occasions to a reversal of the course of economic policy. The central authorities' grip on Russia's regions has also diminished. As a result, the country continues to be affected by serious tax revenue shortfalls and waves of excessive inflation. Its social and medical infrastructure has deteriorated, life expectancy has decreased, crime and corruption have reached alarming proportions, and there is disillusionment with reform. What is needed now is an effective macroeconomic stabilization package. Recent policy has made substantial progress in this direction, but the challenge is still formidable.

The fall in output came to an end in 1994. For the year as a whole GDP is estimated to have fallen by 15%, compared with a 12% drop in 1993. Five years of overall economic decline reduced industrial output below 45% of its 1991 level. However, in the last quarter of 1994 and in the first quarter of 1995 monthly GDP is reported to have stabilized, although it was still declining with respect to the corresponding periods of the previous year. Similarly, on a monthly basis industrial production has remained fairly stable since October 1994, which suggests that it may have bottomed out.

The consequences of the disorder affecting economic decision-making are quite clear if one looks at 1994. A relatively lax fiscal policy in the first quarter of the year was followed by an attempt to contain the budget deficit by sharp spending cuts, and to implement a restrictive monetary policy. As a result, inflation declined markedly, to below 5% per month in August. A renewed surge in government spending and higher money growth in the summer of 1994, led again to a sharp acceleration of inflation during the latter part of the year and the beginning of 1995. It was also a factor behind the sharp fall of the rouble in October 1994.

The current policy stance is again much more restrictive. Monetary policy has been tight since the last part of 1994, and the fiscal deficit for the first quarter of 1995 is estimated at about 2.4% of GDP, against more than 9% in the first quarter of 1994. This has not yet led to a concomitant decline in inflation, which signals that inflation expectations are still high and that the government's credibility has been damaged by its performance in recent years. Yet a considerable effort is currently being made. The budget for 1995, finally approved by the State Duma in mid-March, envisages a deficit reduction that will require major adjustments on both the revenue and the expenditure sides. This should lead to a very sharp fall of inflation, to 1% per month by the second half of 1995.

These measures form part of a wider-ranging economic policy package that should create the conditions for the recovery of the Russian economy. It also envisages substantial liberalization of the external trade regime, including the abolition of quantitative restrictions on imports and exports, the abolition of the system of special exporters for strategic goods, as well as the revision of access to oil pipelines. Tax revenue gained from abolishing tariff exemptions and privileges is among the principal means of reducing the budget deficit. The IMF has approved in April a stand-by arrangement for Russia amounting to SDR 43 billion, about \$ 6.5 billion.

On the external side, in 1994 Russia recorded a large trade surplus, estimated at \$19.8bn in 1994, compared with a surplus of about \$12bn in 1993. Preliminary estimates put the trade balance for the first two months of 1995 at \$2.9 billion. Those amounts, however, may be greatly over-estimated. Compliance of enterprises with reporting requirements is poor, and data are affected by a substantial degree of under-recording, especially for imports, in order to escape tax payments. In recent years trade and financial transactions have been diverted away from traditional partners - the former CMEA and, even more, former soviet republics - and flows have been redirected towards western markets. Industrialized countries accounted for 69% of total imports in 1994, compared to 60% in 1993, while imports from former CMEA countries continued to decline and accounted for less than 8.5%.

The external debt of Russia was estimated at \$85bn at the end of 1994. Slightly less than 90% of the total consists of debt contracted during the Soviet period, which was taken over by Russia in early 1993. Starting in 1991, the USSR and then Russia were no longer able to meet all their debt servicing obligations, and started to run up substantial arrears. Several temporary rescheduling agreements were reached with creditors, but these have now expired. Paris Club talks are about to restart, the IMF loan now being approved.

The mass privatization programme has been highly successful, at least when judged by its own terms. As a consequence of the first stage of privatization, over 15,000 large and medium-sized enterprises have been privatized since December 1992. The second stage of privatization began in mid-1994. This phase is based on sales of shares for cash. This impressive transfer of property rights to private agents did not coincide with substantial changes in the behaviour of enterprises. Governance is still inadequate, insiders dominate firms, and the budget constraint has not hardened enough. There is so far little evidence of enterprise restructuring, as testified, among other things, by the low rate of redundancies. There has been no attempt by the authorities to isolate 'bad' firms from viable ones, or to develop a strategy for dealing with the worst loss-makers.

Progress with the creation of a legislative and institutional framework for a market economy has been particularly slow and, on the whole, the legal and institutional framework remains woefully deficient. Much of the reform effort has been enacted by presidential decrees. Implementing legislation has often been lacking as Parliament disagreed with the measures, or simply failed to follow them up. The resulting body of legislation is neither transparent nor consistent. The long-lasting legal uncertainty, due to major gaps in the legislation and controversial interpretations of existing norms, as well as to the inability to enforce contractual obligations, heavily constrains economic activity and particularly foreign investments.

The European Union and Russia: the future relationship

Commission Communication

ANNEX B

Cooperation between the European Union and Russia

European Union-Russia cooperation has been built up through implementation of the Tacis programme and numerous other actions and programmes.

The Tacis Programme

Since its inception in 1991 Tacis has striven to provide know-how to create the means and conditions for accelerating the transition to a democratic market society. It has three main objectives : to support the transition towards the market economy and democracy, to develop partnerships and foster links and networks at all levels, and to integrate recipient countries into the world economy.

Tacis has as its priority the need to contribute to structural reform and modernisation in the areas which play a key role in the transition process. For this purpose, Tacis allocates grants to five basic project types: policy advice, institution-building and restructuring, design of legal and regulatory frameworks, training and pilot projects. Sectoral concentration is, wherever possible, combined with geographical concentration. South-West Russia and Kaliningrad in 1994, North-West Russia and Baikal in 1995. Tacis has concentrated on the following sectors: nuclear safety and energy (30 %); support for enterprises including privatisation, military conversion and the financial sector (17 %); and human resources development (training, public administration, social policies and civic society) (16 %). In addition Tacis has committed significant funds in such sectors as transport, telecommunications, agriculture and the environment. Tacis works at every level in society, demonstrating new ideas and alternative ways of organisation, providing policy advice, advisory and consultancy teams, training and studies, it helps to develop new regulatory frameworks, reformed institutions and NGOs, and setting up partnerships and networks, twinning, pilot projects and framework programmes. Mention should also be made of the Special Privatizations and Restructuring Programme decided at the Tokyo Summit.

Increasingly there is local participation in the design, procedures and implementation of Tacis projects. Local Coordinating Units, which are usually attached to a Minister with a seat in Cabinet, play a key role in identifying the priority needs of the partner countries, the priority sectors and geographical areas for assistance, and subsequently assessing and proposing activities to be funded under the annual Action Programmes. Considerable efforts have been made in view of giving more and better information on Tacis, in order

to improve awareness among the recipients and local populations, as well as within the EU, as to what Tacis is doing and how it operates.

In the past Tacis was criticised for the slow rate at which commitments and payments were made. The situation changed, thanks to the introduction of multi-annual programming and a concerted effort to eliminate the backlog of uncontracted projects built up in 1991 and 1992. The table below clearly indicates the progress achieved; the fact that the volume of Tacis projects started in 1994 exceeded the annual budget, demonstrates that Tacis is catching up past backlogs. Russia's annual share of the above total Tacis budget available for national programmes has on average been 60 % (1065 MECU since 1991).

Year	Budget	Contracts signed (MECU)	Payments made (MECU)
1991	396.5	5.3	0.4
1992	420.0	203.0	32.1
1993	475.0	348.0	180.3
1994	460.0	512.0	300.0
1995	506.85		

It is worth noting that staff levels for implementation of Tacis are far below those of other donor organizations.

During the informal meeting of Foreign Ministers at Carcassonne in March 1995, particular emphasis was laid on the importance of certain Tacis sectors, namely nuclear safety, the reinforcement of democracy and civil institutions, education and training programmes and policy advice. These areas in fact absorb a large share of the Tacis national budget for Russia even before taking into account the nuclear safety programme which should be more easily implemented now that the memorandum on nuclear liability has been agreed. Russia receives the largest share of funds allocated to the Nuclear Safety programme (some 65 % out of a total of 321 MECU) and a large share of the Inter-State Programmes (total 1992-1994: 200 MECU) and other non-national Tacis programmes.

Assistance in support of the development of the enterprise sector will continue to be necessary in Russia: the ability of the enterprise sector to develop successfully in the short to medium term is severely constrained by lack of effective financial intermediaries, insufficient management know-how, particularly as regards financial management, and lack of an adequate regulatory and accounting and auditing infrastructure. This "systemic" problem also discourages the inflows of foreign capital vital for growth prospects. There is therefore a continued important role for Tacis assistance, working in close cooperation with other donors, in helping to improve and develop the whole business system and institutions. In the short to medium term, particular attention also needs to be paid, through Tacis and other donor programmes, the establishment of effective social policies mitigating the serious consequences of economic restructuring.

The new Tacis regulation emphasises continuity and reform. While the transfer of Western know-how in support of the reform process should remain at the core of Tacis,

proposed innovations include limited support for investment, cross-border infrastructures, emphasis on the regions and multi-annual financial and sectoral programming.

Other actions and programmes

There are many other actions and programmes where the European Union cooperates with Russia, as outlined below:

Humanitarian assistance

Russia is eligible to receive support from the European Union's food aid and humanitarian assistance programmes, should the need arise. Particularly during the initial phase following the break-up of the Soviet Union, the European Union provided massive food aid in the form of grants and loans with the aim of cushioning the adverse effects of the economic decline on the Russian population: 353 MECU in the form of free food supplies and 999 MECU in the form of credit guarantees and loans for food and medical supplies. In addition the EU provided targeted humanitarian assistance through ECHO to particularly vulnerable parts of the population. In 1994 this totalled 9.16 MECU plus a small amount of a global programme was allocated to relieve the effects of the Chernobyl disaster. Equally the fighting in the Autonomous Republic of Chechnya created a massive humanitarian need for which the Commission's aid has been the largest single form of assistance. To date 20.31 MECU is being provided to those affected in the Northern Caucasus and it has been distributed as far as possible irrespective of political or ethnic considerations.

Customs cooperation

Russia currently benefits from a TACIS-financed programme by which the European Commission works with the State Customs Committee of the Russian Federation to upgrade the Russian customs administration.

Democracy Programme

The Democracy Programme, funded from Tacis so far as the CIS countries are concerned, is designed to develop democratic practice in three main fields: the acquisition of knowledge and techniques of parliamentary practice and organization by politicians and parliamentary staff, the strengthening of non-governmental organizations which can contribute to the promotion of a pluralist democratic society, and the transfer of expertise and skills relating to democratic practice and the rule of law to professional groups and associations. The Democracy Programme contributed to one of the first Common Actions implemented by the European Union following the entry into force of the Treaty on European Union, namely that relating to the observation of the 1993 elections in Russia.

Energy and Energy Charter

Since 1992 the European Union has been cooperating actively in the energy field with the Central and East European countries, and the countries of the CIS, including Russia. Cooperation has focussed on the promotion of energy technologies and energy saving, through programmes such as THERMIE and the funding, under the TACIS programme, of Energy Centres, three of which are in Russia (Moscow, St. Petersburg, Tyumen). The

Energy Charter Treaty, concluded at Lisbon in December 1994, sets the framework for long-term cooperation in the energy sector among the signatories, including the European Union and Russia. Subjects covered by the Charter include the transit of energy, transfer of energy-related technology, promotion of investments and removal of trade barriers.

In the energy sector, the SYNERGY programme is helping Russia to make more effective policy decisions, for example in the following areas: advice on energy legislation and regulation, with emphasis on the European Energy Charter; support for an ongoing dialogue between the EU and Russia on the social and economic regeneration of coal mining areas; fostering the development of sustainable institutions to improve energy efficiency.

Interregional Cooperation

In 1993, along the lines of the scheme to encourage cooperation between local and regional authorities of the European Union and those of Central and Eastern Europe, the Commission extended the ECOS-OUVERTURE cooperation programme to local and regional authorities of the CIS states. It will be proposing, within the framework of the Tacis Regulation, to render this type of cooperation more effective by allowing the financing of the CIS partners taking part.

Environment

Environmental issues assume increasing priority in European Union/Russia relations. So far three Environmental Centres for Administration and Technology (ECATs) have been or are being set up in Russia (Kaliningrad, Moscow and St.Petersburg), the aim of these LIFE-financed centres being to provide local government and industry with support in their efforts to find environmentally sound solutions to problems in their areas. The 1995 TACIS Action Programme gives special emphasis to the environmental dimension in the areas of regional concentration, notably in the Baikal area in 1995. The LIFE Programme supports sustainable development in the Baltic Sea region, through ECATs in St. Petersburg and Kaliningrad.

Nuclear safety

The European Union/Russia nuclear safety programme, funded by TACIS, focusses on four different but complementary topics: assistance on six nuclear sites, by which experience is transferred in the operation of nuclear plants; design safety, comprising safety studies relating to the appraisal, definition and remedial proposals for VVER, RBMK or fast breeder reactors; support to regulatory authorities for the development of a strong technical and legal basis in fields such as licensing, training and inspections; the waste and fuel cycle, providing advice on management of waste and matters such as the transport of fuel. A similar approach will apply to nuclear safeguards;

Human resources

The Trans-European cooperation scheme for higher education (TEMPUS), which is financed from TACIS, is designed to assist the Central and East European countries and

the CIS states to restructure their higher education systems. Extended for a second four-year term, it has been open to Russia since 1993 and is financed under the TACIS programme. From 1995, the Youth for Europe III programme finances youth exchanges and mobility schemes involving the European Union and third countries, including Russia. A meeting of the European Union and Russia Ministers of Education was held in September 1994, focussing on Russian educational reform and cooperation activities in the field of education and training.

Industrial Cooperation

The European Union is seeking to promote industrial cooperation with Russia through pilot projects and the provision of sectoral analysis. The pilot projects have aimed at building up common experience in the design and implementation of cooperation projects, particularly in the electrotechnical sector, and in the enhancement of Russian skills in developing cooperation proposals. Sectoral analysis has concentrated on, inter alia, steel, aluminium, the wood and paper industry, the aeronautics industry, textiles and automobiles.

Scientific Cooperation

The European Union also supports reform in Russia through its activities of international cooperation in the field of science and technology.

Urgent action has been taken in recent years: research projects with the participation of Russian researchers have been supported by programmes such as COPERNICUS (joint projects and scientific networks) and PECO (participation in specific programmes of the Framework Programme), and through the International Association for the Promotion of Cooperation with Scientists from NIS (INTAS) along the lines of a recent communication from the Commission to the Council (COM (95) 109). In all, more than 50 MECU has been committed during 1993-1994 for cooperation of this type.

These activities complement the initiatives undertaken by TACIS-funded action in support of the International Science and Technology Centre (ISTC), by which the European Union assists the conversion of military researchers to civil applications. Initiatives supported to date have aimed at giving assistance to a wide number of researchers in small/medium size projects.

In the coming years, priority will be given to research projects having high potential applications both for industry and the public domain, which are likely to create nuclei for a renewed and reinvigorated RTD culture.

Statistical Cooperation

Since 1992 many actions, organized by Eurostat together with the statistical offices of the Member States, have been implemented in the field of statistical cooperation. Such actions, funded by TACIS, include consultancy, seminars, publications, study visits and training courses and the supply of equipment.

Transport and Trans-European Networks (TENs)

In the transport field, the Union is very active in promoting the integration of transport networks between the Union and Russia in a Trans-European Network perspective. For road and rail transport, these cover important corridors such as that between Berlin and Moscow or between Helsinki-St. Petersburg-Moscow-Kiev (both identified as priorities by the Essen European Council), and the G-24 is coordinating international financial assistance to these corridors. In the ports sector, the Union is an active partner to regional bodies in the Black Sea and the Baltic Sea looking at ports developments in a regional context. Furthermore, TACIS has identified air transport and in particular Air Traffic Control as priority sectors within the transport sector, and has financed many large-scale projects in these fields.

Information Society

There are many other areas of activity where the European Union experience is assisting Russia to set aside its legacy of the past in order to develop its resources in a sustainable manner. Examples include the Information Society where the European Union is providing advice to the Russian government on draft laws in the information sector, notably as data protection and import/export of informational documents.