

South Stream: Business Deal of the Century or Lawsuit of the Century?



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Summary

Serbia has been a member of the Energy Community since 2006. The main goal of the Energy Community is to create an integrated gas and electricity market between the EU and the associated countries. Two years later Serbia and Russia concluded the Agreement on Cooperation in the Oil and Gas Sector, which, inter alia, envisages construction of the South Stream gas pipeline. Apart from Serbia, six EU member states also concluded international agreements with Russia on the construction of the South Stream gas pipeline. The European Commission and Secretariat of the Energy Community warned that bilateral international agreements signed between EU member states, Serbia and Russia are in breach of EU law and Energy Community regulations, which jeopardized the implementation of this significant project. In this paper the author will analyze whether and in which part the rules of the Energy Community and provisions of the agreement with Russia are incompatible, consequences of this conflict at the level of international law, legal system of the Energy Community and Serbian legal system, and possible solutions aimed at resolving the current situation. The author concludes that the key parts of the Agreement on Cooperation in the Oil and Gas Sector signed between Serbia and Russia are in conflict with the obligations Serbia has to fulfill as a member of the Energy Community.

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Picture 1: First welded pipes of the Pipeline between Šajkaš and Kovilj

1. Introduction

The cover photograph best illustrates the current situation in which the construction project for the South Stream gas pipeline is. Announced as one of the most significant construction projects which was supposed to supply extra quantities of Russian gas to the European Union, the South Stream project is threatening to turn into a major international dispute whose legal consequences will be dealt with by European courts and arbitrations for years or maybe decades. The way it happened and prospects for the implementation of this undoubtedly significant project are just some of the issues we will try to address in this paper.

The subject of this paper is limited to a legal analysis of the problem concerning the construction of the South Stream gas pipeline. We will see how the six EU member states and Serbia, being a member of the Energy Community, signed bilateral international treaties with Russia without taking into account that certain provisions of these agreements are incompatible with the regulations of their respective organizations. This paved the way for an international legal dispute between the European Union and Russia, which escalated due to deteriorating international situation caused by the Ukrainian crisis. Being stuck in a dispute between two global powers, Serbia found itself in an unenviable legal situation, pressed between conflicting obligations under the Energy Community Treaty and those under the international treaty with Russia.

In further sections of this paper we will try to use an analysis of all relevant facts and regulations so as to ascertain which issues caused a dispute between the European Union and Energy Community on the one side, and Russia on the other and how it happened, including the impact of this dispute on Serbia. Unfortunately, due to the limited scope, the analysis did not encompass economic or legal aspects of the South Stream project, in which many European companies participate along with the Russian Gazprom and where many huge problems and disputes may occur if the project fails. In the first chapter we will present provisions of the Energy Community Treaty, of which Serbia became a member in 2006. We will then present provisions of the Agreement on Cooperation in the Oil and Gas Sector, which is the legal basis of all economic and legal agreements about the construction of the section of the South Stream in Serbia. In the third chapter we will deal with the compatibility of obligations under of the above-mentioned international treaties so as to identify disputed issues. The fourth chapter will provide an analysis of the corresponding rules of public international law which may be of importance for resolving this legal rigmarole. We will also explain the constitutional framework for resolving incompatibilities between two international agreements within Serbian legal system. In the end, we will give certain recommendations for avoiding similar situations in the future.

2. Energy Community

2.1. Aims, tasks and principles

The foundation of the Energy Community is based on an international treaty between the European Community¹, on the one side, and Albania, Bulgaria², Bosnia and Herzegovina, Croatia³, Macedonia, Montenegro, Romania⁴, Serbia and the United Nations Interim Administration Mission in Kosovo pursuant to the United Nations Security Council Resolution 1244 (associated countries), on the other. The treaty was signed in Athens on 25 October, 2005.⁵ The Energy Community Treaty entered into force on 1 July 2006.⁶ Serbia ratified the Energy Community Treaty on 14 July 2006.⁷

The main goal of the Treaty is to establish an integrated natural gas and electricity market between the European Union and associated countries. This entails a unique regulatory framework which should, *inter alia*, enable a more steady gas supply by way of developing networks with Caspian, North African and Middle-Eastern gas reserves.

Title I of the Treaty contains the founding principles of the Community. Similarly to the Treaty on the European Union, the Energy Community Treaty prescribes the loyalty principle which means that contracting parties must take all necessary measures, both general and special, to ensure fulfillment of obligations under the Treaty. The contracting parties are also obliged to ensure that the Community's tasks are accomplished and to refrain from taking any steps which could jeopardize the attainment of the objectives stated in the Treaty.⁸ Any kind of discrimination within the scope of the treaty is strictly forbidden.⁹

2.2. Application of the EU acquis

The Treaty envisages implementation of the EU acquis in the fields of energy, environment protection, competition and renewable energy sources in the territories of the associated countries. In further text we will focus on the application of the EU acquis in the fields of energy and competition, since these two fields are important for the subject in question.

Regarding the gas sector, it entails the application of Directive 2003/55/EC of the European Parliament and the Council of June 26 2003, concerning common rules for internal market in natural gas.¹⁰ Deadline for the implementation of Directive 2003/55/EC was within 12 months of the entry into force of the Treaty and it expired on July 1, 2007.¹¹

Rules taken from the then Energy Community Treaty are applied in the field of competition. The following shall be incompatible with the proper functioning of the Treaty, insofar as they may affect trade of natural gas and electricity (Network Energy) between the contracting parties:

- all agreements between undertakings, decisions by associations of undertakings and concerted practices which have as their object or effect the prevention, restriction or distortion of competition;
- abuse by one or more undertakings of a dominant position in the market between the Contracting Parties as a whole or in a substantial part thereof;
- any public aid which distorts or threatens to distort competition by favoring certain undertakings or certain energy resources.¹²

It is prescribed that any practices contrary to the aforementioned provisions of the Energy Community Treaty shall be assessed on the basis of criteria arising from the application of the rules of Articles 101, 102 and 107 of the Treaty on the Functioning of the European Union.¹³ Associated countries shall ensure that as from six months following the date of entry into force of the Treaty on the Functioning of the European Union, the principles thereof referring to competition are applied on their public undertakings.¹⁴

Rules taken from *acquis communautaire* are part of the EU legal system and their legal effect is determined by the rules of this organization. Regarding the significant differences between the structures of the EU and the Energy Community, it is envisaged that the Energy Community can adopt measures to adapt the EU *acquis*, taking into account both the institutional framework of the Energy Community Treaty and the specific situation of each of the Contracting Parties.¹⁵

The Energy Community Treaty contains a special provision which regulates harmonization of the [Energy] Community law with future EU law. It is envisaged that the Energy Community may take measures to implement amendments to the *acquis communautaire* in line with the evolution of European Community law.¹⁶ By decision of the Ministerial Council of 8 December 2007, the Energy Community law incorporated Regulation (EC) N° 1775/2005 on conditions of access to the natural gas transmission networks. The deadline for the implementation of this Regulation expired on 31 December 2008.

On 13 July 2009 the European Union adopted the Third Energy package, which brought significant changes in the natural gas and electricity sectors. We will now state regulations pertaining to the natural gas sector: Directive 2009/73/EC of the European Parliament and of the Council concerning common rules for the internal market in natural gas, repealing Directive 2003/55/EC and repealing Regulation (EC) N° 715/2009 of the European Parliament and of the Council on conditions for access to the natural gas transmission networks, and repealing regulation (EC) N° 1775/2005. In view of the changes in the EU regulations, on 6 October 2011 in Chisinau the Ministerial Council of the Energy Community adopted a decision on the implementation of Directive 2009/73/EC and Regulation (EC) N° 715/2009.¹⁷ The aforementioned Directive 2009/73/EC and Regulation (EC) N° 715/2009 thus became integral parts of the Energy Community Treaty. The deadline for their implementation expires on 1 January 2015.

2.3. Establishing a common energy market

The Energy Community Treaty envisages the establishment of an internal energy market on the territories of the contracting parties, without customs duties, quantitative restrictions on the import or export of Network Energy or equivalent measures. Furthermore, customs duties of a fiscal nature and/or fiscal discrimination are also prohibited.¹⁸ Regarding the external energy trade policy it is envisaged that the Community may take measures necessary for the regulation of imports and exports of Network Energy to and from third countries with a view to ensuring equivalent access to and from third country markets in respect of basic environmental standards or to ensure the safe operation of the internal energy market.¹⁹

2.4. Institutions of the Energy Community

The Energy Community has a permanent institutional framework. Institutions of the Energy Community are the following:

- Ministerial Council,²⁰
- Permanent High Level Group,²¹
- Regulatory Board²² and
- Secretariat.²³

In performing their duties Institutions of the Community can adopt decisions or Recommendations. Decisions are legally binding in their entirety upon those to whom they addressed.²⁴ The Adhering Parties shall implement Decisions addressed to them in their domestic legal system within the period specified in the Decision.²⁵ Recommendations have no binding force, although the Adhering Parties are supposed to use their best endeavors to carry them out.²⁶

2.5. Dispute settlement

The Treaty contains provisions which regulate settlement of disputes between the Adhering Parties about failure to comply with obligations under the Treaty. Any Adhering Party, Secretariat or Regulatory Board may notify the Ministerial Council that an Adhering Party does not act in compliance with the obligations under the Treaty or that failed to implement addressed to them within the required period. Private bodies may approach the Secretariat with complaints an Adhering Party fails to comply with its obligations under the Treaty.²⁷ The Ministerial Council may determine the existence of a breach of obligations under the treaty and shall decide:

- by a simple majority, if the breach relates to the extension of the *acquis communautaire*;
- by a two-thirds majority, if the breach relates to the mechanism for operation of network energy markets;
- by unanimity, if the breach relates to the creation of a single energy market.²⁸

A Decision by the Ministerial Council is binding upon the party to which it is addressed and the party shall comply. If the party fails to comply, the Secretariat may launch proceedings against the Party concerned for disregarding a Decision by the Ministerial Council.

In the case of a serious or permanent breach of treaty obligations, the Treaty envisages possible suspension of certain rights of the party which concerned. Upon proposal of the Adhering Parties, Regulatory Board or the Secretariat, the Ministerial Council, acting by unanimity, may determine the existence of a serious and persistent breach by a Party of its obligations and may suspend certain rights deriving from application of the Treaty, including the suspension of voting rights and exclusion from meetings or mechanisms provided for in the Treaty.²⁹

2.6. Interpretation of the Treaty

Terms and concepts used in the Energy Community treaty and are derived from EU Law, shall be interpreted in conformity with the case law of the General Court and the Court of Justice of the EU. If no interpretation from the said courts is available, the Ministerial Council shall give guidance in interpreting provisions of the Treaty.³⁰

2.7. Relationship with previous international treaties

Finally, the relationship between the Energy Community Treaty and other treaties concluded by the Contracting Parties before signing this Treaty was defined. It is explicitly stated that the provisions of the treaty shall not affect the rights and obligations arising from earlier agreements signed by the Contracting Parties³¹. However, if such agreements are not compatible with the Treaty, the Contracting Parties shall take all appropriate measures to eliminate the incompatibilities established within one year after the date of entry into force of the Treaty. The aforementioned measures entail repealing of incompatible agreements.

3. Agreement on Cooperation in the Oil and Gas Sector between Serbia and the Russian Federation

The agreement between the Government of the Republic of Serbia and the Government of the Russian Federation on cooperation in the oil and gas sector (hereinafter the „Energy Agreement“) was signed on 25 January 2008 in Moscow. The National Assembly of Serbia ratified the agreement on 9 September 2008.³² The Agreement entered into force on 30 September 2008.

The purpose of the Agreement is defined in Article 1 and it entails mutual cooperation and assistance in planning, construction and operation of assets in the implementation of the following projects:

- development of the main gas pipeline from the Russian Federation via the Black Sea, the territories of third countries and the Republic of Serbia for transit and supply of natural gas to other countries of Europe (the South Stream gas pipeline),
- *Banatski Dvor* underground gas storage, and
- reconstruction and modernization of a processing facility, owned by
- “Naftna industrija Srbije -NIS” Joint-Stock Company.

For the purpose of the implementation of the South Stream project and Banatski Dvor underground gas storage construction appropriate companies in joint ownership shall be established. It is envisaged that participants in these companies shall be Joint-Stock Company Gazprom or its affiliates, from the side of the Russian Federation, and state-owned enterprise Srbijagas [JP Srbijagas] from the Serbian side, respectively. Infrastructure, production, other assets and other property constructed, modernized, or acquired by the joint companies during their economic activity within the projects in question constitute their property. It is explicitly stated that the property of the joint companies shall not be expropriated, nationalized or subjected to measures resulting in consequences equal to expropriation or nationalization.³³ Each of the joint companies shall have the following shares of the initial capital: the Russian participant shall have no less than 51% , and the Serbian participant shall have no less than 49%.³⁴

The agreement defines that the Serbian section of the South Stream gas pipeline shall have the annual transmission capacity no less than 10 billion cubic meters of natural gas. Gazprom and Srbijagas shall examine the possibility of increasing the supply volume of natural gas from Russia to Serbia, and the specific volumes, terms, conditions and timeframes of these supplies shall be prescribed in the relevant contracts.³⁵ Serbia shall guarantee full and unrestricted transit of gas through the gas pipeline in accordance with the relevant contracts.³⁶

The South Stream gas pipeline and the storage facility in Serbia shall be operated by the appropriate joint company which will be established for the implementation of these projects. Establishment of tariffs for services relating to transportation and pumping, storage and production of gas shall be within the exclusive competence of the aforementioned joint company. The Russian participants shall have exclusive rights to all capacities of the gas pipeline and the storage facility.³⁷

Apart from the conditions pertaining to the construction of the gas pipeline and the underground gas storage, the Agreement defines that the Serbian party shall sell 51% of the state share in the Oil Industry of Serbia Joint-Stock Company to the Russian Gazprom.³⁸ Simultaneously with the Energy Agreement, the Government of the Republic of Serbia and the Government of the Russian Federation signed a Protocol on basic conditions of buying 51% shares of the initial capital of Oil Industry of Serbia Joint-Stock Company, Novi Sad by Open Joint Stock Company Gazprom Neft [OAO Gazprom Neft] for 400 million euros.

The agreement envisages the most favorable tax regime for both Serbian and Russian companies participating in the projects undertaken. In that respect, the Serbian party shall insure that in case of changes in the legislation [of Serbia] which result in higher tax obligations for the companies participating in the project, their taxation shall be in accordance with the legislation in force at the time of conclusion of the agreement until the payback period for the contracted projects³⁹. Favored treatment of Serbian and Russian companies also refers to selection of contractors, equipment suppliers and services necessary for the implementation of the projects undertaken. Furthermore, it is stated that the selection shall be carried out by the joint companies on the basis of tender procedures, on condition that „all other things being equal”, preference shall be in favor of Serbian and Russian companies.⁴⁰

The agreement states rules which regulate overcoming of potential problems in the implementation of the project and solving disputes and differences about interpretation or application of the provisions of the agreement.⁴¹ Thus, in case that circumstances that prevent any of the Parties from fulfillment of its obligations or any other differences regarding the agreement should arise, authorized entities of the Contracting Parties shall consult in order to reach mutually acceptable decisions to overcome the said circumstances or differences and to ensure the implementation of the Agreement.

Disagreements and disputes concerning the implementation or application of the agreement shall be resolved through negotiations between the Parties, with the conclusion of relevant legal protocols

The agreement shall remain in force for 30 thirty years after entry into force. The termination of the Energy Agreement shall not affect the implementation of obligations under contracts concluded within its framework while it is in force. The Agreement can be amended by written consent of the Parties.⁴²

Finally, the Parties defined the relationship between the Energy Agreement and other international treaties to which they are parties. In that respect, the Energy Agreement shall not affect the rights and obligations of each Party under other international treaties to which they are parties.⁴³

4. Compatibility of the Energy Agreement with obligations arising from the membership in the Energy Community

Shortly after signing the Energy Agreement local experts expressed certain doubts about its compatibility with the obligations Serbia has to fulfill as a member of the Energy Community. Some remarks are given in the legal analysis of the arrangement between Serbia and Russia in the oil and gas industry by ISAC Fund and Nikolić–Kokanović–Otašević Law Office of 21 December 2009. The remarks primarily refer to the more favorable position of Russian and Serbian companies in terms of customs tariffs and tax regime, implementation of regulations on foreign exchange operations, preferential treatment in project implementation tenders etc. The said privileges, according to the author of the legal analysis, are incompatible with the provision governing competition in Article 18 of the Energy Community Treaty, which prohibits abuse of a dominant position and public aid which distorts or threatens to distort competition by favoring certain undertakings.⁴⁴

The first official response to the agreement with Russia came from the Energy Community in March 2010 in a letter from the Community's Secretariat to the Ministry of Energy and Mining of the Republic of Serbia.⁴⁵ This letter voices concern over the state of compliance between the Energy Agreement and provisions of the Second Energy package of the EU, which are integral part of the Energy Community Treaty. In that regard, a special emphasis was placed on the problem of providing free access to gas infrastructure and setting tariffs for gas transportation.

The problem concerning the construction of the South Stream gas pipeline suddenly escalated in early December 2013, when first pipes were welded in Serbia and Bulgaria.⁴⁶ It is obvious that the planned beginning of construction of the gas pipeline made the European Commission stop issuing internal warnings and move on to announcing particular measures to ensure implementation of EU regulations. In his address to the European parliament of 4 December 2013, Director for Internal Energy Market of the European Commission Klaus-Dieter Borchardt expressed the Commission's official stance that international treaties between the six EU-member states (Bulgaria, Hungary, Greece, Slovenia, Croatia and Austria) and Russia on the construction of the South Stream are in breach of EU law and have to be renegotiated.⁴⁷ If that does not happen, the Commission shall require that the said EU-member states revoke the treaties with Russia. It was also announced that the Commission shall use all legal means at its disposal to stop the operation of the gas pipeline on the EU territory if it fails to comply with EU regulations. Apart from the already mentioned remarks concerning free access to gas infrastructure and setting tariffs for gas transportation, European Commission's main concern is the separation of ownership of the pipeline and ownership of the gas being transported. Although Serbia does not fall into the jurisdiction of the European Commission, it was explicitly stated that the EU expects Serbia to fulfill its obligations under the Energy Community Treaty. There was a similar warning about the Energy Agreement from the Energy Community Secretariat of 21 February 2014.⁴⁸ Decision of the Energy Community Secretariat of 25 April 2014 to seek opinion from the Council of the EU on the legality of the bilateral treaty between Serbia and Russia in terms of EU regulations implemented in the Energy Community shows that there will be further steps after the warnings. In the rest of this paper we will consider the remarks of the Energy Community Secretariat and European Commission regarding the incompatibility of provisions of the agreement between Serbia and Russia with the regulations of the Energy Community. The focus is on parts of the EU acquis that are incorporated in the Second and Third Energy packages, which in turn are taken from the Energy Community Treaty. Considering that there is also the question of the time-frame of certain regulation, we will provide separate analyses of obligations which Serbia has to fulfill under the Second Energy Package, which was in force when the agreement with Russia was signed, and those under the Third Energy package, which was later adopted by the Energy Community.

4.1. Compliance with the rules of the Second Energy package: Directive 2003/55/EC

Serbia concluded the agreement with the Russian Federation as a member of the Energy Community. In that respect we will consider if the agreement between Russia and Serbia is incompatible with the Energy Community Treaty and with which provisions, while we will also focus on the EU acquis regulations which were in force at the time the agreement was signed. What we particularly have in mind are the provisions of Directive 2003/55/EC of 26 June 2003 on integrated natural gas market.

Directive 2003/55 is part of the so-called EU Second Energy Package, whose main goal is to complete the internal gas market. In that respect the Directive was supposed to ensure a more open gas market while fully complying with laws regulating competition and minimizing the risk of creating and abusing a dominant position by certain business entities. In order to achieve the

goals set, the Directive prescribes common rules that regulate the transportation, distribution, supply and storing of natural gas. Serious consideration was given to providing free access to transmission and distribution networks and third-party access to storage facilities without any kind of discrimination. These very issues were the subject of the analysis by the Energy Community Secretariat in the letter this body addressed to the Ministry of Mining and Energy of the Republic of Serbia in March 2010.

4.1.1. Obligation to provide free access; setting tariffs

The most important remark of the Secretariat in the March 2010 letter is related to the problem of third-party free access to transportation and storage facilities. Namely, Article 8 paragraph 3 of the Energy Agreement stipulates that the Russian party has the right to use all capacities of the gas pipeline and the underground gas storage facilities. In the opinion of the Secretariat, this provision of the agreement „does not seem to be in compliance” with the regime of free access by a third party as prescribed in the Directive. In accordance with the provisions of the Directive free access to gas networks is obligatory in all instances. The Directive allows the member states to decide whether access to gas storage facilities shall be provided in accordance with negotiated terms or terms prescribed by law. In any case, free access has to be ensured. The letter also points to the fact that the Directive envisages certain derogations from the obligation to provide free access to the gas pipeline facilities to third parties. For example, new and significant gas pipeline networks, such as networks between member states or storage facilities can be exempted from the obligation to provide free access to third parties under certain conditions. In these cases competent national bodies grant derogation under the conditions specified in the Directive, which shall be notified to the Community Secretariat.⁴⁹ However, as it was emphasized in the letter, the Secretariat was not informed about the existence of any request or decision from the Serbian party to exempt the gas pipeline facilities subject to the Energy Agreement from the third-party free access rule.

The other remark is related to the way the gas transportation tariff was calculated prescribed by the Energy Treaty. Article 8 paragraph 2 of the Energy Treaty prescribes that establishment of tariffs for services relating to transportation and pumping, storage and production of gas shall be within the exclusive competence of the joint company which will be founded by Gazprom and Srbijagas. In relation to that, the Secretariat pointed to provisions of Article 18 paragraph 1 and Article 25 paragraph 2a of the Directive, which envisage competence of regulatory authorities of the Member States in establishment or approval of tariffs for transportation of gas or at least methodologies of their calculation. Competence of a regulatory body is obligatory, but like in the previous instance, it can be subject to exemptions under the conditions stated in Article 22 paragraph 1 of the Directive, which is subject to decision of the competent authority of the member state. Still, there is no evidence that Serbia asked for such exemption in this case as well.

Finally, the Secretariat pointed to the problem related to increasing the capacity of the gas pipeline. Namely, Article 4 of the Energy Treaty envisages that the pipeline shall have the annual transmission capacity no less than 10 billion cubic meters of natural gas, while Gazprom and JP Srbijagas shall consider the possibility of increasing the volume of natural gas transmission from Russia to Serbia. Particular quantities, conditions and deadlines for gas delivery shall be established by relevant contracts. In the opinion of the Secretariat, the said provision of the agreement is not compatible with Article 2 paragraph 4 of the Directive, which defines the function of the gas transmission system operators. The said provision of the Directive imposes obligation on the operator to meet „reasonable demands for the transportation of gas”. This obligation cannot be restricted by a decision of the owner of the gas pipeline to limit the quantity of gas supplied through the pipeline.

Regarding the two said remarks, i.e. the obligation to provide free access to the gas pipeline and the way tariffs are set, one can hardly argue against them due to linguistic clarity of the formulations of the relevant provisions of the Energy Agreement and Directive 2003/55. The nature of their incompatibility is such that it cannot be eliminated by interpreting these documents. The situation with increasing the capacity of the gas pipeline is somewhat different and it is possible to find solutions which would satisfy all parties, which is also indicated by the fact that 2009/2010 and 2012/2013 annual reports on the implementation of *acquis communautaire* submitted by the Secretariat of the Energy Community are focused solely to the matters of unrestricted access to the gas pipeline and calculation of tariffs.

4.1.2. Obligation of legal and functional unbundling of activities

In the said annual reports on the implementation of *acquis communautaire* the Secretariat looked into another problem that can have an impact on the implementation of the Energy Agreement: it is obligation of legal and functional unbundling for the operator of the gas transport system and gas production, supply and distribution in cases when these activities are operated by a vertically integrated company.⁵⁰

This obligation is prescribed so as to provide efficient and non-discriminatory access to gas networks by third parties. Article 9 paragraph 1 of the Directive prescribes that legal entities which operate gas transmission and distribution systems must be independent from other activities not relating to transmission in terms of their legal form, organization and decision making. In order to ensure that, the following minimum criteria shall apply:

- those persons responsible for the management of the transmission system operator may not participate in company structures of the integrated natural gas undertaking responsible, directly or indirectly, for the day-to-day operation of the production, distribution and supply of natural gas;
- appropriate measures must be taken to ensure that the professional interests of persons responsible for the management of the transmission system operator are taken into account in a manner that ensures that they are capable of acting independently;
- the transmission system operator shall have effective decision-making rights, independent from the integrated gas undertaking, with respect to assets necessary to operate, maintain or develop the network. However, this does not prevent the existence of appropriate coordination mechanisms to ensure that the economic and management supervision rights of the parent company in its affiliates;
- the transmission system operator shall establish an appropriate program to set out measures taken to ensure that discriminatory conduct is excluded, and ensure that observance of it is adequately monitored.⁵¹

Serbia was bound to fulfill this obligation before 1 July 2007 and to restructure JP Srbijagas in accordance with the requirements of the Directive by that time. Serbia has not fulfilled this obligation so far. After a series of warnings, in its annual report of 1 September 2013 the Secretariat announced launching proceedings against Serbia for persistent breach of obligation under Directive 2003/55. Apart from JP Srbijagas, Yugorosgaz was also subject to monitoring: it was founded in 1996, its stakeholders are Srbijagas (25%), Gazprom (50%) and Central ME Energy and Gas Vienna (25%), and the company is also licensed for gas supply and transportation in Serbia.⁵²

In accordance with the announcement, on 24 October 2013 the Secretariat launched proceedings against Serbia for failure to meet contractual obligations under the Energy Community Treaty.⁵³ In the opening letter of the Secretariat it is stated that Serbia failed to meet the obligation of unbundling activities in its legal form in two vertically integrated companies licensed for transportation of gas, i.e. JP Srbijagas and Yugorosgaz. In its response of 20 February 2014 the Ministry of Energy, Development and Environmental Protection of the Republic of Serbia basi-

cally confirmed the allegations from the Secretariat's opening letter and mentioned the complexity of the unbundling process which entails financial, technical and legal problems, including energy safety. At the same time, the Ministry professedly expressed willingness to unbundle the activities of Srbijagas and Yugorosgaz in compliance with the obligations under the Third Energy Package, without stating an exact time frame or a particular action plan to fulfill this obligation.⁵⁴ It is interesting to note that the expressed willingness refers to harmonization with the Third Energy Package, which is more demanding in terms of unbundling of activities (which will be further dealt with in the following chapter), but not with the Second Energy Package.

After Serbian response to the allegations from the opening letter, on 24 February 2014 the Secretariat submitted a Reasoned Opinion in which it reiterated the stance that Serbia failed to fulfill its obligation under Directive 2003/55. Along the same lines, the Secretariat stated that the process of legal and functional unbundling of activities had not even started in JP Srbijagas, while Yugorosgaz established a subsidiary for gas transport in 2013, named Yugorosgaz Transport d.o.o, but it did not fulfill the obligations under the Directive, because it did not ensure independent decision making of the subsidiary (functional unbundling). In the opinion of the Secretariat, failure to unbundle activities of these two companies is a key obstacle to the development of a competitive gas market in Serbia and negatively affects the development of a wider regional gas market and the urgently needed gas infrastructure investments. It was also emphasized that despite the expressed willingness to unbundle the activities of the said companies in accordance with the Third Energy Package, Serbia is still responsible for failure to comply with its obligations under the Second Energy Package, of which Directive 2003/55 is an integral part.

Finally, on 24 April 2014 the Energy Community Secretariat submitted a Reasoned Request to the Ministerial Council to pronounce Serbia responsible for failure to legally and functionally unbundle the activities of JP Srbijagas and to ensure independence in decision making in Yugorosgaz Transport d.o.o, which would breach the obligations under Article 9 paragraph 1 and paragraph 2 of Directive 2003/55.

Launching proceedings against Serbia for failure to comply with obligations under the Directive can have serious consequences on the implementation of the Energy Agreement. JP Srbijagas is one of the participants in the South Stream and Banatski Dvor projects. The Energy Agreement envisages that the gas pipeline and underground gas storage facilities will be operated by joint companies in which Gazprom and JP Srbijagas will participate. Thus, every change in the status of any participant in joint companies is significant for the implementation of the planned projects. Secondly, and what is more important, is that launching proceedings against Serbia is a clear sign that the Secretariat will insist on strict implementation of the Community's regulations concerning the functioning of the South Stream gas pipeline.

Concerning this issue, we should also bear in mind that the Energy Agreement does not regulate organization and management of joint companies which will operate the gas pipeline and gas storage facilities or the relationship between the said companies and their founders. This matter is to be handled by the Adhering Parties, i.e. AO Gazprom and JP Srbijagas and their mutual agreement. Apart from the tax regime, the Energy Agreement does not envisage a special treatment of the joint companies which would allow them to be exempted from national regulations; therefore, there are no legal obstacles to solving this issue in accordance with Serbian law. Since ratified international treaties are an integral part of the Serbian legal system and are applied directly, in this case the application of the Energy Community Treaty and regulations based on it is implied.⁵⁵ However, even in spite of that, Gazprom and JP Srbijagas concluded several contracts which regulate this matter contrary to the rules under Directive 2003/55.

General conditions of the basic agreement on cooperation between OAO Gazprom and JP Srbijagas of 5 December 2008 envisage that the Adhering Parties shall establish a joint company for the implementation of the South Stream project in Serbia.⁵⁶ It is interesting to note that the Ad-

hering Parties agreed to establish the joint company in accordance with Swiss law, no later than 1 March 2009. Pursuant to general conditions, Gazprom and JP Srbijagas founded the joint company *South Stream Serbia AG* on 17 November 2009 with headquarters in Zug, Switzerland. *South Stream Serbia AG* established an affiliate in Serbia on 28 November 2011, named *South Stream d.o.o. Novi Sad*. Main activities of the Novi Sad affiliate are pipeline gas transmission and operating gas transport system.⁵⁷ Regarding the fact that *South stream d.o.o. Novi Sad* will directly operate the transportation system in Serbia, it is subject to rules under Directive 2003/55 in terms of legal, functional and organizational independence. On the other hand, the Memorandum of Association of these companies does not envisage any guarantees in that sense. Quite contrary to the obligations under the Directive, it is envisaged that Gazprom and JP Srbijagas will appoint managers of the company via their representatives in Board of Directors of *South Stream Serbia AG*, which functions as shareholders' assembly, and shall supervise their work.⁵⁸ Apart from that, it is prescribed that the managers of the company must implement all decisions made by the body of the founder, which is also a serious breach of obligations under Directive⁵⁹. The only reason why *South Stream d.o.o. Novi Sad* was not subject to monitoring by the Energy Community Secretariat is that it had not even started performing its activity, because the construction of the gas pipeline is still in initial stage

4.2. Compliance with the Rules from the Third Energy Package: Directive 2009/73/EC

The main objection of the European Commission concerning bilateral agreements between the six member states of the EU and Russia on the construction of the South Stream gas pipeline refers to the issue of ownership unbundling concerning the gas pipeline and the gas to be transmitted.

The ownership unbundling obligation is stipulated in the Third Energy Package of the EU, namely Directive 2009/73 of 13 July 2009, repealing Directive 2003/55.⁶⁰ At the time when Serbia concluded the agreement with Russia, this directive was not part of the applicable EU *acquis* under the Energy Community Treaty. It was not until 6 October 2011 that the Ministerial Council of the Energy Community decided on taking over parts of the Third Energy Package, with an obligation of harmonization until 1 January 2015. In this regard, the question arises as to whether and to what extent Serbia is obliged to implement the regulations from the Third Energy Package on the projects planned by the Energy Agreement after that date.

4.2.1. Validity period of the Directive 2009/73/EC

The answer to the question about the Serbian obligations stipulated in the Directive 2009/73 regarding the implementation of the Energy Agreement with Russia must be sought in the general system of the Energy Community Treaty. As we have seen, the principle of loyalty from Article 7 of the Energy Community Treaty obliges Member States to refrain from any measures which could jeopardize the attainment of the Treaty objectives. The obligation prescribed is identical to that of Article 4, paragraph 3 of the Treaty on the European Union. The principle of loyalty applies equally to legal domestic and international legal documents that may jeopardize the objectives of the Community. Let us remind that the main reason for the establishment of the Community is to create an integrated market for natural gas and electricity between the EU and the associated countries. Achievement of this objective necessarily implies the creation of a single legal framework and constant harmonization of the Community rules with the new EU regulations in the field of energy, which is stipulated in Article 25 of the Energy Community Treaty. Having concluded the Energy Community Treaty, Serbia transferred certain legal and creative powers to the Community bodies. At the same time, Serbia undertook an obligation that its legal documents would not affect the development and application of future legislation

in the area. Furthermore, Serbia committed itself to take all measures, both general or specific, which would ensure the fulfillment of the obligations arising from the Treaty.⁶¹ It means that Serbia cannot claim the international agreements, meanwhile concluded with third countries, to be the reason for failure to meet the obligations of membership in the Energy Community. The same conclusion is indicated by the provision of Article 101 of the Energy Community Treaty, which stipulates an obligation upon the parties to take all appropriate measures to eliminate the discrepancy between the treaty and the previously concluded international agreements with third countries. By analogy, one could conclude that the membership in the Energy Community prohibits conclusion of new international agreements with third countries which would be contrary to the regulations of the Energy Community, or could jeopardize its objectives.

As a result of the aforesaid, from the standpoint of the regulations of the Energy Community, Serbia is obliged to promptly and fully take all measures to ensure fulfillment of the obligations set out in the Directive 2009/73 on its territory. This obligation also applies to the projects planned by the Energy Agreement.

4.2.2. The obligation of ownership unbundling

It remains to consider the nature and content of the obligation of ownership unbundling and the question of whether it can be harmonized with the obligations under the Energy Agreement. One of the main reasons for the adoption of the Directive 2009/73 was that the rules under Directive 2003/55 did not result in the expected outcome and did not provide the independence of the transmission systems operators in relation to other parts of vertically integrated companies. This alone threatens competition in the gas market, and above all, free and non-discriminatory access to transmission networks made by third parties. In other words, it was concluded that legal and functional unbundling of activities within the vertically integrated companies is not a sufficiently effective tool that would prevent those companies from discriminating competitors and provide free access to their transmission networks. For the same reason those companies are not sufficiently motivated to invest new funds in the building of new networks and maintenance of the existing ones.

Consequently, Directive 2009/73 provides for a new set of rules that should ensure full independence of transmission systems operators. Member States are allowed a choice of whether to carry out the complete ownership unbundling activities or to opt for setting up an independent system operator or transmission operator.

The conditions for ownership unbundling are regulated by Article 9 of the Directive. In accordance with this Article, Member States have committed to ensure that any company that owns a transmission system acts as a transmission system operator by 1 June 2016.⁶² It is strictly prohibited for the same person or persons to simultaneously exercise control over companies that perform any function of production or supply, and over a transmission system operator or over a transmission system itself, and vice versa. In addition, the same person or persons cannot appoint members of the supervisory board, board of directors or other boards with the right of representation, in a company that acts as the transmission system operator, and directly or indirectly exercise control or exercise any right over the company which carries out the business of production or supply of gas. In the end, it is envisaged that the same person shall not be simultaneously a member of the supervisory board, board of directors or other boards with the right of representation, in a company which carries out the business of production or supply and a company that acts as an operator.

Instead of full ownership unbundling, Member States may, on the proposal of the transmission system owner, decide to set up a system operator or transmission operator that is independent from the interests of the gas producers and suppliers. This solution enables vertically integrated

companies to retain the ownership of gas networks and at the same time provide an effective separation of interests, provided that the set operator performs its function in accordance with the precisely defined conditions and under full supervision of the competent regulatory authority. However, here we must bear in mind that the possibility of choosing this model is limited only to those transmission systems that were owned by vertically integrated companies as of 6 October 2011.⁶³ In all other cases, Member States are required to complete full ownership unbundling in the companies for gas transmission.

For the case of full ownership unbundling certain guarantees were provided to protect the rights of the shareholders of vertically integrated companies. In this regard, Member States were given the right to choose the way to perform ownership unbundling. Member States may decide to implement ownership unbundling through direct seizure and sale of shares or through the division of shares of a vertically integrated company to the shares of a gas transmission company and the shares of a gas production and supply company, provided that they meet all other requirements for ownership unbundling.⁶⁴

Supervision of the fulfillment of the obligation of ownership unbundling shall be exercised by national regulatory authorities that shall issue permits for gas transmission. Article 11 of the Directive prescribes a special procedure for issuing licenses at the requests of the owners or operators of transmission systems which are controlled by entities from third countries. In addition to compliance with the requirements from the Article 9 of the Directive, the national regulatory authority shall take into account the security of Energy Community gas supply in the decision making process and particularly:

- rights and obligation of the Energy Community pursuant to international law;
- rights and obligations arising from international agreements which the members of the Energy Community concluded with third countries, provided that they comply with the Energy Community Treaty;
- rights and obligations arising from the Accession Agreement or from trade agreements between the EU and the associated countries;⁶⁵
- other specific facts and circumstances in connection with the respective third country.

In order to ensure fulfillment of international obligations of the Energy Community, it is envisaged that in such cases the Secretariat of the Community shall previously give an opinion on fulfillment of the conditions for obtaining the license. This procedure shall come into force in the Energy Community as of 1 January 2017.⁶⁶

To what extent is it possible to reconcile the demands from Directive 2009/73 with the obligations under the Energy Agreement? As a reminder, the Energy Agreement envisages that infrastructure, manufacturing and other facilities, as well as other assets which are build, modernized or purchased by joint Russian-Serbian companies during the performance of economic activities within the projects South Stream gas pipeline and the Banatski Dvor gas storage, are the property of those companies.⁶⁷ This provision of the Agreement is in the direct contradiction with the obligation of ownership unbundling. Certain space for finding solutions that would not require an amendment of the Energy Agreement may be sought under Article 36 of the Directive, which provides for the possibility of exempting new major infrastructure projects from the obligation of ownership unbundling. The problem is that such an exemption is limited in time and is subject to strict conditions:

- the investment concerned must enhance competition in the gas supply and enhance security of the supply;
- the level of risk that accompanies the investment must be such that the investment would not have happened without the approval of such exemption;
- the owner of the new infrastructure must be a natural or legal person who, at least in legal terms, must be separated from the system operator, as part of which the infrastructure shall be built;

- the infrastructure users shall be charged fees;
- the exemption must not negatively affect competition or the effective functioning of the internal market of natural gas, or the efficient functioning of a regulated system to which the infrastructure is connected.

The decision on exemption shall be made by the national regulatory authority. When deciding, the regulatory authority shall take into account the need to prescribe conditions for the duration of the exemption and to provide a non-discriminatory access to the infrastructure made by third parties. Before granting the exemption, the regulatory authority shall decide on the rules and mechanisms for the management and distribution of new capacities. These rules shall require all potential users of the infrastructure to be invited to express their interest before the distribution of new infrastructure capacities is carried out, including also for their own needs. The regulatory authorities shall also require the unused capacities of the infrastructure to be offered on the market, and for users to be authorized to trade their contracted capacities on the secondary market. The decision approving the exemption must be duly reasoned and published. The decision shall be submitted to the Secretariat of the Community, which, within two months, may order the national regulatory authority to amend or withdraw the granted exemption. The national regulatory authority is required to comply with the decision of the Secretariat within one month from the receipt of the decision.

4.2.3. Other Obligations under the Directive 2009/73/EC

However, the obligation of ownership unbundling of the gas pipeline is not the only vexed issue in the relations between the EU, Serbia and Russia. This obligation serves to provide free, non-discriminatory access for third parties to the systems for the transmission and storage of gas. That was the basic objection of the Energy Community Secretariat set forth in said letter of March 2010. Free access to gas systems made by other manufacturers of gas is the key condition to enable open gas market and free and fair competition. In this regard, Directive 2009/73 provides more rigorous and detailed obligations for the transmission systems operators and broader jurisdiction to national regulatory bodies, particularly in terms of monitoring. They also changed the existing rules and introduced new ones regarding the manner and criteria for determining fees for the access of third parties to the gas systems. Therefore, it is demanded that these fees are transparent, non-discriminatory, to correspond to actual costs of gas transmission, as well as to take into account the integrity of the gas system. Exactly like the previous Directive stipulated, fees or methodology of their calculation must be approved by the relevant regulatory authority and published prior to their entry into force. What is particularly unacceptable for the Energy Community and the European Commission is the fact that, according to the Energy Agreement, the determination of the prices of transmission services, storage and gas flow is under exclusive jurisdiction of the joint enterprise in which Gazprom will have a majority share. In this regard, the decisions from the Directive 2009/73 only deepened the existing differences and made potential negotiations on the revision of the Energy Community Treaty even more uncertain.

4.3. Possible Consequences due to Violation of Obligations under the Energy Community Treaty

As we could see, the conflict between certain provisions of the Energy Agreement and the rules that oblige Serbia under the Energy Community Treaty is of such nature that it cannot be overcome by a coherent interpretation. In such a situation, the membership in the Energy Community requires Serbia to take all necessary measures to eliminate the discrepancy between the provisions of the Energy Agreement and the Energy Community Treaty. If this is not possible, Serbia is obliged to cancel the agreement with Russia. Otherwise, Serbia could be found

responsible for a violation of the Energy Community Treaty, which entails appropriate legal consequences, and ultimately the suspension of certain membership rights.

Political consequences of violations of obligations under the Energy Community Treaty could be even more serious than legal ones. Serbia is a candidate for EU membership and in January 2014 it started accession negotiations. Fulfillment of obligations under the existing international treaties with the EU is one of the conditions for Serbia's EU membership. This issue is a real test to be used to assess the ability of Serbia to fully implement a complex agreement such as the Energy Community Treaty. If Serbia is not able to timely and properly comply with the obligations under such an agreement, then it is very unlikely that it will be able to meet more comprehensive obligations of EU membership. Therefore, this issue will be discussed in detail during the negotiations under Chapter 15 entitled *Energy*. In this regard, the degree of compatibility of Serbian legislation with the EU regulations will be specifically assessed, together with the administrative capacities of Serbia for proper implementation of these regulations. The duration and outcome of the negotiations will therefore largely depend on the way in which Serbia fulfils its obligations of membership in the Energy Community. After all, this is implied by the report of the European Commission submitted to the European Parliament and the Council pursuant to Article 7 of the Decision 2003/500/EC (Energy Community Treaty) of 10 March 2011. This report explicitly states that the application of the *acquis* of the Energy Community will be a decisive factor in the negotiations on EU membership. Possible lack of application will be negatively assessed in the reports on the progress of the European Commission and could result in re-opening of the energy chapter in the accession negotiations. On the other hand, the candidates that fully apply the legal heritage of the Energy Community can expect rapid progress in the accession negotiations.⁶⁸

It should also be taken into account that the Energy Community occupies an important place within the energy as well as foreign policy of the EU. Therefore, it is more than certain that the EU will insist on consistent compliance with the obligations arising from the membership in the Community, especially when it comes to such fundamental issues that are directly related to energy independence and security of gas supply. The tensions between the EU and Russia in connection with the crisis in Ukraine and the annexation of Crimea and the possibility of introducing economic sanctions to Russia make this problem even more complex. In such circumstances, Serbia will be expected to act as a loyal member of the Energy Community and to properly implement its provisions. European Commission announced that Serbia will have to adjust the Energy Agreement with the European regulations if it wants to avoid the deadlock in the negotiations with the EU. The statement of the European Commissioner for Energy, Günther Oettinger, has the same tone stating that the negotiations on the accession of Serbia to the EU and the negotiations between the EU, Serbia and Russia on the revision of the Agreement on the construction of South Stream gas pipeline are „two related and simultaneous processes.“ However, before we consider the possibility of revision of the Energy Agreement, it is necessary to ascertain its legal effect, according to the rules of international law.

5. South Stream gas pipeline in international law

Legal framework for the construction of the South stream gas pipeline is established in international agreements which six EU Member States (Austria, Slovenia, Croatia, Hungary, Bulgaria and Greece) and Serbia concluded with Russia in the period between 2008 and 2010. The rules of public international law contained in the Vienna Convention on the Law of Treaties from 1969 (hereinafter referred to as the Vienna Convention) shall be applied to the stipulation, the effectiveness, compliance, implementation, interpretation and termination of these agreements. In accordance with the principle *pacta sunt servanda* under Article 26 of the Vienna

Convention, the international agreement binds the parties and they should execute it in good faith. Article 27 of the Vienna Convention expressly provides that the member state of the agreement may not refer to the provisions of its domestic law to justify the failure to execute the agreement. However, in this case, there is a conflict between international agreements that the six Member States of the EU and Serbia concluded with Russia and their former obligations deriving from the membership in the European Union and the Energy Community. Therefore, the logical question is whether responsibility towards previous international agreements and membership in international organizations is an obstacle to the conclusion and implementation of new international agreements with third countries, which would be contrary to existing obligations.

The answer to this question must be sought in the rules of customary international law.⁶⁹ As authentic subjects of international law, states have full contractual capacity and their right to conclude international agreements may only be limited by absolutely mandatory rules of international law. After all, the Vienna Convention itself in its preamble states the principle of free consent of a state to be bound by the provisions of an international agreement. That means that from the standpoint of public international law there is no obstacle for a state to conclude two or more international agreements which conflict with each other. Such international agreements would be valid according to the rules of public international law.

The question of international responsibility of the state towards other parties for breaching contractual obligations must be considered separately from this issue. In this case, a contracting party from the previous international agreement may require implementation of the agreement and declare the new one null and void, or suspend its application and terminate it by demanding appropriate redress and compensation for damage.⁷⁰

To avoid such situations, customary international law and the Vienna Convention prescribe the principle of good faith that states are obliged to respect in all phases of stipulation, implementation and termination of an agreement. States are expected to conscientiously assess the obligations arising from international and domestic law, and which may be an obstacle for the stipulation and implementation of an international agreement. In this case, the six Member States of the EU and Serbia were obliged to assess whether membership in these organizations may impede the stipulation and implementation of the agreement with Russia. On the other hand, Russia itself had to be aware that the agreements would be implemented on the territory of the EU and the Energy Community, and would therefore be subject to the regulations of these organizations.⁷¹ Especially because Russia has developed relations with the EU, with the still binding 1997 Partnership Agreement. However, the primary responsibility regarding the assessment of all legal circumstances related to the implementation of the agreement lies with the Member States, the EU and Serbia. It is more than probable that some of these countries have decided to deliberately ignore the rules of their organizations in order to secure the best possible conditions for the supply of gas for themselves. At the same time, they obviously did not count on a decisive action by the European Commission and its determination to ensure abiding by common rules in the energy sector. Therefore, they have found themselves in an impossible legal situation, pressed by mutually conflicting obligations of membership in their organizations and those from the agreement with Russia. Therefore, firstly, the question arises of whether and to what extent the EU membership, and the Energy Community, is an obstacle to the application of bilateral agreements with Russia. In this regard, we shall consider the constitutional rules of these two organizations, as well as the relevant rules of international law.

The Energy Community and the European Union differ significantly in their structure and legal nature. The Energy Community is a classic inter-governmental international organization. The Energy Community Treaty and the decisions of the Community bodies in Serbia pertaining to it have the status of domestic law, and as such are used in Serbian legal order. In accordance with the Constitution of Serbia, the ratified international agreements are part of the domestic legal

order and are directly applied. As such, they supersede national regulations, but they must be in accordance with the Constitution. However, in this case we have a conflict between two opposing international agreements. The parallel existence of such agreements can lead to significant complications in the domestic legal order, particularly since these agreements provide certain benefits or rights for the other party or its natural and legal persons. For disputes that may arise in this regard, the jurisdiction of domestic courts is envisaged and they are subject to the domestic constitutional rules. Given that these are acts of the same legal force, their conflict is resolved by application of *lex specialis derogat legal generali* rule. In accordance with this rule, the Energy Agreement would supersede the Energy Community Treaty, as it establishes a special regime in relation to the general Community rules.

The situation is completely different in the European Union. In contrast to the Energy Community, the EU contains expressed supranational elements. As a result, the EU is in certain aspects closer to the confederal and even federal model of organization than to traditional international organizations. During its existence, the EU has built its own legal system which is autonomous in relation to the international law and internal laws of the Member States. Subjects of the EU legal order are not only Member States but also their citizens. With the entry into force of the initial agreement, the rules of that legal system have become an integral part of the legal systems of the Member States, and their courts are obliged to apply such rules.⁷²

Basic features of the EU legal order are, among other things, expressed in the principle of homogeneity and the principle of primacy of EU law over the laws of the Member States.⁷³ The principle of homogeneity implies that the EU founding treaties and regulations derived from them equally oblige all Member States and have the same effect on the entire EU territory. This in turn requires the existence of a single court which ultimately decides on all matters relating to the interpretation and application of EU regulations. Within the Union, this function is entrusted to the Court of Justice of the EU. Accordingly, there is another specificity of the EU distinguishing it from traditional international organizations. Application and effect of EU laws in the Member States is determined only by EU law, and not by constitutional rules of the Member States, such as, for example, in the case of the Energy Community. This enabled the Court of Justice to establish the following important legal principle of the EU: the principle of primacy of EU law over the national law. In accordance with this principle, the EU regulations supersede all acts of the Member States, both national and international. The principle of the primacy of EU law is partially based on the transfer of sovereign powers from the Member States to EU bodies, and partly on the principle of loyalty, which obliges all Member States to refrain from any measure which could threaten accomplishment of the objectives of the Treaty. The purpose of this principle is to ensure the full effect of EU law in all Member States. In this regard it should be borne in mind that the principle of the primacy of EU law does not result in termination of conflicting national legal acts, but merely provides that such regulations could not be applied to a particular legal situation. In this case, it means that the agreements that the six Member States concluded with Russia could not be applied within the EU legal system. This does not threaten their validity at the international level, or a possible international responsibility of the Member States towards Russia because of failure to fulfill the commitments. If, by chance, any of these Member States tried to implement the agreement with Russia on its territory, it would be exposed to the risk that the Commission launches a legal action against it before the Court of Justice of the EU because of breaching obligations under Founding Treaties. The ruling of the Court of Justice establishing a violation has a binding effect and the respective state shall take the necessary measures for execution of such judgement. Failure to enforce such a judgment may represent grounds for new trial proceedings in which the Court of Justice may oblige a Member State to pay a lump sum or a fine.⁷⁴ In addition, the judgment of the Court of Justice which establishes that a member state violated an obligation under this Treaty, shall take effect within the national legal system as well. In this case, any legal or natural person with related legal interest may require the national court not to apply an illegal national law.⁷⁵

To conclude, international agreements between the six Member States of the EU and Russia do not bind the Union and cannot be applied in its territory to the extent in which they are contrary to EU law. On the other hand, they continue to exist at the international level. Failure to fulfill the obligations of these agreements may result in international responsibility of the respective EU Member States towards Russia. However, this would impede the basic Russian interest: the construction of the South Stream gas pipeline. So far, Russia has invested substantial resources in implementation of this project and consequently expects to make significant profit. Instead, if in the meantime an amicable solution to the problem is not found, Russia will be drawn into a series of international disputes with the EU Member States, with which they normally have friendly relations. On the other hand, the EU itself cannot be indifferent to international legal problems of its Member States because of incapability to fulfill agreements with Russia. Moreover, the EU itself has an interest in the pipeline construction. This would provide a new route for the gas delivery and increase stability in the supply of this energy-generating product.

In an attempt to resolve the present situation, the EU and Russia have agreed to start negotiations in order to find an amicable solution to the current situation. The EU Member States, which signed agreements with Russia, have authorized the European Commission to participate in negotiations with the Russian party. The problem is that the initial positions of the two sides are far apart. The European Commission insists on consistent compliance with the EU rules on its entire territory. Russia, on the other hand, refers to the concluded international agreements with the six Member States. According to the Russian position, the EU law is part of national law of the Member States, while international agreements are an integral part of international law that has precedence over domestic law, EU law included. As we have seen, such an attitude ignores the fact that the EU is not bound by international agreements which individual Member States have concluded with Russia, as well as that the question of the relation of these agreements and the Union Law will be solved within the EU legal order. Essentially, the starting positions of the EU and Russia represent taking positions before the main battle that will be led for implementation of the Third Energy Package of the EU. This is confirmed by the statement of the Russian Ambassador to the EU Vladimir Chizhov, dated 13 January 2014, that Russia will not negotiate with the EU on cancellation or termination of the bilateral agreements with the six Member States of the EU, or on their compliance with the regulations of the Third Energy Package. According to his own words, only the adjusting of the Third Energy Package to the concluded agreements can be subject to negotiation.

The first meeting of Russian and European representatives was held in Moscow on 17 January 2014 under the Energy Dialogue, which was established at the sixth meeting of the Permanent Partnership Council EU-Russia in Paris in 2000. The meeting was attended by the European Commissioner for Energy Günther Oettinger and the Russian Energy Minister Alexander Novak. After the meeting, the participants gave a brief statement that the EU and Russia agreed to establish a working group to consider the legal and technical issues related to the construction of the South Stream gas pipeline. If nothing else, that way the question of South Stream gas pipeline set the ball rolling. In the meantime, there has been an escalation of the crisis in Ukraine, the Russian annexation of Crimea and the introduction of political sanctions against Russia by the EU, which moved negotiating the fate of the South Stream gas pipeline in the background. The possible extension of sanctions against Russia would alienate both sides even more from the possibility of finding an agreeable solution. In a statement dated 10 March 2014 for the German magazine *Die Welt*, the European Commissioner for Energy Günther Oettinger announced that due to the current international situation, the talks with the Russian side on the South Stream gas pipeline would be delayed and that they would not be rushed by the European Union.⁷⁶ The conclusions of the European Council from the meeting of 20 and 21 March 2014 were formulated in a similar way. Among other things, the European Council called for an effective and uniform application of the rules of the Third Energy Package by all participants in the European energy market, which is a clear signal to the Russian party that no exceptions are welcome in this regard. In addition, the necessity to take additional measures to reduce

energy dependency of the EU from the third countries was emphasized⁷⁷. But it has already been speculated that the South Stream gas pipeline may be the first victim of such measures. On the same day, 20 March, Paolo Scaroni, executive manager of the Italian company ENI, one of the main partners of Gazprom in the South Stream gas pipeline project, at a hearing in the Italian parliament, said that the future of the South Stream gas pipeline was uncertain and that the Ukrainian crisis could jeopardize the already complex process of obtaining the necessary permits in the EU Member States.⁷⁸ Recent events seem to confirm hunches of the ENI management. Namely, on 3 June, the European Commission formally requested Bulgaria to suspend all activities related to construction of the South Stream gas pipeline until the legal framework for the implementation of this project is in compliance with the EU regulations.⁷⁹ In accordance with this request, on 8 June, Bulgaria decided to temporarily suspend work on the project South stream gas pipeline.⁸⁰ Such developments certainly do not leave much room for optimism that the dispute over the South Stream gas pipeline may soon be resolved.

6. Possible outcomes of the dispute

It would certainly be best for Serbia if the EU and Russia reached an agreement to overcome the existing problems and enable construction of the South Stream gas pipeline. Such an agreement would necessarily include Serbia as well, as a member of the Energy Community, which shares the same rules in the energy sector with the European Union. Therefore, it would be good for Serbia to enter negotiations between Russia and the EU, if not directly, then at least through the Energy Community Secretariat. In any case, it is already certain that reaching a compromise solution will require certain changes to the existing agreement between Serbia and Russia. These changes must be made in accordance with the rules of the Vienna Convention, which is applicable to the agreement between Serbia and Russia.

In line with Article 39 of the Vienna Convention, an international agreement may be amended only by agreement between the parties. Unless otherwise stipulated by the present international agreement, general rules of the Vienna Convention on the conclusion of international agreements are applied to its amendment. In this regard, it is important to mention that the Energy Agreement contains provisions which relate to overcoming potential problems in its implementation. Article 15 of the Energy Agreement provides that in the event of circumstances that prevent one of the parties in exercising its obligations or other differences related to the agreement, the competent authorities of the contracting parties will open consultations to reach mutually acceptable decisions on overcoming the circumstances or differences and ensuring the agreement implementation. The aforementioned provisions do not specifically define the term of disabling "circumstances" and "other differences", but the formulations used are broad enough to be applied to the existing circumstances, and the circumstances are such as to demand immediate activation of the procedure of consulting Serbian and Russian sides in order to find a mutually acceptable solution that would be in line with Serbia's international obligations and legitimate interests of Russia.

Another scenario, the worse one, would be the failure of negotiations between the EU and Russia. In this case, the six Member States would be forced to terminate their agreements with Russia. Consequently, Serbia would be in a specific legal situation because of its geographical position. The subject of its agreement with Russia would become impossible, which is one of the reasons for the termination of an international agreement. In this case, each of the parties would be exempt from further implementation of the agreement. Although it would not be held internationally responsible for the termination of the Energy Agreement, Serbia would still be faced with significant material losses. Firstly, it would be deprived of important resources invested in implementation of the agreement so far. In fact, in this situation, when there is no

fault of the contracting parties to the termination of the agreement, the applicable rule is that each party shall bear its own costs. Secondly, Serbia would be left without the pipeline that would ensure the gas supply, as well as without major transit revenue it counted on. What would be particularly interesting in the case of such an outcome is the fate of NIS. As a reminder, Serbia is committed by the agreement with Russia to sell 51% of NIS shares to Gazprom. Specific conditions of sale are governed by a particular protocol and treaty, concluded under the Energy Agreement.⁸¹ Sale of majority share in the strategically important company at a questionable price, to say the least, was a special "ticket" for Serbia's participation in the South Stream gas pipeline project, although it is not specifically stated in the agreement. Since the Energy Agreement provides a legal basis for the conclusion of the Agreement on sale of NIS, the question is whether its termination would affect the fate of this legal affair. In other words, does the impossibility of enforcement of certain provisions of the international agreement result in termination of the entire agreement? This issue is governed by Article 44, paragraph 2 of the Vienna Convention. According to the provisions of this Article, the reason for termination of the agreement may be referred to only with respect to the entire agreement, unless the reason is related only to particular clauses. In this case, the reason for the termination of the agreement may be given only in respect of the following clauses:

- if the said clauses are separable from the remainder of the treaty with regard to their application;
- if it appears from the treaty or is otherwise established that acceptance of those clauses was not an essential basis of the consent of the other party or parties to be bound by the treaty as a whole; and
- if continued performance of the remainder of the treaty would not be unjust.

Formally and legally, the sale of NIS shares is a separate legal activity in relation to projects South Stream gas pipeline and Banatski Dvor gas storage so that there is no obstacle for it to be separated from other clauses of the agreement. Besides, Gazprom has fully paid up the price of shares and completed other contractual obligations in connection with the takeover of the majority share in NIS. Bearing in mind the above facts, it is unlikely that termination of the Energy Agreement would result in termination or cancellation of the agreement on sale of the majority share in NIS, particularly in circumstances when the Russian buyer acted in good faith and invested considerable assets in NIS infrastructure. Finally, when this issue is in question, Article 17 of the Energy Agreement must be kept in mind, since it provides that the termination of this agreement shall not affect the implementation of the obligations set forth in agreements concluded within the framework of the agreement while it is in force. This is exactly the case with the Agreement of purchase and sale of NIS shares.

The third and worst scenario would be that Serbia, under the pressure of the Energy Community and the EU, unilaterally terminates the application and withdraws from the agreement with Russia. The Energy Agreement is concluded for the period of 30 years and it does not stipulate the possibility of unilateral termination within the prescribed term.⁸² Unilateral suspension of its application and withdrawal from the Energy Agreement, contrary to its provisions, would be a substantial breach of the Agreement. In this case, Serbia would be held internationally responsible for failure to fulfill of the Agreement. However, responsibility under the rules of public international law would not be the only problem for Serbia. Serbian companies involved in the implementation of the South Stream gas pipeline project, primarily JP Srbijagas, would be unable to fulfill their contractual obligations to the Russian partners, and would face much more severe consequences. If that happens, it is more than likely that a series of lawsuits before national courts or international commercial arbitration would follow with the Russian companies demanding compensation for damages incurred due to failure of the Serbian companies to fulfill the Agreement.

7. Conclusion

Based on the foregoing, it can be concluded that the Energy Agreement between Serbia and Russia in its essential elements is in conflict with the obligations Serbia has to fulfill as a member state of the Energy Community. First of all, it is about obligations under the Second Energy package of the EU, which were in force at the time of signing the agreement with Russia, and which were related to legal and functional unbundling of transmission system operators, freedom of third party access to gas infrastructure and the method of tariff calculation. To make matters even more serious, Serbia has not fulfilled some of these obligations so far, although the deadline for doing so expired on 1 July 2007.⁸³ In addition, Serbia has an obligation to implement the provisions of the Third Energy Package of the EU until 1 January 2015, which was adopted by the Energy Community in the meantime. These regulations, *inter alia*, provide that the same entity cannot be the owner of the gas pipeline and gas that it transports. On the other hand, Russia is strongly opposed to the application of this rule, referring to the Energy Agreement, which stipulates that the ownership of the pipeline belongs to joint ventures established by Gazprom and JP Srbijagas. Serbia has thus found itself in a complicated legal situation in which the fulfillment of obligations towards one party leads to a dispute with the other party. Serious legal and political consequences may arise out of it, especially in the EU accession process. Apart from the danger of being found responsible for a violation of the Treaty establishing the Energy Community, Serbia may face serious problems in the negotiations on EU membership. It should be borne in mind that beside the Stabilization and Association Agreement, the Treaty establishing the Energy Community is the most important legal instrument in the process of Serbia's accession to the European Union. The pace at which Serbia moves towards EU membership will depend on the ways in which Serbia will enforce these agreements. The fact that apart from Serbia, some EU Member States have concluded similar agreements with Russia may be considered as a mitigating circumstance to some extent. But ultimately, it is a poor consolation, especially if one takes into account the special exposure of Serbia in the entire situation. Here, we primarily think of the fact that Serbia, for its participation in the South Stream gas pipeline project, has agreed to sell 51% of the NIS shares to Russia, i.e. the company which is in its majority ownership at a price based on vague criteria. The main reason for Serbia's entry into such an arrangement with Russia was the desire to provide a safe and cheaper gas supply, as well as significant revenues from gas transit route.⁸⁴ On the other hand, at first glance it appeared that certain provisions of the Energy Agreement are contrary to the rules of the Energy Community. When calculating between the potential benefits of the arrangement with Russia and consequences resulting from breach of obligations related to the Energy Community membership, Serbia consciously decided to take the risk. Now it is obvious that Serbian authorities underestimated the possible legal consequences of non-compliance of agreements with Russia and the rules of the Energy Community, as well as the determination of the European Commission to consistently apply EU regulations. Serbia is also found in the middle of an international dispute between the European Union and Russia, in a situation in which the fate of the South Stream gas pipeline, in the development of which it has invested so much, does not depend on it.

8. Recommendations

In all external activities undertaken within its jurisdiction, the authorities must ensure that Serbia consistently and in good faith fulfils its international commitments. This is the only way to increase the international credibility of Serbia, which was seriously damaged in the 1990s. By full implementation of the international agreements, not only does Serbia meet its obligations towards third countries, but it also contributes to greater legal security of its citizens. In this regard, we should not forget that ratified international agreements constitute an integral part of the Serbian legal system and that courts and state authorities are obliged to apply them. Therefore, proper implementation of these agreements is an essential prerequisite for the rule of law in Serbia.

The existing international legal issues related to the construction of the South Stream gas pipeline is another one in a series of good causes for the authorities of Serbia to open a public debate on all aspects of Serbia's accession to the European Union and the impact of this process on relations with Russia. The European Union is no longer merely an economic and monetary union, but also has political, security and military components. In this regard it should be borne in mind that, although they have developed political and economic relations, the European Union and Russia are two global competitors, which in some areas have opposing interests. Serbia, as a candidate for EU membership is expected to show loyalty to the organization which it intends to join, including the fulfillment of commitments and compliance with external actions of the European Union, in which energy security has an important place. It can be estimated that both the previous and the current Serbian governments were mostly reserved about political and security aspects of the accession of Serbia to the European Union in relation to Russia in their public addresses. After all, it arises from more than restrained responses of Serbian authorities to Ukraine crisis, of which important segments are associated with the dispute over the South Stream gas pipeline.

If Serbia has opted for membership in the European Union and successful completion of the accession negotiations as soon as possible, then it should properly and timely comply with all the international commitments it has made to this organization. It is untenable that, almost seven years after the expiry of the deadline, Serbia is still not able to ensure implementation of the Second Energy Package rules, which is an integral part of the Energy Community Treaty.

In connection with the ongoing debate between the European Commission and the Russian Government related to the South Stream gas pipeline project, Serbia should make use of all institutional possibilities offered by the membership in the Energy Community to strengthen its negotiating position towards Russia and better protect its own interests. Serbia has a special interest in revision and improvement of the Energy Agreement conditions and implementation of the Third Energy Package, bearing in mind that Serbia is the only country that agreed to minority ownership of the pipeline on its territory.

Bibliographic notes (endnotes)

- 1 The European Community ceased to exist on 1 December 2009, when the Treaty of Lisbon came into force. Its rights and obligations were transferred to the European Union.
- 2 Bulgaria became an EU Member State on 1 January 2007.
- 3 Croatia became an EU Member State on 1 July 2013.
- 4 Romania became an EU Member State 1 January 2007.
- 5 Another two states joined the Energy Community in the meantime: Moldavia on 1 May 2010 and Ukraine on 1 February 2011.
- 6 The treaty was concluded for a period of ten years, and the Ministerial Council, acting by unanimity, may decide to extend its duration (Article 97 of the Treaty). By Decision of the Ministerial Council D/2013/03/MC-EnC of 24 October 2013 the duration of the Treaty was extended for another ten years.
- 7 See: *Ugovor o osnivanju Energetske zajednice*, Službeni glasnik Republike Srbije, No. 62/06, 19 July 2006.
- 8 Ibid., Article 6,
- 9 Ibid., Article 7.
- 10 Ibid., Article 11.
- 11 Ibid., Annex I
- 12 Ibid., Article 18, paragraph 1.
- 13 Ibid., Article 18, paragraph 2.
- 14 Ibid., Article 19.
- 15 Ibid., Article 24.
- 16 Ibid., Article 25.
- 17 *Decision of the Ministerial Council D/2011/02/MC-En-C: On the implementation of Directive 2009/72/EC, Directive 2009/73/EC, Regulation (EC) No 714/2009 and Regulation (EC) 715/2009 and amending Articles 11 and 59 of the Energy Community Treaty.*
- 18 Article 41, paragraph 1 of the Energy Community Treaty.
- 19 Ibid., Article 43.
- 20 Ibid., Articles 47 and 48. The Ministerial Council is the highest body of the Community. It consists of one representative of each Associated Country and two representatives of the EU. Competence: The Ministerial Council provides general policy guidelines and adopts Measures.
- 21 Ibid., Articles 53 and 54. The Permanent High-Level Group consists of one representative of each Associated Country and two representatives of the EU. Competence: to prepare the work of the Ministerial Council, to report to the Ministerial Council on progress made toward achievement of the objectives of the Treaty, to take Measures if so empowered by the Ministerial Council and to discuss the development of the *acquis communautaire* on the basis of a report submitted by the European Commission etc.
- 22 Ibid., Articles 58 and 59. The Regulatory Board is composed of one representative of the energy regulator of each Contracting Party, pursuant to the relevant parts *acquis communautaire* on energy. Competence: to advise the Ministerial Council or the High-Level Permanent Group on statutory, technical or regulatory issues, to issue Recommendations on cross-border disputes involving two or more national Regulators and to take Measures, if so empowered by the Ministerial Council.
- 23 Ibid., Articles 67, 68, 69 and 70. The Secretariat comprises the Director and the staff that assists in carrying out the activities. The Director is appointed by the Ministerial Council. The Secretariat is independent in the performance of its duties from other bodies of the Community and the Contracting Parties. The Secretariat must act impartially, in the best interest of the Community. Competence: to review the proper implementation of obligations under the Treaty and to submit yearly progress reports on the implementation of *acquis communautaire* to the Ministerial Council.
- 24 Ibid., Article 76, paragraph 2.
- 25 Ibid., Article 89.
- 26 Ibid., Article 76, paragraph 3.
- 27 Ibid., Article 90.
- 28 Ibid., Article 91, paragraph 1.
- 29 Ibid., Article 92. Paragraph 2 of the same article envisages that the Ministerial Council may subsequently decide by simple majority to revoke a decision to suspend certain membership rights.

- 30 Ibid., Article 94.
- 31 Ibid., Article 101.
- 32 See: *Međunarodni ugovori*, Službeni glasnik RS, No. 83/2008.
- 33 Article 2 of the Energy Agreement.
- 34 Ibid., Article 3.
- 35 Ibid., Article 4.
- 36 Ibid., Article 6.
- 37 Ibid., Article 8.
- 38 Ibid., Article 9.
- 39 Ibid., Article 13, paragraph 2.
- 40 Ibid., Article 10, paragraph 2.
- 41 Ibid., Article 15.
- 42 Ibid., Article 17. After the thirty year period the Agreement shall automatically be extended for five years, unless one of the Contracting Parties notifies the other party of its intention to terminate it nine months before the said period expires.
- 43 Ibid., Article 16.
- 44 Nikolić–Kokanović–Otašević Law Office, *Pravna analiza aranžmana između Srbije i Rusije u oblasti naftne i gasne privrede*, (Beograd: ISAC fond, decembar 2009), pp. 13–14. Almost identical remarks by the European Commission of 3 June 2014 on the international agreement between Bulgaria and Russia of 18 January 2008 point to the fact that the conclusion of the authors of the legal analysis is well-founded. Key elements of the said agreement are similar to those in the Energy Agreement between Serbia and Russia. More information on European Commission's remarks can be found online: EurActiv, EU News & Policy debates, across languages, *Agreement between the Government of the Republic of Bulgaria and the Government of the Russian Federation on Cooperation in Construction of the Gas Pipeline for Transit of Gas via the Territory of the Republic of Bulgaria*, <http://www.euractiv.com/sections/energy/bulgaria-build-south-steam-despite-commission-warnings-302572>.
- 45 The author did not have access to the original text of the letter by the Energy Community Secretariat that was addressed to the Ministry of Mining and Energy of the republic of Serbia of 2010 since it is not a public document. At the request of the author, the PR office of the Energy Community Secretariat sent a letter outlining the gist of the Secretariat's remarks on the Energy Agreement. The said letter and basic remarks on the Energy Agreement can be found in the following source: Energy Community Secretariat, *Annual report on the implementation of the acquis for the years 2009-2010*, p. 95.
- 46 Bulgaria hosted the ceremony of welding first pipes on 4 November 2013. Three weeks later, on 24 November 2013, first pipes in Serbia were welded in Šajkaš.
- 47 Bulgaria signed the agreement with Russia on 18 January 2008, Hungary on 28 February 2008, Greece on 29 April 2008, Slovenia on 14 November 2009 and Austria on 24 April 2010. The agreement between Croatia and Russia was signed on 2 March 2010, when Croatia was still a member of the Energy Community. The agreements are available at MENA Chambers, *South Stream Intergovernmental Agreements*, International Energy Agreements, MENA Chambers, <http://www.menachambers.com/expertise/energy/South-Stream-IGAs.pdf>
- 48 On 21 February 2014 Deputy Director of the Energy Community Dirk Buschle called upon Russia to reach an adequate agreement with the Energy Community about the South Stream and at the same time warned it "not to waste money on a project that falls foul of EU law.
- 49 Article 22 paragraph 1 of the *Directive* envisages exemption under the following conditions: 1) the investment must enhance competition in gas supply and enhance security of supply; 2) the level of risk attached to the investment is such that the investment would not take place unless an exemption was granted; 3) the infrastructure must be owned by a natural or legal person which is separate at least in terms of its legal form from the system operators in whose systems that infrastructure will be built; 4) charges are levied on users of that infrastructure; 5) the exemption is not detrimental to competition or the effective functioning of the internal gas market, or the efficient functioning of the regulated system to which the infrastructure is connected.

- 50 Energy Community Secretariat, *Annual Implementation Report on the of the Acquis under the Treaty Establishing the Energy Community*, years 2009-2010, 10 September 2010, p. 95; *Annual Implementation Report on the of the Acquis under the Treaty Establishing the Energy Community*, years 2012-2013, 1 September 2013, pp. 88 and 119, http://www.energy-community.org/portal/page/portal/ENC_HOME/DOCUMENTS?library.category=758
- 51 Article 9 paragraph 2 of *Directive 2003/55/EC*.
- 52 Energy Community Secretariat, *Annual Implementation Report on the of the Acquis under the Treaty Establishing the Energy Community*, years 2012-2013, 1 September 2013, *op. cit.*, p. 120.
- 53 Case ECS 9/13.
- 54 The author did not have access to the response by the Ministry of Energy, Development and Environmental Protection. The gist of the response was published in the Reasoned Request of the Energy Community Secretariat, case ECS-9/13 of 24 April 2014. Energy Community Secretariat, *Reasoned Request in Case ECS-9/13, Secretariat of the Energy Community against The Republic of Serbia*, Energy Community, <http://www.energy-community.org/pls/portal/docs/3088024.PDF>
- 55 Constitution of the Republic of Serbia, Article 16 paragraph 2.
- 56 Implementation of the project includes development, financing, construction, functioning and maintenance of the Serbian section of the South Stream gas pipeline.
- 57 Agencija za privredne registre Republike Srbije, *Osnivački akt South stream d.o.o. Novi Sad*, član 3.3 i 3.4, 2. 11. 2011, sa *Izmenama i dopunama* od 31. januara 2012. godine EnterprisePublishedDocuments/4927940?code=, , <http://pretraga2.apr.gov.rs/EnterprisePublicSearch/Details/FEB36C456C9083212F6D8634ABEC73A17788E3AA>
- 58 *Ibid.*, Article 8.
- 59 *Ibid.*, Article 9.5.
- 60 "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", in *Official Journal of the European Union*, L 211/94, 14 August 2009.
- 61 Article 6 of the *Treaty establishing the Energy Community*.
- 62 Article 8 of the *Decision of the Ministerial Council D/2011/02/MC-En-C*, 6. 10. 2011.
- 63 Article 4, Paragraph 1, Item j. of the *Decision of the Ministerial Council D/2011/02/MC-En-C*, 6 October 2011.
- 64 Item 15 of the Preamble to *Directive 2009/73*.
- 65 Article 10 of the *Decision of the Ministerial Council D/2011/02/MC-En-C*, 6. 10. 2011.
- 66 *Ibid.*, Article 3, Paragraph 1.
- 67 Article 2 of the *Energy Agreement*.
- 68 Energy Community Treaty, *Report from the Commission to the European Parliament and the Council under Article 7 of the Decision 2006/500/EC*, paragraph 4.a, 10 March 2011, p. 8.
- 69 In accordance with Article 1, Vienna Convention on the Law of Treaties is applied only to agreements between countries. Bearing in mind that in this case there is a conflict between the Energy Agreement with Russia and the Treaty establishing the Energy Community, in which the EU is a party, rules of customary international law are applied to the conflict between these two agreements.
- 70 See more about this topic: Milan Bartoš, *Međunarodno javno pravo*, (Beograd: *Službeni list SFRJ*, 1986), pp. 124–133.
- 71 In this regard it should be noted that the agreement between Russia and Slovenia signed on 14 November 2009, a treaty between Russia and Austria on April 24, 2010, subsequent to the adoption of the Energy Package III. At the time of signing the agreement on 2 March 2010, Croatia has not been the member of the EU.
- 72 Judgments of the Court of Justice of the EU in the Case 26/62, *Van Gend en Loos v. Netherlands Fiscal Administration* (1963) ECR 10 and the Case 6/64, *Flaminio Costa v. ENEL* (1964) ECR 592. About the autonomy of the EU legal system in relation to international law, see more at: Obrad Racic, "The Court of the European Union: When the UN Security Council resolution on imposing economic sanctions can be applied in the legal order of the European Union" in: *Life and research: Memorial to Dejan Janca*, (Belgrade: Official Gazette, 2011), pp. 227–242.

- 73 About the importance of these principles, see more at: Vladimir Medović *International Treaties in laws of the European Union*, (Belgrade: Official Gazette, 2009), pp. 97–102.
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- 75 Case 48/71, *Commission v. Italy* (1971) ECR 529.
- 76 “South Stream pipeline project frozen over Crimea crisis”, statement of the European Commissioner Günther Oettinger, *EurActiv.com*, 11/3/2014, <http://www.euractiv.com/energy/south-stream-project-takes-crime-news-534038>
- 77 Item 19 and item 20 of the Conclusions of the European Council from the meeting of 20 and 21 March 2014, EUCO 7/1/14 REV 1.
- 78 Alberto Sisto and Stephen Jewkes, “UPDATE 1 – Future of South Stream pipeline „gloomy” – ENI CEO”, statement by Paul Scaroni, *Reuters*, 20. mart 2014, <http://www.reuters.com/article/2014/03/20/ukraine-crisis-eni-southstream-idUSL6N0MH4M120140320>
- 79 About the content and reasons for the decision of the European Commission, see the website: EurActiv, EU News & Policy debates, across languages, ‘Bulgaria to build South Steam despite Commission warnings’, *EurActiv.com*, 3. 6. 2014, <http://www.euractiv.com/sections/energy/bulgaria-build-south-steam-despite-commission-warnings-302572>
- 80 Bulgaria has suspended works on the South Stream Gas Pipeline, *RTS*, 8. 6. 2014, <http://www.rts.rs/page/stories/sr/story/13/Ekonomija/1618391/Bugarska+suspendovala+radove+na+%22Ju%C5%BEnom+toku%22.html>
- 81 *Protocol on the basic conditions of purchase by OAD Gazprom Neft shares of the company Oil Industry of Serbia*, 25 January 2008; *Agreement on sale and purchase of shares of the Oil Industry of Serbia Inc. Novi Sad*, 24 December 2008.
- 82 Article 17 of the *Energy Agreement*
- 83 This refers to the obligation of the legal and functional separation of activities.
- 84 See the announcement of the Government of the Republic of Serbia: “The Government has adopted the Energy Agreement”, *B92*, 22. 1. 2008, http://www.b92.net/info/vesti/index.php?yyyy=2008&mm=01&dd=22&nav_id=281558

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