



Country Strategy Paper 2007-2013

RUSSIAN FEDERATION

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1. EXECUTIVE SUMMARY

The main interests of the EU in Russia lie in fostering the political and economic stability of the Federation; in maintaining a stable supply of energy; in further co-operation in the fields of justice and home affairs, the environment and nuclear safety in order to combat 'soft' security threats; and in stepping up cooperation with Russia in the Southern Caucasus and the Western NIS for the geopolitical stability of the CIS region, including for the resolution of frozen conflicts.

EU cooperation with Russia is conceived in terms of, and is designed to strengthen, a strategic partnership.

At the St. Petersburg Summit in May 2003, the EU and Russia agreed to create four 'common spaces': a Common Economic Space; a Common Space of Freedom, Security and Justice; a Space of co-operation in the field of External Security; and a Common Space for Research and Education, including Cultural Aspects. A set of roadmaps towards the Common Spaces were agreed at the St Petersburg Summit in May 2005.

Progress towards achieving the Common Spaces is vulnerable to security threats; alleviating and preventing any such is a key objective of EU external action. The conflict in Chechnya has provoked widespread humanitarian problems, and the continuing crisis has threatened to tip the wider Northern Caucasus into disarray and conflict. The EU is thus concerned to support the stabilisation, recovery and ultimately the development of the North Caucasus.

Because surrounded by EU Member States, the EU maintains a particular interest in the Kaliningrad Oblast. Its objective is to ensure that the socio-economic potential of Kaliningrad and the surrounding region is fulfilled.

The EU places emphasis on the promotion of democracy, the rule of law and good governance in general, as well as respect for human rights and fundamental freedoms.

The Country Strategy Paper is based on the premise that the Common Spaces as the defining expression of EU policy towards the Russian Federation, the wider EU Neighbourhood Policy, the EU Security Strategy and its development objectives, are mutually-reinforcing; and that together they make up a robust and coherent approach to Russia.

Given current political and economic circumstances, the EU will need to work hard to maintain the pressure for the implementation of the Common Spaces. Russia is characterised by a powerful bureaucracy, a politically-biased legal system, powerful and repressive law enforcement agencies and a relatively weak civil society. Power is increasingly concentrated within the Presidential administration.

Recent economic growth in Russia has been impressive on any measure, and remains strong. A generally positive macroeconomic environment and the present current account surplus can be attributed largely, although not exclusively, to high oil and commodity prices. Yet Russia has so far neglected to use the window of opportunity provided by high oil prices to significantly diversify its economy away from the energy complex. Reform in the more recent period has slowed, and a perception of increasing State interference in the economy will have a negative effect on business confidence.

The TACIS programme has been the biggest programme of technical assistance to the Federation, worth more than €2.7 billion since 1991. The programme has traditionally been justified in terms of easing and indeed encouraging transition towards a market economy and democracy. The TACIS Programme's comparative advantage lies partly in the clear policy line which underpins it, and it has proved a usefully flexible framework for supporting Russia's transition. Since future cooperation is equally intended to support clear strategic goals – the Common Spaces – there can be some confidence that the new instrument will meet with some success, as long as not spread too thinly between sectors. More effort will have to be paid to developing interventions in a spirit of greater equality, if there is to be a greater sense of ownership on the Russian side, and coordination with remaining donors will need to be stepped up if complementarity and coherence of approach is to be achieved.

The Commission must steer a course towards meeting the objectives set out by the EU for its relationship with Russia, deploying the whole mix of policies and instruments at its disposal, including financial cooperation, in particular under the European Neighbourhood and Partnership Instrument. The ENPI includes a national allocation for Russia, as well as regional and cross-border components. Funding from the Nuclear Safety Instrument, from the Democracy and Human Rights Instrument, and from a number of thematic programmes will also be available for financial cooperation with Russia.

Funding under the national allocation is limited to €30m *per annum* over the period 2007-2010. This Paper, and the associated National Indicative Programme, describe how the strategic partnership with Russia can most effectively be supported through financial cooperation. The strategy for financial cooperation should be that of providing judiciously-selected support intended to entrench the Common Spaces. A certain proportion will be allocated to recovery/development and security objectives in the North Caucasus and in Kaliningrad.

2. THE OBJECTIVES OF EU COOPERATION WITH RUSSIA

EU cooperation with Russia is conceived in terms of, and is designed to strengthen, a strategic partnership founded on shared interests and common values.

The main interests of the EU in Russia lie in fostering the political and economic stability of the Federation; in maintaining a stable supply of energy; in further co-operation in the fields of justice and home affairs, the environment and nuclear safety in order to combat 'soft' security threats; and in stepping up cooperation with Russia in the Southern Caucasus and the Western NIS for the geopolitical stability of the CIS region.

In 1997, the EU and Russia committed to a Partnership and Cooperation Agreement, to run for an initial period of ten years. The Agreement establishes the institutional framework for bilateral relations, and sets out the principal common objectives for trade and economic cooperation across a range of sectors, for political dialogue, and, to a limited extent, for cooperation in justice and home affairs.

At the St. Petersburg Summit in May 2003, the EU and Russia agreed to create four 'common spaces' in the framework of the Agreement: a Common Economic Space; a Common Space of Freedom, Security and Justice; a Space of co-operation in the field of External Security; and a Common Space for Research and Education, including Cultural Aspects. The overriding objective of all four Common Spaces is to strengthen the strategic partnership between the EU and Russia across the broadest range of policy domains.

- The objective of the Common Economic Space is the establishment of an open and integrated market between the EU and Russia.
- The objective of the Common Space of Freedom, Security and Justice is to facilitate ease of movement between the EU and Russia, in particular for business, travel and tourism, within a context free of terrorist threat, organised crime and corruption.
- Within an international order based on effective multilateralism, the objective of Common Space on External Security is to strengthen cooperation on security and crisis management in order to address global and regional challenges and the key threats of today, notably terrorism, the proliferation of WMD, and existing or potential regional and local conflict.
- For the Common Space on Research, Education and Culture, the objective is to create and reinforce bonds between the EU and Russian research and education communities and to build on a shared cultural and intellectual heritage.

A set of roadmaps towards the Common Spaces were agreed at the St Petersburg Summit in May 2005. The roadmaps in effect set out the agenda for co-operation between the EU and Russia for the medium-term in order to make the four Common Spaces a reality. Annex 2 provides a summary of the range of policy objectives which have been set out, by the Commission in consultation with the Member States, corresponding to each roadmap.

- The EU has a particular concern for developments in the North Caucasus. In partnership with the authorities and in respect of Russian sovereignty, the objective of EC financial cooperation is to support the stabilisation, recovery and ultimately the development of the region.
- Because surrounded by EU Member States, the EU maintains a particular interest in the Kaliningrad Oblast. Its objective is to ensure that the potential for socio-economic development of Kaliningrad and the surrounding region is fulfilled.

Given its improved financial position on the back of substantial energy export revenues, its economic standing as a member of the G8, and indeed its sheer size, it would not be appropriate that poverty alleviation – to which Russia has committed itself - figure as one of the objectives of financial cooperation with the Federation. Still, EC actions which contribute to political and economic reform should ultimately help increase investment, employment opportunities and improve living standards. And the EU places emphasis on the promotion of democracy, the rule of law and good governance, as well as respect for human rights and fundamental freedoms, in line with its development policy.

Progress towards achieving the Common Spaces may at any time be undermined by security threats, putting lives at risk, endangering the environment and compromising socio-economic reform and growth. One of the key implications of the European Union Security Strategy of December 2003 is the need for the EU to promote a ring of well-governed countries surrounding the EU with whom close and cooperative relations can be enjoyed. If the regions adjacent to Russia are not stable, this will have consequences for the security of the EU itself. The conflict in Chechnya has engendered humanitarian disaster, and the continuing crisis threatens to tip the wider Northern Caucasus into disarray and conflict. The NIS region as a whole remains vulnerable to other regional tensions boiling over, putting national and even regional security at risk, particularly since the illicit availability and misuse of conventional

weapons is a problem for which the NIS region is notorious. The threats of organized crime and terrorism cannot be discounted.

The threat to safety – and indeed to regional security - posed by the continuing operation of aged nuclear plants and equipment in Russia cannot be over-emphasised. In the light of the insecure management and regulatory régime applying to the whole industry, it must remain one of the objectives of EU policy to maintain pressure for continuous improvements in this area.

Alleviating and preventing security threats of all kinds, as well as enabling states to comply with and implement their international obligations, are key objectives of EU external action. Equally, the EU and Russia share an interest in strengthening cooperation in the field of justice and home affairs in order to tackle the threat of organized crime, terrorism and other illegal activities of a cross-border nature. A balance will need to be struck by both sides between security on the one hand, and justice and freedom on the other.

The European Union has recently set out its Neighbourhood Policy for relations with its neighbours to the south and east. Russia has made clear that it should not be considered as falling under this policy. The EU has acknowledged this by establishing, in cooperation with the Federation, the quite distinct Common Spaces framework. Yet the overriding objectives contained within the Neighbourhood Policy remain highly relevant to the Common Spaces: preventing the emergence of new dividing lines in Europe; the progressive consolidation of a zone of shared stability, security and prosperity to be achieved through a significant degree of economic integration and political cooperation, and on the basis of shared values and common interests.

This Country Strategy Paper is based on the premise that the Common Spaces as the defining expression of EU policy towards the Russian Federation, the wider EU Neighbourhood Policy, the EU Security Strategy and EU development objectives, are mutually-reinforcing; and that they thus together form a robust and coherent approach to the EU relationship with Russia. This Paper, and particularly the associated National Indicative Programme for Russia, describe how this ambitious set of objectives can most effectively be supported through the financial cooperation extended by the EU to this strategic partner.

3. RELATIONS WITH THE EU AND THE RUSSIAN POLICY AGENDA

As well as being a key actor on the UN Security Council, it has significant influence on its near abroad to the West - the EU neighbourhood – and in Central Asia. Russia is also a major supplier of energy to the EU. Despite its relatively small economy, Russia is a large market for EU goods and services, with considerable potential for growth. Russia is a key ally in EU efforts to combat new threats to security, including pollution and carbon emissions, crime, illegal migration and trafficking, and terrorism.

Russia has a dense network of institutional relations with the EU. These are to some extent determined by the current Partnership and Cooperation Agreement and a series of sectoral agreements stemming from it. For the time being two Summits are organised per year, various Ministerial meetings are held on a variety of issues, and a number of technical level sub-committees have been established. However, the roadmaps to the Common Spaces – which go beyond the scope of the Agreement to a considerable extent - reflect a more up-to-date perception of common challenges, tasks and opportunities. A number of new dialogues intended to structure EU-Russia institutional relations around the Common Spaces therefore function alongside the sub-committees.

The chart at Annex 3 provides an overview of these structures. It captures current sectoral agreements with Russia, in the framework of the Partnership and Cooperation Agreement, as

well as ongoing dialogues, grouped according to Common Space. The chart therefore serves as a summary of the range of policy areas in which relations with Russia are currently entertained.

Negotiations for a new agreement to replace the existing Partnership and Cooperation Agreement should begin in 2007. The roadmaps remain, in any event, the short and medium-term instruments for the EU-Russia relationship and this is likely to be confirmed in the new agreement.

President Putin referred at the 16th EU-Russia Summit in London in October 2005 to a 'consistently strengthening partnership' with the EU. This Section briefly reviews Russian policy in those areas of most significance for the EU-Russia relationship.

3.1. The political agenda

President Putin indicated in his annual address to the Russian Parliament on 25th April 2005 his intention to bolster democracy, human rights and fundamental freedoms, to protect property rights and counter widespread corruption. Yet it is far from being the case that everyone in Russia shares the European view of what a stable, secure and prosperous Federation will involve: accountable institutions and an independent judiciary, a free market system integrated with the rest of the European economy, and a strong civil society.

Indeed, European observers tend to see state dominance of the economy – notably of oil and gas – for private interest, the corruption of the bureaucracy, increased control of civil society, and the lack of independent media. The murder of journalist Anna Politkovskaya has done nothing to allay such concerns, while recent changes in the law on NGO registration may further discourage the emergence of a true civil society in Russia. More prosaically, many observers consider that the inertia of the large Russian bureaucracy will handicap reform efforts in general.

3.2. Foreign and regional affairs

The Concept of National Security of the Russian Federation (2000), and the Concept of External Policy of the Russian Federation (2000) reflected fears of territorial disintegration and sought to prioritise the Federation's near abroad. Yet the Georgian Rose Revolution, a failure to resolve the Transdniestra dispute and eastern enlargement all seemed to demonstrate a decline in Russian influence. Moldova, Georgia, Armenia and Ukraine participate in the European Neighbourhood Policy and dream of EU membership. Azerbaijan and Uzbekistan are more interested in building good relations with the US than with Russia.

The Ukraine Orange Revolution of December 2004 has galvanised Moscow. Increases in oil prices make Russia stronger, while the EU seems a great deal weaker following its constitutional crisis (it is already clear that the Kremlin considers Berlin, London, Paris and Rome of more significance than Brussels). The EU cannot take Russia for granted.

A constitution for the Russia-Belarus union is now being drawn up, and Russia has started to devote more attention to the Single Economic Space with Belarus, Kazakhstan and Ukraine. This may be in part in reaction to the Orange Revolution, and indeed the Russian Prime Minister has hinted that the renewed emphasis is in response to the EU's eastern enlargement. While results have been mixed - Ukraine's position is ambivalent, and Belarus resists economic liberalisation - Russia's apparent objective seems to be to

create a customs union, just as the objective of the Eurasian Economic Community ('Evrases') is to establish such a union with Belarus, Kazakhstan, Kyrgyzstan and Tajikistan. Meanwhile Russia has considerably increased trade with China (largely through sales of energy and military equipment).

While Russia also offers security and military partnership through the security-oriented Collective Security Treaty Organisations (as well as through Evrazes since its merger with the Central Asian Cooperation Organisation), it is not likely to repeat the mistake of relying purely on military strength to extend its influence. In March 2005 Putin created a Kremlin department specifically dedicated to promoting Russian influence in its near abroad particularly through the exercise of its 'soft power': energy supply, trade and investment, jobs for migrant workers, cultural and linguistic influence. The signs are that the Kremlin is also getting into the game of 'creating' NGOs to counter the influence of Western-funded organisations operating in its sphere of influence.

As Russia becomes more assertive, the EU must rely on Russian goodwill, not only for its efforts to promote a ring of stable and prosperous states to its east, based on democracy and respect for human rights, but also for final border demarcation with Latvia and Estonia, and indeed for the resolution of international issues from Moldova to the Middle East. Of particular concern to the EU are the questions of Kaliningrad and the continuing conflict in the North Caucasus; as well as frozen conflicts in the neighbourhood.

The EU is concerned that the Kaliningrad exclave may skew the development of the Baltic region. At present statistics tend to indicate that employment, GDP per capita, income, wages and investment - in Kaliningrad on the one hand and in surrounding EU Member States on the other - are starting to converge. Growth is high, and trade with and through Kaliningrad is currently increasing. The Oblast is due to be granted 'Special Economic Zone' status from April 2006 (although it is not clear whether this measure is WTO-compatible). Yet it remains difficult to do business in Kaliningrad due to centralisation and bureaucracy. Once its neighbours - Poland and Lithuania in particular - start implementing substantial EU structural funds in 2007, social indicators and standards of living in Kaliningrad may once again start to diverge. Both factors would favour the present tendency to corruption and organised crime, which in turn threatens EU investors and even regional stability. The EU is also concerned by Kaliningrad's poor environmental record, particularly in terms of water pollution, and by the potential for catastrophic oil spills in the Baltic.

The North Caucasus region is characterised by flagrant socio-economic inequality, massive unemployment and a general breakdown of education and social services, in turn provoking general disaffection and disorder. A decade of conflict and instability has largely destroyed civilian infrastructure in Chechnya itself, while oil and chemical pollution and general environmental degradation pose a serious threat to human health. Low-intensity armed conflict and inter-communal tension persists, rights violations are commonplace, and the application of the rule of law is heavily restricted. Small arms and landmines will continue to pose a formidable threat to human security, life and livelihood for some time to come; civilian casualty rates are higher than in Afghanistan or Cambodia, and around a third of agricultural land is affected.¹ There has still been no effort to date to comprehensively survey the mine problem, let alone start clearance.

¹ UNICEF estimates that 500,000 landmines have been planted in Chechnya, making it one of the most landmine-polluted zones in the world; some estimates put the number of mines at six times this amount.

The EU has signalled its intention to play a beneficial role - not least through the commitment in 2005 of €20m from the EC budget to contribute to economic and social recovery – while recognising that the Russian Government must play the leading part in bringing about the peaceful and durable settlement of the conflict, and regional socio-economic recovery. The Kremlin claims to have invested some €2 billion in Chechnya alone over the past five years.

Yet it is far from clear that instability can be contained; there have been a number of terrorist incidents throughout Russia in recent years, notably the bombing of apartment blocks in Moscow and the notorious Beslan siege. The EU is particularly concerned, particularly since the events of Autumn 2005 in Nalchik, that instability threatens to spread to other parts of the North Caucasus. Given the relatively fragile hold exercised by the Russian authorities on a sprawling and multi-ethnic Federation, further regional or sub-regional conflict cannot be ruled out.

Russia supports the Non-Proliferation Treaty and cooperates with the IAEA. The Federation is a member of the Missile Technology Control Régime, of the Cooperative Threat Reduction and Global Partnership programmes, and of the G8 Global Partnership against the spread of Nuclear Weapons and Materials of Mass Destruction. National export control agencies have been strengthened under President Putin.

3.3. Justice, freedom and security

Over recent years, Russia has become a country of origin, transit and destination for migrants. More than 80% of all illegal migrants come from CIS countries, others from China, Southeast Asia and Africa. Current estimates of illegal immigrants in Russia range from 5-6 million. While this net inflow has compensated for population decline since 1989, legal immigration has been severely restricted, despite growing labour force needs. When in 2002 the Government declared immigration policy a priority, variable quotas were introduced for foreign workers, and some effort was made to draw illegal immigrants out of the shadows. (Russia has not, however, signed ILO conventions on migrant workers, preferring to conduct regularisations on its own.) A new Law on Citizenship and the Law on the Legal Status of Foreign Citizens was adopted, tightening the requirements for acquiring Russian citizenship. The net result was to tighten controls, including for citizens of CIS countries, and the immigration of mainly ethnic Russians from the CIS and Baltic States has been tailing off since 2002.

Thus more recently there have been calls for the liberalisation of Russia's immigration policy to take into account Russia's continuing demographic decline and the needs of a booming economy. Calls for an immigration policy review are intensifying. The Kremlin is reportedly preparing draft legislation to serve as the foundation of a new migration policy, which may include a large-scale amnesty. The Federal Migration Service has begun to experiment with legalising immigrant workers.

The EU and Russia are preparing the ratification of the Visa Facilitation and Readmission Agreements signed at the EU-Russia Summit in May 2006. By opening up the prospect of easier travel and contacts between Russia and the EU, while at the same time providing for a more effective cooperation against illegal migration, the agreements go to the very heart of the Common Space.

Russian legislation implementing the UN Convention relating to the status of refugees permits an asylum-seeker only 24 hours in which to make a claim. Asylum-seekers are not given papers entitling them to stay in Russia while awaiting a decision on their

claim, making them vulnerable to removal as illegal immigrants. During that period – which can last for 1-2 years – the applicant has no other legal rights and is not entitled to work or receive state medical assistance. State facilities for asylum seekers are minimal. Russia maintains observer status at the IOM, but does not appear interested in becoming a full member

Measures have been taken to improve demarcation and control of Russian borders although the long border with Kazakhstan in particular remains largely undemarcated. There is a general need to strengthen border management and controls. In December 2004, President Putin announced new measures to improve Russia's Border Guard Service, and it is expected to be fully operational on a non-conscript, professional basis by 2008.

The Government intends to modernise its passport issuing arrangements to include biometric data from 2006 onwards, and has expressed interest in developing cooperation in this field with the EU. Kaliningrad has been chosen as the first region to issue biometric passports. The new passports will not in themselves eliminate the problem of multiple identities, if corruption in passport issuing authorities is not tackled vigorously.

All recent documents and statements on nuclear security mention WMD proliferation and international terrorism at the top of the list of Russia's security concerns.

3.4. Economic policy

With the Kremlin having set the goal of doubling Russian GDP by 2010, the challenge will be to combine macroeconomic and fiscal stability with economic diversification beyond the energy sector and structural reform, indeed the wider integration of Russia into the world economy. Russia is the EU's fifth trading partner while the EU is Russia's main trading partner. There is mutual interest in closer EU-Russian economic integration in the face of the rapid economic development of China and India.

Thus the Federal Government has emphasised its desire for closer ties with the EU, and the gradual establishment of the Common Economic Space should bring closer the ultimate goal of a free trade area. Some progress is being made on various facets of the regulatory dialogue, and discussions are ongoing on agriculture, fisheries and veterinary issues. The bilateral trade agenda in the coming period will largely be determined by Russia's WTO accession – expected in the foreseeable future – and the corresponding bilateral and multilateral commitments to liberalisation.

Russian policy-makers have announced on many occasions that the diversification of the economy is one of their major objectives, and they will have to continue to pay attention to establishing a more predictable and transparent environment for business and investment. A new strategy for foreign involvement in the economy, and a new concessions policy are under preparation; Russia badly needs foreign technology and expertise. However, the risk is that the current tendency towards state control of the strategic sectors of the economy is extended to the more dynamic sectors. For the moment, those parts of the Government interested in economic reform are not in the ascendancy. The danger is that Russia falls into the trap of becoming a petro-state: an economically and technologically backward country used as a source of raw materials for the EU and China.

Energy

In 2003 the Federation approved an Energy Strategy to 2020, drawn up in consultation with and indeed to a considerable extent reflecting developments in EU energy thinking. It envisages the Government's role as being one of regulator and guarantor of an investment-friendly environment rather than as an actor on the market itself. However, commodity revenues have tempted the Government into slowing down demopolisation and reform of the Russian energy market. Reform of the gas sector in particular is slow, and the new subsoil law and a general lack of transparency are giving investors pause. There is a clear tendency towards increased state control of the hydrocarbon industry.

Russia has been a reliable supplier of energy to the European Union for some years (although the crisis over Russian gas exports, to Ukraine in particular in early 2006, caused some nervousness). Energy products represent over 60% of Russia's overall exports to the EU, equivalent to a quarter of total EU oil and gas consumption. Russia is also an important supplier of nuclear fuels to the EU. There is clear mutual interest in enhancing continental energy security and price stability.

While current energy production levels are impressive, if growth of the sector is to be sustained - and in order to ensure that it continues to shore up the Russian economy - the need for new capital has been estimated at between €60-€50 billion over the period to 2020. As well as offering a large integrated market, the EU can offer capital, and new technology - including renewable - for energy production, consumption and efficiency (Russia consumes 4-5 times more energy per unit of GDP than other countries of similar climate).

In the electricity sector, the potential for cooperation remains largely unrealised. Reform of the UES electricity monopoly, intended to create competitive markets for the production, wholesale and retail of electricity, is still under preparation. The feasibility of an interconnection of the EU and Russian electricity grids is presently under consideration. Interconnection would demand reciprocity and a level playing field with regard to market access and infrastructure, as well as environmental protection and safety standards.

The EU continues to push for the replacement of the first generation of Russian nuclear plants and for emphasis on other forms of energy. The EU is pressing for greater dialogue with Russia on nuclear safety issues and is keen to reach an agreement on the trade in nuclear materials.

Russia stands to benefit from early implementation of the Kyoto Protocol. The Protocol creates significant opportunity for cooperation and investment in energy efficiency, on which there is vast potential for improvement. The official Russian energy strategy envisages a 45% reduction in energy intensity by 2020, currently estimated to be three times that of the EU.

Transport

As a reflection of the importance of transport issues, particularly since the accession of the new, eastern Member States in 2004, the EU and Russia signed a Memorandum of Understanding in October 2005 for the creation of a Transport Dialogue structured around five working groups: transport strategies and public-private partnerships; transport security; air transport; maritime, sea-river and inland waterway transport; and road and rail transport. Emphasis is placed on the extension of the main axes of the trans-European transport networks to Russia and on other measures to improve transport flows.

In December 2003, Russia announced a Federal Programme for improving and modernising the transport system with the aim of turning Russian transport services into one of the country's main exports. The Programme combines a mix of policies and a budget of \$60 billion for the 2006-2008 period alone.

A Federal Targeted Programme for developing international rail transport corridors was adopted in 2001 (budget \$50 billion). Priorities include restructuring and liberalisation. Further electrification, the introduction of high-speed trains and the improvement of cross-border facilities and customs inspection procedures are envisaged, as well as the extension of the Trans-Siberian railway to Pusan (Korea) to provide a competitive Pacific route to Europe. An important challenge for the EU and Russia remains that of increasing the interoperability of their railway systems.

The future development of the aviation market will depend in large part on the regulatory régime to be adopted, and on airline modernisation. The latter will depend particularly on the development of the right banking, fiscal and financing frameworks, in order to allow Russian airlines access to modern, competitive aircraft. Russia has bilateral aviation agreements with nearly all Member States, while the Commission has requested a mandate to negotiate a comprehensive agreement with the Federation. Increased cooperation on regulatory convergence, industrial cooperation and market access could generate significant mutual benefit. The question of Siberian overflight charges – in the framework of the WTO accession negotiations, Russia made a commitment to phase out discriminatory charges by December 2013 - will continue to influence relations until there is the clear perspective of a solution.

If Russian roads are able to cope with expected increases in traffic volume, it will be necessary to create a framework for investment and cost recovery. Road freight operations between the EU and Russia will continue to be undertaken for the foreseeable future in the framework of the TIR transit facility system. Both the Commission and the International Road Union have expressed their concern about the level of claims, some possibly fraudulent, under the financial guarantee scheme included in the system. Russia has expressed strong interest in joining the Transit Convention, although the development of the necessary administrative and technical capacity will take some time. Another of Russia's goals is to introduce a single certificate valid for circulation of goods through a vast geographic region including also the CIS, the EU and candidate countries. For the nearer future, the simple improvement of road border crossing points and procedures, particularly with the EU, would produce an increase in trade volumes and a reduction in costs.

A long-standing EU request for reciprocal access to inland waterway transport systems (rivers and canals) by operators of both sides remains unfulfilled.

Telecommunications

The Federal Target Programme of Electronic Russia 2002-2010 - eRussia – makes clear the intention of the Government to pursue the transformation of Russia into a knowledge-based information society, as well as the full liberalisation of the telecommunications sector and the development of a pro-competitive, technology-neutral regulatory framework, enforced by an independent National Regulatory Authority. It is likely that Russia will continue to push for the interoperability of networks (including research networks) and services (including e-commerce services and electronic signatures) between the EU and Russia.

Science and technology, research and development

The President has approved the basic principles of the Russian Federation's policy in the domain of science and technology to 2010 and beyond. A number of private foundations have been established to move funding from the existing Academy of Sciences, where the focus is on the institutions and organisations, to a more researcher/team-based funding paradigm. A new IPR regime will have to be defined to encourage technology transfer to the commercial sector. Yet the Russian scientific community continues to function in a centralised manner, and changes in legislation and a review of the role of the Academy of Sciences will be necessary if cooperation is to be enhanced in the long-term.

Two objectives of EU international science and technology policy would naturally apply to the relationship with Russia: supporting European competitiveness through strategic partnerships with third countries, and engaging the best third country scientists to work in and with Europe; plus that of addressing specific problems which third countries face or which have a global character. The further consolidation of a European research area will create a vast intellectual, scientific and cultural space, allowing Russia increasingly to become part of a competitive and attractive knowledge-based economic macro-region.

In space, the Russian Government has committed the budget required to modernise its satellite navigation system GLONASS in order to be able to offer civilian services in the future. Discussions continue on increasing the co-operation between GALILEO and GLONASS to ensure maximum complementarity and interoperability, as well as the opening of additional markets for applications, the sharing of positions in international negotiations, and the participation of Russian and EU firms and organisations in GALILEO and GLONASS respectively.

3.5. Social policy

An Education Modernisation Programme was adopted in September 2001. To run until 2010, the Programme urges a long-term education reform strategy covering primary, secondary and tertiary education. Coupled with an intention to raise expenditure on education to 4.5% of GDP in 2006, the key objectives of the Programme include providing greater access to and raising the content and quality of education, as well as overall efficiency and effectiveness in a current context of current overcapacity. A further challenge will be to maintain the overall quality of education while at the same time seeking to devolve financial and management responsibility for education delivery. Although investments in education and human resources in general are on an upward trend, implementation of the Modernisation Programme has been poor so far and a revised action plan covering 2006-2010 is expected to be adopted. A new lifelong learning strategy and action plan is also being prepared, for the same period. Russia has

subscribed to the Bologna process and has shown interest in cooperation with the EU on language training.

Major structural reforms have been initiated in health, housing and other social areas. Some \$1 billion are to be allocated for HIV/AIDS treatment and prevention over the next five years.

3.6. Environmental policy

Russian environmental policy and problems have a direct impact on EU Member States and candidate countries, and there is every expectation that the significance of environmental issues to EU-Russian relations will grow.

The Russian Federation ratified the Kyoto Protocol in 2004, enabling it finally to come into force. Under the Protocol Russia has the opportunity to gain economically from international emissions trading and joint implementation projects. Russia's climate policy for the years 2008-12 will be defined by the way it decides to implement the Protocol, and how it plans to allocate and use its surplus emission quotas. While an EU-Russia Working Group on Climate Change has been established, Russia has not committed itself to participation in any global arrangement after 2012, and indeed has openly stated that if China and India are to continue to enjoy the benefits of Kyoto without taking responsibility for their own emissions, then it would have to reconsider its own approach.

Russia is the EU's most important outside source of timber. In 2004 Russia initiated a ministerial Forest Law Enforcement and Governance Ministerial Process for Europe and Northern Asia, with the aim of tackling illegal logging and trade, as well as improving forest management. A new forest code has been prepared and has been under discussion by Government and Duma for some years. The new legislation is expected to bring clarity to forestry ownership and user rights, as well as to the sharing of responsibilities between authorities, owners and users, including indigenous peoples.

Russia participates in the EU Water Initiative in Eastern Europe and Central Asia, which is designed as a foundation and catalyst for future action in the interests of an integrated approach to water resources management.

The Government has stressed the importance of the destruction of chemical weapons and the dismantling of nuclear submarines in Russia.

3.7. Conclusion

The Russian side has been slow at first to respond to EU proposals for implementation of the Common Spaces road maps, probably due, at least in part, to reluctance to move fast in areas implying political or economic liberalisation. The signs are that the EU will need to work hard to maintain the pressure for the implementation of the Common Spaces for some years to come.

4. THE POLITICAL, ECONOMIC AND ENVIRONMENTAL SITUATION

4.1. Politics and governance

Russia is characterised by a powerful bureaucracy, increasingly dominated by the Kremlin and widely seen as highly corrupt, a legal system described by some as

politically-biased, powerful and repressive law enforcement agencies and a relatively weak civil society. The human rights situation throughout Russia is of particular concern, despite international commitments entered into by the Federation, while there remain no independent Russian media to speak of. And yet Russian citizens in general are not sensitive to political or civic rights issues.

Power is increasingly concentrated within the Presidential administration. The Duma remains quiescent, and the role of the recently-instituted Public Chamber in relation to the Duma itself is unclear. Many observers express increasing concern about recent constitutional change, and the position of the judiciary in particular.

The President has announced that he will not seek a third term when his mandate expires in 2008 (which would require a change in the constitution), but the political opposition remains weak and fractious. Party political rivalry appears to be a mask for the struggle between rival clans for control of the national wealth.

4.2. The economy

Since the financial crash of 1998 the Russian economy has enjoyed high growth rates, and the macroeconomic situation is positive. Yet the economy continues to be largely dependent on the export of a limited range of natural resources, mainly hydrocarbons and metals. Just like other oil-dominated economies – some of which have experienced severe economic crisis in recent years – Russia is particularly vulnerable to external shocks due to a lack of diversification, the volatility of financial markets and capital flows, and its fragile financial services sector. The absence of a sufficiently large SME sector, combined with insufficient competition and concentration, hampers innovation and diversification.

The current wealth of the economy means that the Government is under less pressure to conduct reform. A number of market reforms have in the more recent period actually slowed down, do not go far enough – or have simply not begun. This is equally true for the weak and inefficient administration of the state itself. Russia ranks on a par with Albania on the Transparency International scale of corruption, and a 2005 INDEM report estimates that Russian business people pay \$3 billion in bribes annually.

The reduction in growth in 2004, and the forecast reductions for the coming period, are largely attributable to a slowing of growth in the industrial sectors – particularly oil and gas. Given declining birth rates, high mortality and poor health and education indicators, long-term prospects are uncertain. It is not clear that the Government has the vision to cope with the current huge inflows of cash and at the same time transform the tremendous wealth generated from Russia's natural resources into the enormous investments necessary both for public infrastructure and for economic diversification.

4.3. The environment

Over 20% of the world's fresh water resources and forests lie in Russia, and biodiversity is particularly rich across the vast areas of Siberia that remain virtually pristine. Russia's boreal forest is considered to be a major absorber of greenhouse gases.

Yet Russia faces a range of global, regional and trans-boundary environmental challenges. Russia has the world's largest forest reserves, yet sustainable forest management is threatened by illegal logging, estimated to account for over half the logging east of the Urals. Other environmental risks include those to human health from

water and air pollution (particularly in industrial and densely populated urban areas); poor management of waste (including radioactive waste); the depletion of natural resources and the loss of natural systems and biodiversity; and the drying out of the Aral Sea. A large portion of oil production is exported by tanker. Around one third of the tanker traffic from Russia through EU waters transits through the Baltic, and a strong financial incentive to use single hull vessels persists. The Barents, Black and Caspian Seas are also under threat from pollution.

5. OVERVIEW OF PAST AND ONGOING ASSISTANCE

5.1. Past and ongoing assistance

The TACIS programme has been the biggest programme of technical assistance to the Federation. More than €2.7 billion worth of projects has been implemented since 1991. The programme has traditionally been justified in terms of easing and indeed encouraging transition towards a market economy and democracy. Early support focussed more on the economic challenges of transition and restructuring. Current assistance – at levels of €50m *per annum* or more - prioritises institutional, legal and administrative reform, assistance for economic development and the private sector, and helping Russia address the social consequences of transition.

Special allocations have been made for the Kaliningrad Oblast (€25m); and for the North Caucasus (€20m). The latter programme is in addition to the €172m of humanitarian assistance granted through ECHO to this troubled region since the start of the second conflict. (Funding was also set aside for demining activities in Chechnya, but under current security circumstances it has proved impossible to employ.)

Although the allocation of funding to date has had to respect priorities established under the TACIS Regulation, it is instructive to examine past funding allocations in the light of the Common Spaces.

The broad support for public administration reform provided under TACIS has been relevant to the Common Economic Space. Annex 5 provides a diagrammatic representation of TACIS projects in this field. There have been efforts to promote regulatory convergence and to support trade (WTO membership, veterinary/phytosanitary controls, customs modernisation, intellectual property rights and investment in general).

Technical assistance and advice has been provided to the federal and to a number of regional authorities across a number of other sectors of relevance to the Common Economic Space:

- *Energy*: energy policy, technical standards; modernisation of gas and oil distribution network; electricity and power markets, utility reform;
- *Environmental issues*: environmental standards and reform (including in the context of Kyoto), energy efficiency, renewable energy and small-scale hydro power plants, oil spill safety system for the Baltic; and
- *Infrastructure*: road and port management/development; St Petersburg sewage treatment plant

For the private sector, there have been attempts to facilitate the provision of small business credit, and to support SMEs, including those with an export-orientation. There has been some support to the Russian tourism sector. More recently attention has been paid to the financial sector, banking and insurance, and to improvements in the business climate more generally.

Thus although much support in recent years has been in areas now covered by the Common Economic Space, the roadmap introduces a number of new activities which have not been funded before.

A certain number of sizeable projects have commenced in recent years of relevance to the Common Space of Freedom, Security and Justice. The presentation of these projects at Annex 6 demonstrates the rather broad range of areas in which projects have already been funded under TACIS. Such work could now be built on. TACIS-funded work on the development of immigration legislation has also taken place.

Some €7m is provided each year to support civil society organisations, including for environmental projects and activities intended to foster a culture of democracy and respect for human rights.

Rather fewer current projects relate to the Common Space of External Security, but these include activities to encourage the conversion of ex-military territories to civilian use and improve export controls on dual use items. Scoping studies have been undertaken in the non-proliferation and disarmament field. Some €18m has been devoted to the destruction of chemical weapons stockpiles, in cooperation with Member States' programmes.

For the Common Space of Research and Education, and Culture, Russia participates in a number of Community programmes, including the framework programmes for research and development, TEMPUS, Erasmus Mundus and the Youth Programme.

Cooperation under the Sixth Framework Programme for Research and Development (including INTAS) has been particularly positive across a number of areas with a bearing on competitiveness, namely materials and nanotechnologies, IT, aeronautics, space, and climate change, as well as ITER. The EC-funded International Science and Technology Centre has been instrumental in redirecting the talents of former WMD scientists and engineers to civilian purposes.

Since 1994 nearly 200 Russian universities have participated in the TEMPUS programme with an emphasis, since Bologna, on the convergence of university curricula and qualifications. With some 20 joint European projects selected for funding every year; the TEMPUS Programme has become popular in Russia. There has also been some EC support for vocational and management training and exchanges supported, like TEMPUS, by the European Training Foundation. The number of Russian students on Erasmus Mundus scholarships is reasonably high compared with other countries, although in relation to numbers in tertiary education in Russia the number could certainly be increased.

Further contributions to a common educational and cultural space have been a scholarship programme offered to staff of the Russian public administration, as well as support for the establishment of a European Studies Institute.

More than 40% of TACIS projects committed in 2005 will contribute to building the Common Economic Space, and about a quarter the Common Space of Research and Education, and Culture. (A further 15% of the assistance available will go to Kaliningrad.) Relatively little funding is intended to support the Common Space of External Security in particular.

On nuclear safety issues, nearly €100m has been committed, over the past three years alone, for safety promotion at Russian nuclear power plants, and for the management of nuclear waste (particularly in North West Russia).

Russia has also been eligible for regional cooperation, and the cross-border and neighbourhood programmes. However, Russia has been somewhat reticent to become involved on the same basis as the neighbourhood countries.

5.2. Lessons learned

A recent evaluation of the TACIS Regulation found that the Programme's comparative advantage lies partly in the clear policy line which underpins it. Since it provides large-scale funding over a long period, and it is generally possible to provide follow-up funding where desirable, TACIS has helped build real momentum for transition and reform. Since ENPI is intended to provide a flexible instrument in support of clear strategic goals, like TACIS, the new instrument should meet with some success in Russia.

But while there is evidence that TACIS advice and support for institutional and administrative reform in Russia in a number of sectors has been useful – the evaluation team has gone as far as to say that support has been ‘unfailing relevant and very influential’ – the evaluation has also pointed out that TACIS projects have tended to be stand-alone and to be dispersed too thinly. Further, they have tended to be designed according to less than rigorous analysis of the wider, sectoral context. There has been too great a focus on activities and output rather than sector goals, and too rigid an adherence to implementation rules. Such comments are consistent with the 2005 Court of Auditors Report on TACIS in Russia, which detected a tendency to imprecision in objectives stemming from problems at the identification, design and planning stage, with the Court also criticising a low level of involvement of Russian project counterparts and line DGs at design stage. The evaluation and the audit argued that poor project preparation meant that projects sometimes failed to achieve, or only partially achieved, their wider reform goals.

The Court of Auditors report has argued that the success of the TACIS Programme has been compromised, at least in the recent period, by the lack of a clear vision, shared with the Government, of desirable development for Russia. The 2000 and 2004 TACIS evaluations suggested that TACIS partner country administrations have a perception that they are not treated as partners by the Commission, with states that have made the greatest progress in economic transition, including Russia, now questioning the value of TACIS (the later evaluation has claimed that a quarter of TACIS projects score low for relevance or sustainability). The Russian administration has given increasingly clear signals of impatience with the European Commission's continuing ‘development assistance’ approach, indicating a preference for a more symmetrical relationship – an emphasis on cooperation rather than assistance.

Russian involvement in EU cross-border cooperation, neighbourhood and regional programmes under the New Neighbourhood Policy has been disappointing. This may

have been because Russia did not appreciate being treated on a par with smaller, neighbourhood states. It is anticipated that the establishment of the Common Spaces, in recognition of the Strategic Partnership, may help overcome Russian hesitations. Indeed, it is hoped that Russia will assume a leadership role, where appropriate, on regional cooperation programmes.

In the interest of greater Russian commitment to financial cooperation, attention will need to be paid to developing interventions under the national allocation in a spirit of greater equality. Russia has quite openly complained that large, international private sector consultancy teams can be slow, unresponsive and ineffective (there is a preference within the Government for policy advice and support from Member State civil servants). Often the smaller interventions, undertaken as a result of explicit Russian demand for advice or exchange, are the most effective. This is because they are not seen to be imposed, but rather as responding clearly and flexibly to Russian policy concerns. There is generally a higher commitment to the application of such policy advice at regional as opposed to federal level, and the establishment of local support offices in some regions has enabled constructive dialogue across a range of policy areas, including with other donors. Where Russia does feel itself to be a true partner, such as under the Northern Dimension Environmental Partnership, its commitment is evident, to the point of committing significant resources. One of the more successful recent projects, for the training of Central Bank personnel, entailed significant Russian co-financing.

The evaluation recommends that the sector-wide approach - negotiated in a spirit of partnership - should be adopted where possible, rather than the project approach. This would improve beneficiary commitment, impact and sustainability. (Another recommendation, at first sight paradoxical, is that micro-projects funded under grant programmes can be, if judiciously selected, disproportionately effective; the Court of Auditors also noted that the most successful projects were small ones for which objectives were clear and simple.)

The negotiation of financial cooperation with Kaliningrad, and assistance for the North Caucasus, has not been straightforward. Although the Kremlin has expressed appreciation for the solidarity shown by the EU for recovery in the North Caucasus, Russia is sensitive to any suggestion that the EU might be meddling in outlying regions of the Federation.

Commission projects in support of civil society have tended to take democracy and human rights as their ostensible focus. Yet Russian citizens are in general disappointed with the democratic experience since 1991, and see democracy as an abstract concept with little meaning for their daily lives. Experience has shown that civil society projects focussed on issues of everyday concern, in cooperation with regional government - for example in the interest of improvements in community services - tend to have the highest impact both in terms of improving services, and in involving local people in the democratic process. Efforts will need to be made, however, to reverse the tendency for a disproportionate amount of funding to be awarded to foreign as opposed to Russian civil society organisations.

Commission evaluations applying to TACIS are ongoing for interventions in the governance sector, water, transport, for the private sector, and of scholarships. Lessons may need to be learned from these and from the various project-level evaluations carried out.

5.3. Other donors

Given that Russia is not considered a developing country, there are relatively few donors. The principal ones are the World Bank and UNDP, the US and Canada, and of the EU countries, Denmark, Finland, Germany, the Netherlands, Sweden and the UK. The UN agencies work principally in the more disadvantaged, conflict-prone areas, notably the North Caucasus.

USAID's €100m *per annum* programme focuses on the private sector and on democracy and health sector interventions through NGOs (USAID is beginning to become active through civil society organisations in Chechnya, complementing the ongoing State Department humanitarian assistance programme). The Netherlands also chooses to work with and through civil society. Sweden provides assistance principally to North West Russia, including for environmental actions. Finland concentrates its work in Karelia, the Leningrad and Murmansk regions, and St Petersburg. Denmark concentrates on the regions neighbouring the Baltic, notably Kaliningrad, but also Pskov and Leningrad.

A number of donors have prioritised work on HIV/AIDS, and contribute to the Global Fund.

The UK is one of the few outside actors to work principally with the federal level. DfID focuses on four broad areas of public administration reform. Denmark too provides some support for capacity-building in the public sector.

The World Bank is also active at the federal level, particularly on the transparency and accountability of government. Of the European IFIs, the EBRD is considerably more active than the EIB. EBRD works in the financial sector, with SMEs, on energy and infrastructure projects, and with a number of municipal administrations, including municipal utilities. It places considerable emphasis on policy dialogue and reform conditionality.

Most donors have decided considerably to scale back their assistance, notably the World Bank, Germany, the UK within three years and Sweden by 2010. Canada is also considering an exit strategy. Several such outgoing donors nevertheless remain active on the humanitarian front, in particular in Chechnya and the North Caucasus.

For the North Caucasus the UN has led coordination through a 'consolidated appeals' process for humanitarian assistance and, from 2006, socio-economic recovery. A number of donors are joining in, most recently Norway. Sweden too runs a number of bilateral projects in the North Caucasus and has expressed a strong desire to coordinate its activities with those of the Commission. The European Commission has agreed to fund a secretariat for dialogue with the regional authorities on governance issues, and for the harmonisation of donor assistance in general in the region.

While the Court of Auditors suggested that coordination is too often left to the beneficiary, the TACIS evaluation noted that Russia is the only country in which there is anything like a formalised system of donor coordination. As a result notably of the DfID-funded Donor Secretariat for Civil Service and Public Administration Reform, in Moscow, there is considerable dovetailing of support for governance and public administration reform. For example, in Autumn 2005 donors waited for the outcome of negotiations between the World Bank and the Russian Government on a loan for judicial reform, before themselves deciding whether or what assistance to provide in this sector.

The Delegation calls EU coordination meetings three or four times a year, as part of a range of coordination activities fostered also by the Donor Secretariat, the UN and other bilaterals.

6. EC RESPONSE STRATEGY

A decade and a half on from transition, the EU's relationship with Russia cannot and should no longer be one of donor and recipient. The Common Spaces have been established in a spirit of cooperation and mutual self-interest, with the roadmaps setting out the agenda for co-operation between strategic partners. The EU and Russia are entering into a renewed contractual arrangement intended to provide the legal framework for a strategic partnership.

The EU seeks constructive, mutually-beneficial engagement with the progressive elements of Russian government, politics and society, within the framework provided by the PCA and the Common Spaces, while also offering support and encouragement for solving the problems thrown up by the situation in the North Caucasus.

6.1. Policy mix

Annex 3 provides a schematic representation of the relations between the Russian Federation and the European Commission in the framework of the current Partnership and Cooperation Agreement and of the Common Spaces.

EU relations with Russia draw on a large spectrum of EU policies, including external policies like the Common Foreign and Security Policy, European Security and Defence Policy and trade policy; the external aspects of EU policies such as on energy, transport and the environment; and the external dimension of freedom, security and justice policies.

By deploying the whole mix of policies and instruments at its disposal, it is the role of the European Commission to chart a course towards the achievement of EU objectives expressed through the Common Spaces. The EU thus extends to Russia a stake in its internal market, strong support for political, economic and social reform and for combating environmental and security threats, and the chance to participate in a range of EU programmes. Virtually every Commission service is involved, as well as a variety of European institutions, including Europol, Eurojust, Frontex, the European Training Foundation, and the European Monitoring Centre for Drugs and Drug Addiction. A framework is provided by the Common Spaces.

Common Economic Space

A significant proportion of Russian goods entering the Community market already benefit from the EU's General System of Preferences, while a Russian application to benefit from the GSP social preference clause is being examined. EU imports from Russia are to a large extent already liberalised, and remaining restrictions are under examination; the Common Economic Space aims to establish an open and integrated market between Russia and the EU. A series of formal dialogues are being established as *fora* for promoting the necessary changes and for identifying areas of practical cooperation (see Annex 3). Russia is encouraged to align its legislation with the EU *acquis* where appropriate and to take measures to facilitate trade in general, particularly in the context of its forthcoming accession to the WTO. European FDI in Russia is far below its potential, and Russia is encouraged through the dialogues to improve its investment climate. Customs matters are also relevant in this respect. Alongside work

on the Common Economic Space, the Commission strives for cooperation over employment and social issues in general, and where possible to encourage convergence with EU standards, in order that the social dimension of the Common Economic Space is effectively promoted. The Roadmap recognises the EU-Russia Industrialists Roundtable as the main business partner for many of the dialogues; the introduction of new technologies and a new managerial and business culture, little-by-little, is arguably amongst the best ways to help Russia transform herself.

The Energy Dialogue is intended to ensure energy security and price stability for both the EU and Russia. The idea is to build a closer energy relationship and to pursue the opening and integration of energy markets and respect for environmental standards. The Dialogue provides an opportunity to raise questions of common interest, including cooperation on energy saving, the rationalisation of production and transport infrastructures, to encourage investment and in general to improve relations between producer and consumer countries. The EU encourages Russia to ratify the Energy Charter. In the light of the Kyoto Protocol, the Commission works for a diversification of energy use in Russia and for increased energy efficiency, in production and consumption. It is EU policy to encourage Russia to decommission its first generation of reactors and to improve its management of nuclear waste. The possibility of an agreement on trade in nuclear materials is foreseen.

Environmental issues ranging across climate change, forestry, biodiversity and water are pressed in a number of dialogues and consultations with Russia (see Annex 3). Biodiversity and climate change feature amongst the four priority areas of the EU's Sixth Environmental Action Programme. Russia is an important partner in the EU Water Initiative.

The Transport Dialogue is used to discuss issues of common interest across all modes of transport and to seek the approximation of legislation where appropriate. As far as concerns infrastructure, the intention is to improve transport flows by addressing technical and administrative bottlenecks, as well as encouraging transport connections. Through the Dialogue the ground is prepared for aviation cooperation (including in infrastructure and industrial projects such as the proposed new air traffic management system, SESAR), and for the eventual conclusion and implementation of a comprehensive aviation agreement between the Russian Federation and the EU. Such cooperation depends on a solution of the Siberian overflights issue.

Cooperation is being stepped up on other issues under the Common Economic Space, including financial services, telecommunications, space activities and space launching.

Common Space of Freedom, Security and Justice

Cooperation with Russia in the area of security is increasingly close, and a number of Common Space dialogues have begun to enhance cooperation on justice and liberty issues too (see Annex 3).

The October 2005 Justice and Home Affairs Permanent Partnership Council identified a number of priority areas for future cooperation: counter-terrorism; cyber-crime (including child pornography); document security; judicial cooperation; border management; and drugs. The Action Plan on Common Actions on Combating Organised Crime, specific to the Russian Federation, signed in 2000, has now been incorporated into the road map. The EU Liaison Officers' Network established in Moscow provides a useful tool for the implementation of the Action Plan. The Europol-

Russia Cooperation Agreement of November 2003 will allow cooperation to be stepped up in tackling transnational criminal activity, including trafficking in human beings, money laundering and drugs trafficking. There is agreement on developing greater cooperation between FRONTEX and the Federal Border Security Service of Russia, as well as to explore the possibilities of an agreement between EUROJUST and the Russia Prosecutor General's Office. The EU also provides support for anti-corruption measures in Russia and for the reform of the Russian judicial system in general.

Following signature of the Visa Facilitation Agreement in 2006, visa dialogue will continue in order to examine the conditions for a mutual visa-free travel regime as a long-term perspective. A Readmission Agreement was also signed in 2006 will enhance current cooperation in migration management.

Human rights consultations with Russia have been established, and non-state actors are also consulted in this context. There is dialogue with the Council of Europe and the OSCE as regards the Federation with a view to upholding respect for internationally-agreed norms and standards.

Common Space of External Security

Work is ongoing to strengthen cooperation in the five priority areas identified in the Road Map: strengthening dialogue and cooperation on international matters; the fight against terrorism; non-proliferation of WMD (for example, the EU encourages Russia to agree that the new Member States and Acceding States be admitted to export control regime groups such as the Nuclear Suppliers Group, the Missile Technology Control Régime and the Wassenaar Arrangement); crisis management; and civil protection. Particular attention is paid to securing stability in the regions adjacent to Russian and EU borders (notably the 'frozen conflicts' in Transnistria, Abkhazia, South Ossetia and Nagorno-Karabakh). For the North Caucasus, the Commission has followed up on the EU commitment to assist Russia to resolve the conflict, expressed in the framework of the CFSP, through the North Caucasus Action Programme.

Common Space of Research and Education, and Culture

The Commission intends to create a truly inclusive European Research Area through the implementation of the EC-Russia Scientific and Technological Cooperation Agreement. Dialogues have yet to be opened under the Common Space of Research and Education, and Culture. Still, the opportunity has been extended to Russia for some time to participate in a range of EU programmes. The Framework Programme for Research and Development entails the possibility of Commission co-financing of Russian participation, as for an EU Member State, and the Seventh Framework Programme allows substantial room for third country participation in decision-making. While Russian take-up of funding available under the Sixth Framework Programme was generally satisfactory, the Commission is looking to enhance cooperation under the Seventh. Other activities include the implementation of the INTAS Programme for the Promotion of Cooperation with Scientists from the NIS, while the International Science and Technology Centre in Moscow provides weapons scientists with new opportunities to deploy their skills. Further efforts will be made to collaborate with Russia on satellite navigation through GALILEO.

In the field of education, both the EC and Russia participate in the Bologna Process, aiming to establish a European Higher Education Area by 2010. More generally, EC university programmes, Erasmus Mundus student exchanges and the Youth programmes

encourage contact with Russia's new generation. In the field of education and lifelong learning in particular, the European Training Foundation provides advice and support to the Russian authorities.

Cultural cooperation with Russia through the EC is less advanced for the time being. Still, the possibility of cooperation with Russia through the EU Culture Programme may be explored.

The EC is committed to the implementation of transit arrangements for **Kaliningrad**. Beyond the efficient handling of transit matters, the EC promotes a broad agenda for cooperation on Kaliningrad, including on socio-economic development and on common challenges such as the environment and health.

The EU calls on Russia to cooperate with the UN, the Council of Europe and the OSCE to promote stability, transparency and the rule of law in **Chechnya**, and to investigate claims of human rights abuses and prosecute those found responsible. The EU is the largest provider of humanitarian assistance in the North Caucasus, and has committed funding under the TACIS programme to assist in the recovery of the region.

The European Commission is a partner in, and has contributed financial resources from regional allocations to, the **Northern Dimension** Environmental Partnership. The Northern Dimension includes EU Member States, the Russian Federation, Norway and Iceland, and the EBRD provides both a secretariat function and significant resources. The purpose of the Northern Dimension is to strengthen dialogue and cooperation on the challenges of the area stretching from the Urals to Greenland, including the Baltic Sea, North-West Russia and the European Arctic regions, and to ensure the optimal use of public and private resources to meet those challenges.

6.2. Financial instruments

To aid the realisation of EU external policy goals, a number of financial instruments are to be placed at the disposal of the European Commission under the new financial perspectives for 2007-2013.

It is unlikely that total resources available for financial cooperation with Russia under *all* Instruments and programmes put together, national, regional, cross-border and thematic, will do much more than match previous levels of assistance under the past national allocation alone. The challenge will be to ensure that what is overall a modest allocation generates maximum impact in terms of policy objectives. Whatever impact TACIS and other instruments might have had in the past, it would be inappropriate now – given the size and recent performance of the Russian economy – to seek direct effects on economic development or social indicators as the principle objective of cooperation (except, possibly, in the cases of the North Caucasus or Kaliningrad).

6.3. European Neighbourhood and Partnership Instrument

The ENPI will be the main financial instrument for supporting the implementation of the strategic partnership with Russia. It includes a national allocation for Russia, as well as regional and cross-border components. Funding from the Nuclear Safety Instrument, from the Democracy and Human Rights Instrument, and from a number of thematic programmes will also be available for financial cooperation with Russia.

In order for these instruments to be extended to Russia, the Federation will need to accept the general provisions applying to financial cooperation with the Commission, entailing signature of the general framework agreement covering such cooperation.

National allocation

The **national allocation** for Russia will amount to €30m *per annum* (that is, less than half the average annual allocation to Russia in recent years under the TACIS Programme). This amount has been determined as appropriate for fostering policy goals, rather than as a result of the application of pre-set population or economic criteria. The overriding objective of the national allocation is to cement the strategic partnership with Russia. It will be dedicated to judiciously-selected policy advice, institutional support or other actions intended to reinforce this partnership. Actions funded in support of the Common Spaces – the centrepiece of the partnership - will respond to the corresponding roadmaps.

A certain proportion of the national allocation will be dedicated to recovery/development and security objectives – through more classical resource transfer/investment – in two regions in particular.

The objective of EC financial cooperation in the North Caucasus is to support stabilisation, recovery and ultimately the socio-economic development of the region. The national allocation will be used as far as possible to link current relief and rehabilitation activities funded under ECHO, to recovery and possibly long-term development (LRRD), especially in Chechnya.

In Kaliningrad the objective will be to ensure that the potential for socio-economic development of the Oblast, and surrounding region, is fulfilled. The significant funding that has already been allocated to the Oblast in recent years will be taken into account.

Decisions on which policy priorities under the Common Spaces should be supported by financial cooperation will arise from dialogue between the Commission and the Russian Government. The establishment of a secretariat-type structure or structures linked to the Russian administration (associated with the coordinators of the Common Spaces) would facilitate such agreement with the Commission.

Since resources are limited, actions should be prioritised according to the degree to which they are likely to make a direct contribution to the realisation of policy objectives. In order to avoid excessive dispersion of modest funding, agreement will be reached to concentrate financial cooperation on a limited number of actions. (The provision of grant finance to fund works contracts for infrastructure projects is not expected, although an exception might be made for the North Caucasus.) The Kremlin has set out a number of so-called national projects intended amongst other things to modernise the Russian economy, increase the effectiveness of the state, resolve the demographic problem, modernise healthcare, improve the quality of education, and to develop infrastructure. A number of these strategies and related Government policies are discussed in Section 3, and are of particular relevance to EU policy and objectives in Russia. Where EU objectives are similar, EU-Russia financial cooperation should, in the interests of effectiveness, seek to complement, and where appropriate directly contribute to such national projects.

Also in the interests of effectiveness, there will be an emphasis on rigorous context analysis by making use of economic analysis performed by specialist international

organisations or EU Member States, in complement to analysis performed by the Commission itself. Coordination with other donors will be stepped up, both upstream and downstream, in the interests of complementarity and coherence.

The areas corresponding to the Common Spaces in which support has been concentrated over the period 2000-2006, under TACIS and other instruments, will be taken into account in the planning of interventions, as will the degree of success of past assistance, particularly in the light of recent and ongoing evaluations.

Russian commitment will be engaged through requests to provide co-financing or in-kind contributions where appropriate, and at the very least the authorities will be expected to facilitate the implementation of actions funded. Where commitment to activities in a given sector is equivocal, funding should not be engaged.

Russia may receive support for participation in Community programmes, agencies and networks, in so far as these are open to the country.

A proportion of funding might be used to lever in loan finance, to be provided by the EIB, EBRD or other IFI, possibly through contributions to the proposed Neighbourhood Investment Fund. While in Russia it is not expected that interest rate subsidies will in general be either appropriate or necessary, they might be useful in certain, exceptional circumstances in order to leverage in IFI investments. Such cases might include those in which key EU interests are involved and in which it would otherwise be difficult to get a project started. They would be used in particular for environment projects (water and waste management or industrial pollution), energy projects (including renewable energy resources and energy efficiency) and transport projects (particularly for catalysing funds for critical infrastructures, notably cross-border measures on priority axes). When interest rate subsidies are considered, their relevance shall be considered on a case-by-case basis and care should be taken to avoid significant market distortions.

The Delegation in Moscow has extensive contacts with non-state actors. It is recognised that the involvement of civil society in financial cooperation can help underpin the development of the Common Spaces.

Cross-cutting issues such as gender, the environment, human rights and the rights of indigenous peoples and minorities will be taken into account in the design of interventions.

The general objective of the national allocation being to entrench a strategic partnership, an indicator of the success of the Country Strategy would be that policy objectives agreed under the roadmaps have been enabled through financial cooperation. Yet given the sheer size of the country, its economy and government, realistically it must be accepted that more often than not it will be difficult to directly attribute such advances to financial cooperation with the European Commission. The conviction nevertheless is that the strategic partnership with Russia should be backed by a certain level of financial cooperation in order to provide support for policy objectives that may be difficult to realise without judicious financial encouragement.

Regional programme (Eastern Neighbourhood)

Russian participation in the TACIS regional programme has been limited, and it may yet prove a challenge to ensure full Russian involvement. Recent signs have however been more encouraging, and areas eligible for support for 2007-2010 are of clear relevance to

the realisation of at least three of the Common Spaces, in particular the Common Economic Space and the Common Space of Freedom, Security and Justice. They include:

- transport, energy, and trade and investment issues;
- environmental cooperation (water – the EU Water Initiative, forests, the Regional Environment Centres, and the regional consequences of industrial pollution);
- freedom, security and justice issues (border and migration management, customs, and the fight against organised crime and drugs);
- people-to-people activities, through civil society organisations; and
- demining activities (there are economies of scale in funding activities in this area on a regional basis, thus pooling technical expertise and experience – although national-level funding is also likely to be necessary).

Some support may be possible through the regional programme to the Northern Dimension - whose objectives are compatible with those of the regional programme - and under which it is expected that particular attention will be paid in the post-2006 period to North West Russia.

Cross-border cooperation/neighbourhood programmes

A number of Russian republics and oblasts will be eligible for six of the neighbourhood programmes proposed under the ENPI: Barents and Baltic Sea; Karelia, and South-East Finland/Russia; Estonia/Latvia/Russia; and Lithuania/Poland/Russia (the latter being of particular relevance to the development of Kaliningrad). The Russian side has shown interest in the planning of the neighbourhood programmes. It is expected that the neighbourhood programmes will be of relevance to the Common Economic Space and the Common Space of Freedom, Security and Justice in particular. Four overall objectives will be addressed:

- promoting economic and social development in border areas;
- tackling common challenges in various fields, such as the environment, public health and the prevention of and fight against organised crime, including drugs (trafficking and demand reduction);
- improving the efficiency and security of borders; and
- encouraging people-to-people type contacts.

It is expected that certain programmes will contribute to the realisation of Northern Dimension objectives.

Region-wide programme

There will be an over-arching regional programme covering the whole neighbourhood, and which will also cover Russia. This programme will include a dedicated allocation for the new TEMPUS across the whole neighbourhood and Russia, as well as for a new student scholarship scheme for which Russian students will also be eligible.

The Russian side has stressed the importance for the Common Spaces of people-to-people contacts. While Russian take-up of the existing, Erasmus Mundus scholarships has not been as high as it might, academic and student exchange contains great potential for building contacts and shared understanding. Therefore an amount of €9m, which would otherwise have been included in the national allocation for Russia, has been added to the ENPI region-wide programme, more specifically to the Russian share of the allocation under that programme for TEMPUS and the neighbourhood scholarship scheme. This brings the Russian allocation for TEMPUS and for scholarships to some €27m *per annum*.

The region-wide programme will also include an allocation for TAIEX and for twinning, now also extended to Russia.

6.4. Democracy and Human Rights Instrument

The objectives of this Instrument include: enhancing respect for human rights and fundamental freedoms, supporting victims of repression or abuse, and the promotion of democracy. A further objective is that of bolstering the role of civil society in the promotion of human rights and democratic reform, and in supporting conflict prevention. Grqnt funding will be provided to civil society and international organisations, including certain UN bodies.

Projects funded through this Instrument will be of relevance to the Common Space of Freedom, Security and Justice, particularly to the aim of promoting democracy and human rights in Russia.

6.5. Nuclear Safety Instrument

Assistance will be provided in the period 2007-2013 to regulatory authorities and to nuclear operators throughout the neighbourhood region, particularly in order to improve the safety of civilian nuclear installations, and to improve nuclear waste management, storage and disposal. Given the scale of the nuclear sector in Russia, it is likely that past levels of assistance to the Federation will need to be maintained.

Assistance might be made available, for example, to help deal with the remains of the Arctic Fleet, including submarines and other nuclear vessels, which continue to pose a significant threat to security. Meeting such challenges is of great relevance to the Common Space of External Security.

The Northern Dimension may require additional resources in North West Russia to reduce the risk of nuclear pollution (including from obsolete nuclear bases and submarines).

6.6. Humanitarian Aid Instrument

For over ten years the EC Humanitarian Office (now DG ECHO) has supported projects in the North Caucasus region to help meet emergency needs arising from the war in Chechnya, with €172m allocated since 1999 for the victims of the second conflict. Present priorities include assistance to displaced people in Ingushetia and Dagestan as well as to the local population in Chechnya itself, including protection, the distribution of food and non-food items, medical care, shelter, water and sanitation, primary education, income-generation activities and various psycho-social projects. Some €500,000 has been devoted to mine awareness. Humanitarian assistance will continue to

be deployed as long as is necessary, despite difficult conditions and unless these become intolerably dangerous.

6.7. Stability Instrument

The Stability Instrument will apply principally in situations of political crisis, man-made or natural disasters. It is designed to deliver an effective, timely, flexible and integrated response to unforeseen needs until such time as normal cooperation can resume under the normal policy instruments. It is also designed to allow the Community to support measures to prevent violent conflict and to finance Community measures accompanying initiatives taken by the Council in the framework of the ESDP. Thus the Instrument may be used to provide support where there is an unforeseen window of opportunity to help avoid further conflict, or promote stabilisation.

Funding under this Instrument will be divided between short-term crisis response for operations of up to 18 months; and longer-term, cross-regional activities designed to take place under conditions of relative stability and intended to counter the proliferation of WMD and in support of the fight against organised crime more generally. Although funding is limited, actions under the Instrument for Stability may thus complement those funded under the ENPI for Russia, in particular any in support of the Common Space of Freedom, Security and Justice, the Common Space of External Security, and any designed to support recovery in the North Caucasus.

6.8. CFSP

Limited funding may also be made available under CFSP for security and stability issues of relevance to the Common Space of External Security.

6.9. Thematic programmes

Intended to support third country governments in efforts to better manage migratory flows, and to combat illegal migration and trafficking in human beings, the *Migration and Asylum* programme will be of particular relevance to the Common Space of Freedom, Security and Justice.

The programme for the *environment and the sustainable management of natural resources* may support projects in Russia supplementary to the Environment Dialogue under the Common Economic Space. Calls for proposals made under the *investing in people* programme may contribute to the achievement of certain Common Space objectives, particularly the expected call for proposals to support the fight against HIV/AIDS in Eastern Europe.

The programme in support of *non-state actors* will complement the Democracy and Human Rights Instrument, thus providing further support for the promotion of democracy and human rights under the Common Space of Freedom, Security and Justice.

Annex 1

Russia at a glance



Political

Russia is characterised by a powerful bureaucracy, increasingly dominated by the Kremlin, a legal system described by some as politically-biased, powerful and repressive law enforcement agencies and a relatively weak civil society. Indeed, civil society organisations have effectively been sidelined, freedom of expression is tolerated only within limits, and the media is forced to exercise a prudent self-censorship. The human rights situation throughout Russia is of particular concern, despite international commitments entered into by the Federation, while Russian citizens are not generally sensitive to political or civic rights issues.

The Yukos affair provides the most high profile recent example of a tendency to state intervention in the economy, its clumsy handling demonstrating the selective application of the rule of law and the absence of a truly independent judiciary. Meanwhile the Kremlin is the majority shareholder in Gazprom – a company which controls a fifth of the world's gas reserves - and seems determined to ensure that it soon has the controlling stake.

Power is increasingly concentrated within the Presidential administration. The Duma remains quiescent, and the role of the recently-instituted Public Chamber in relation to the Duma itself is unclear. The selection of members for the Public Chamber is largely oriented by the President, and it appears that a number of human rights institutions will want little to do with it. Political opposition remains weak and fractious. In a climate of apparently politically-motivated fiscal and criminal investigations, possible successors remain conspicuous by their absence, while party political rivalry appears to be a mask for the struggle between rival clans for control of the national wealth.

A decade and a half on from transition, Russia is thus some way from being a truly plural society. It ranks low on the Freedom House democracy scale. Many observers express increasing concern about recent constitutional change (for example, the nomination by the President of regional governors and the ability that the Kremlin now has to dissolve regional Dumas), and the position of the judiciary in particular. Still, the President has announced that he will not seek a third term when his mandate expires in 2008 (which would require a change in the constitution).

A decade of conflict and instability in Chechnya has hampered governance and largely destroyed civilian infrastructure. Massive unemployment and a general breakdown of social services – including education – provoke disaffection and disorder. It is far from clear that the conflict can continue to be contained, and there is some risk that it will continue to affect the North Caucasus region for some years to come, if not to worsen; there have been a number of terrorist incidents throughout Russia in recent years, notably the bombing of apartment blocks in Moscow and the notorious Beslan siege. Chechnya remains characterised by low-intensity armed conflict, severe restrictions on the application of the rule of law, continuing rights violations, compounded by the inability of media and civil society to mediate between federal authorities and their Chechen allies and the local population, tensions between communities, an absence of non-violent dispute-regulation mechanisms, all on top of flagrant socio-economic inequalities. Small arms and landmines will continue, post-conflict, to pose a formidable threat to human security, life and livelihood.

Given the relatively fragile hold exercised by the Russian authorities on a sprawling and multi-ethnic Federation, further regional or sub-regional conflict cannot be ruled out in the coming period.

Economic

Macroeconomic performance

Economic growth in the past five or six years in Russia has been impressive on any measure, and remains strong. 2005 will be the sixth straight year of strong growth after the 1998 crisis, with the average annual GDP growth rate for 1999-2004 standing at almost 6.8%, translating into a cumulated real GDP growth of almost 50%

Russia: key macroeconomic indicators 1998-2005

	1998	1999	2000	2001	2002	2003	2004	2005*
GDP, real % growth	-5.3	6.4	10.0	5.1	4.7	7.3	7.1	5.7(S1/05)
Industrial production, real % growth	-5.2	11.0	11.9	4.9	3.7	7.0	7.3	3.9 ¹ (01-10/05)
Fixed investments, real % growth	-12.0	5.3	17.4	8.7	2.6	12.5	10.9	9.9 (1-10/05)
Unemployment, %, end of period	11.8	11.7	10.2	9.0	7.1	8.9	7.6	7.6 (10/05)
Exports, \$ billion	74.4	75.6	105.0	101.9	107.3	135.9	183.5	199.7 (01-10/05)
Imports, \$ billion	58.0	39.5	44.9	53.8	61.0	76.1	96.3	96.9 (01-10/05)
Current account, \$ Billion	0.2	24.6	46.8	33.9	29.1	35.4	60.1	69.1 (1-09/05)
Current account, % of GDP	0.1	12.7	18.0	11.0	8.5	8.2	10.3	11 (1-09/05)
Inflation (CPI), 12-month % change	84.4	36.5	20.2	18.6	15.1	12.0	11.7	11.2 (01-11/05)
Fed. Govt. balance, % of GDP	-5.9	-1.4	1.2	3.0	2.3	1.7	4.4	7.6 (1-09/05)
Foreign currency debt, % of GDP	50.1	87.7	55.3	44.4	36.2	25.7	19.6	12.5 (9/05)
Forex and gold reserves, US\$ bn	12.2	12.5	27.9	36.6	47.8	76.9	124.5	168.4 (11/05)
Nominal exch. rate to US\$ (end year)	20.65	27.00	28.16	30.14	31.78	29.45	27.74	28.78 (11/05)
Nominal exch. rate to EUR (end year)		27.23	26.14	26.49	33.11	36.82	37.81	33.94 (11/05)
Real effective exch. rate, % change				18.7	3.3	3.5	7.8	9.3 (1-10/05)

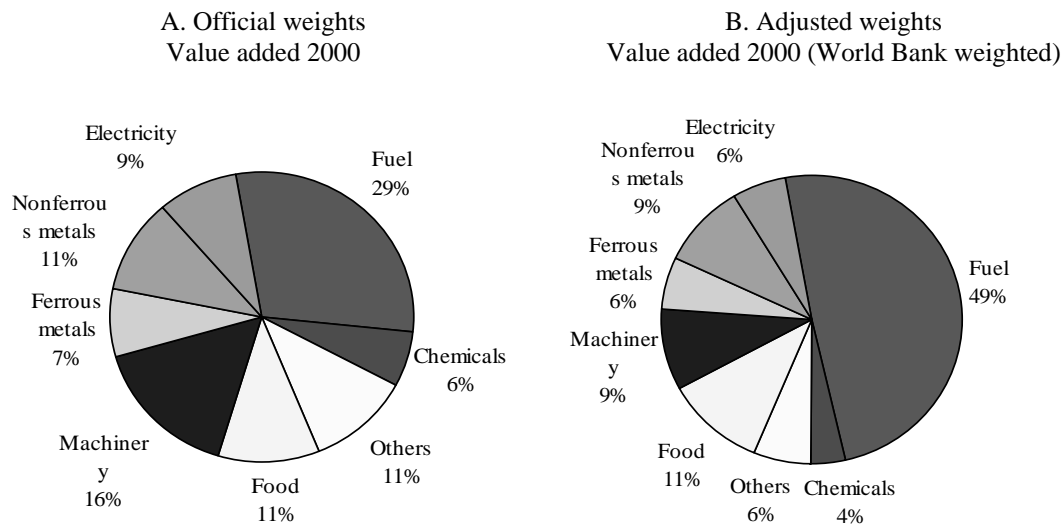
Source: various official

*Partial figures for 2005, period indicated in brackets

¹New methodology from 1 January 2005 onwards, figures for 2001-2004 revised and not comparable to previous years.

This impressive performance is to a large extent linked to the performance of the most important sector of the Russian economy, that of the export of primary commodities, in particular energy. Official Russian output data present a somewhat distorted picture of its true importance, since a large share of the value added by natural resource sectors is reflected not in the accounts of the extraction companies, but in the accounts of their affiliated trading arms. As a result export-oriented industries are under-represented in figures for industrial production, and industry as a whole is under-represented in the national accounts (while the trade and service sectors are over-represented). There have been attempts to correct these distortions. In a World Bank analysis the share of industry increases from 27% to 41%, and the oil and gas sector's share of GDP rises from around 8% in the Goskomstat data for 2000 to just above 19%. Similar estimates were produced by the Russian Ministry of Finance, which suggest that the oil and gas sector's share of GDP was around 21% in 2000, and was around 17% thereafter. At the same time, the services share drops from 60% to 46% (as for agriculture it probably makes up only around 5% of GDP). The figure below shows the structure of value added in industry by industrial sector under 'official' and adjusted weights.

Structure of industrial value added



Source: Vinhas de Souza (2005a)

Using these weights to analyse the contribution of the various production sectors to economic growth in Russia shows that the natural resource sectors directly accounted for roughly 70% of the growth in industrial production in 2001-2004, with the oil sector alone accounting for almost 45%. This implies that natural resource sectors directly contributed more than one third of all Russian GDP growth over this recent period, and oil industry alone close to 25%. These estimates include only the *direct* contribution of the oil sector to growth, and if the side effects of the oil sector (via, for instance, wages) on domestic demand are taken into account, the actual contribution of the oil industry to economic growth is even greater.

Growth resumption accompanied by a general rise in living standards and rather remarkable poverty reduction. A Russian business class has emerged, and according to the World Bank, estimates of people living below the poverty line have fallen from a peak of over 30 million people in 1999 to slightly below 12.5 million in 2002, with further falls since (total pop. 145m, on a declining trend). Yet Russia's GNI per capita amounts to only \$3,400, and millions of people still suffer energy shortages through the long winters. Russia still in theory falls within the threshold for World Bank IDA loans, although it at last graduated from the OECD's Development Assistance Committee list of aid recipients in 2005.

As shown above, the generally positive macroeconomic environment can be attributed largely, although not exclusively, to increased production and exports of energy products, high oil and commodity prices and favourable terms over the recent period. The share of the energy sector in the economy is approaching the levels of some OPEC countries, and it is estimated that taxation of the oil/gas sector now provides almost 50% of federal government fiscal revenues. Yet Russia has so far neglected to use the window of opportunity provided by high oil prices to diversify its economy away from the energy complex.

With a small reduction of private investment forecast for the coming period, and private and government consumption steady or accelerating, real GDP growth may fall to around 6% in 2005 from the 7.1% recorded for 2004 (cf. the CIS average of around 10% for the same year); and in the immediate period may fall to an average 5.5 % (according to European Commission forecasts). That growth rates are slowing despite continuing high prices of Russia's main export resources can in large measure be attributed to losses in competitiveness. A perception of increasing State

interference in the economy will also continue to have an effect on business confidence and will affect investment. Thus current growth is increasingly consumption-driven. Inflation, while substantially lower than in the mid-1990s, remains to be brought down to single figures.

Recent budgetary exercises have seen considerable increases in budgetary expenditure, including a staggering nominal planned increase of 40% in 2006 from 2005 in rouble terms, to be concentrated on military and social expenditures (particularly health care and pensions) and public sector salaries. (Note that defence spending remains a larger item than education, health and social policy put together.) On the other hand, 14% of the forecast 2006 budget is destined for infrastructure investment, up from just half that in the 2005 exercise.

To put such figures into perspective, government expenditure as a percentage of GDP at 17.5% for Russia, stands far below the EU average. The budget was in surplus for the fifth consecutive year in 2004 (with the surplus forecast at 3.2% of GDP for 2006). With debts to the IMF and Paris Club settled earlier than expected, foreign currency debt now stands at less than 20% of GDP (from a high of nearly 90% in 1999).

With record revenues coming in as a result of oil price rises, the Government has established an Oil Stabilisation Fund. Forecast to reach \$50.5 billion in January 2006 (or 6% of GDP), and expected to rise to €88 billion by end 2008, the Stabilisation Fund was originally intended to reduce vulnerability to any sudden collapse of oil prices. The Government has now decided to transfer some €2.1 billion *per annum*, from 2006, into a special Infrastructure Investment Fund. It is arguable that were public expenditure management tighter, it would be possible to make investments in public infrastructure through more effective planning of government spending.

Some progress has been made in reforming a number of core sectors, including business deregulation, land ownership, taxation and customs, trade and currency liberalisation, the banking sector and the restructuring of the power and railway sectors.

Investment climate

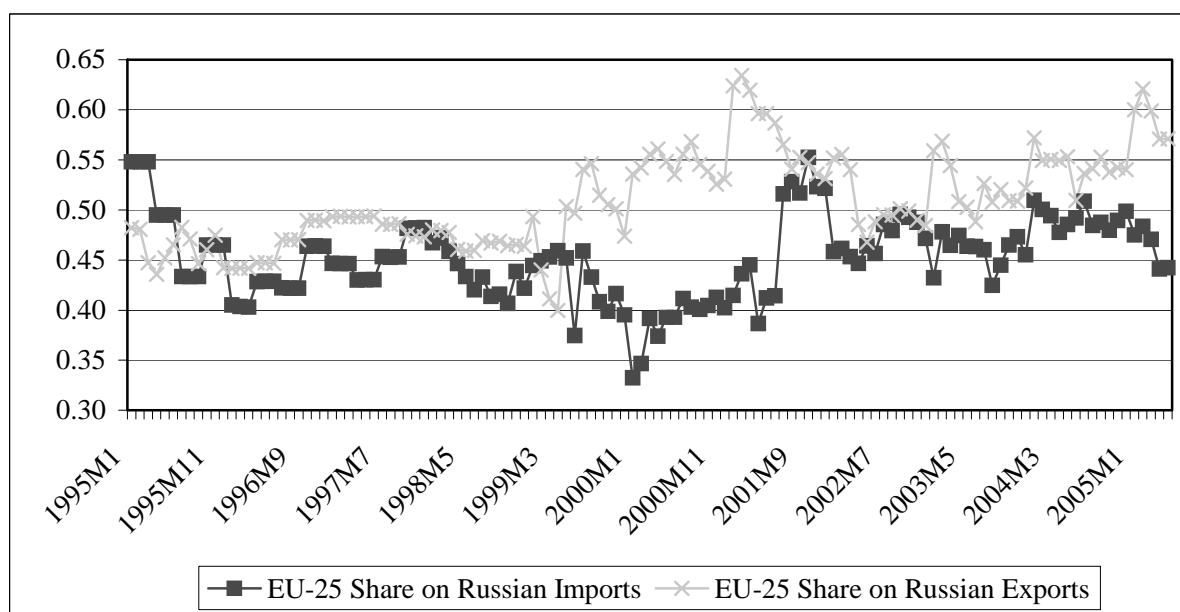
Although foreign direct investment has accelerated considerably, the accumulated stock of FDI amounts to only about 6.5% of GDP, a fifth of the average level of other Eastern European economies. The comparison with China or even Poland is stark. While investors currently active in Russia are generally satisfied with returns, there is hesitation on the part of potential new investors. Corruption continues to be a major problem, and the legal system is perceived as opaque, inefficient and politically biased. Capital flight has also been a problem.

The financial sector in general remains characterised by low levels of financial intermediation – particularly outside Moscow – and credit relative to GDP, albeit in recent years these have been growing by double digits annually. But the sector is also hampered by limited corporate governance and transparency; and, for small businesses in particular, high interest rates and limited access to finance.

Trade

Russia is a large commodity exporter and has benefited from favourable terms of trade since 2000. The EU is easily Russia's most important trading partner (followed by the CIS countries and China), while Russia is the EU's fourth most important partner. Russia enjoyed a trade surplus of some €35 billion with the EU in 2004. The EU's most important export to Russia is machinery. The EU is also the main source of technology, know-how and investment for Russia. In turn, Russia has immense natural resources and a qualified labour force. Still, the structure of Russian exports is rather unbalanced and largely dominated by mineral fuels and raw materials. Other export sectors are chemicals, agriculture and industrial products.

Over the past few years, EU-Russia bilateral trade has grown by more than 10%. Given that the majority of the new EU Member States are traditional economic partners of Russia, this trend is likely to be maintained. Examination of monthly figures for the 1995-2005 period reveals that by mid-2005 the EU-25 received close to 60% of all Russia's exports, a notable increase from the roughly 45% of the mid-1990s, and supplied 44% of Russian imports. Yet Russian imports from the EU *fell* in share terms by more than 10%, from the 55% observed in the mid-1990s: close to half of this loss can be related to China's growing importance in world markets, as this country *quadrupled* its share of Russian imports, from 2% to around 8% over the period in question. This fall in the EU share in Russian imports was not affected by the 2004 enlargement – see below.



Source: Vinhas de Souza (2005b)

Russia's accession to WTO will provide in most cases immediate non-discriminatory access to the major world markets, and should, in theory at least, spur economic reform. Russian producers will however be exposed Russia to fiercer competition, particularly in the services sector. Financial services and telecommunications are expected to undergo significant changes, with the telecommunications sector in particular needing to respond better to international trends, in particular those of the EU internal market. The need for further economic adjustment may arise in a number of industrial sectors.

The energy sector

Russia controls more than 20% of the world's known gas reserves, 5% of proven oil reserves and at least a fifth of coal reserves. The Federation is out in front as the world's largest producer and exporter of natural gas, and ties for first position with Saudi Arabia for the production and export of oil. The EU is likely to remain the dominant market for Russian energy exports: 63% of Russia's oil exports and 62% of Russia's natural gas exports go to the EU. Russia is a traditional and reliable supplier, the origin of 30% of the EU's oil imports (currently representing 27% of total EU oil consumption) and 50% of gas imports (25% of gas consumption), as well as being the EU's main supplier of uranium. EU dependence on energy imports is estimated to grow to about 70% by 2030, and Russia's share is expected to remain high.

Under the Federal Energy Strategy, oil production is set to reach 490 million tonnes in 2010 and 520 million tonnes by 2020. Gas production is planned to rise 15% on the 634 billion m³ produced in 2004, by 2020. If compared with IEA figures, Russian Government forecasts look conservative; after all, production growth has hit levels of 10% per annum in recent years (even if expected to slow significantly in 2005). Oil production amounted to some 460m tonnes in 2004, surpassing

even the low range estimate cited in the Energy Strategy. According to the Strategy, €450-600 billion will be needed to renew ageing capital stock and to sustain a planned 4-5% annual growth rate of the economy (with 30% of the required investment expected to be foreign). The IEA estimates even higher investment requirements, of around €800 billion by 2030. While these figures look daunting, by way of comparison total 2003 operational profits (before tax/depreciation costs) for the oil/gas sector in Russia amounted to some \$50 billion. Yet for the same year investment in oil exploration/production amounted to only \$5 billion. Revenues are available for investment, but they must be used wisely, and they will need to be combined with foreign direct investment; the legal framework applying to FDI in the sector must be clarified.

As it is, growth in oil and gas production is slowing, and production of crude oil may well decline in the future. In the oil sector, most of the recent growth in production has been achieved through relatively small scale investments in existing sources. Yet huge investments in oil, gas (and transport) infrastructure are overdue. A lack of large-scale investment means that oil reserves are becoming increasingly difficult to exploit, while the refinery industry will eventually be forced to respond to growing environmental, efficiency and quality concerns. In the gas sector, more than two-thirds of gas production comes from three large fields in Western Siberia. These are already depleted, with investment needed for exploration, reservoir management and improved drilling techniques. Gas flaring is another significant challenge that remains to be addressed (around 16 billion m³ of gas is flared every year according to perhaps conservative estimates).

The electricity sector suffers from serious underinvestment and ageing infrastructure. This threatens security of supply in- country and to the neighbouring regions. Reform delays threaten to make the situation worse by provoking further hesitation over investment decisions.

The share of nuclear in Russia's energy mix is likely to remain at current levels or grow slightly. The continued operation of ageing nuclear power plants, despite serious safety deficiencies, is of serious concern, as is the question of the management of radioactive waste; it is predicted that by 2007 existing storage sites will be full to capacity.

Even if the energy sector remains attractive in the short-term due to high energy prices, investor confidence has been badly dented as a result of the Yukos and similar affairs. There has been increased uncertainty since mid-2003 in business-government relations, and a fear of continued state meddling in the economy. Increasing state control of the energy and other strategic sectors may turn out to be a significant long-term disadvantage.

Transport

According to some estimates Russia will require investments of somewhere between €400-600 billion over the next 10-15 years in order to renew and maintain its ageing transport infrastructure.

The total share of goods transported by road is expected to increase substantially over the next few years from the present c. 10% to a proportion more in line with the forecast in the EU by 2010, of almost 50%.

The Russian aviation industry has some way to go before it achieves full recovery and sustainability. Most of the over 6,000 commercial aircraft do not comply with international noise standards and cannot fly to EU airports.

Social

The UNDP's recent report on Russia in 2015 highlights the key issues of regional income differentiation and remaining pockets of deep poverty, unequal access to education and social services, alarming rates of HIV/AIDS and TB as well as low life expectancy aggravated by behavioural, social and environmental factors. While it is true that absolute poverty has been

reduced, and that Muscovites' average incomes are superior to those in several capitals of the enlargement countries, it may be that some 65% of the population - the vast majority of ordinary employees, urban and rural, skilled and unskilled - while not living below the poverty line, are vulnerable to slipping below it. Meanwhile around 20 people own roughly 40% of the national economy.

According to the State Statistics Committee, the Russian population fell from 148.3 million in 1992 to 145.2 million in 2002. By 2010 the total population is expected to be less than 142 million (–6.7 per 1,000 in 2002 and –6.2 for 2003...). The last census (2002) gives 73.3% of the population living in urban areas (of which 15 million concentrated in Moscow and St Petersburg). Almost 74% of the population lives to the west of the Urals.

The fall-off in population can be put down to a low birth rate (1.1 children per woman, cf. 1.5 in the EU) combined with low life expectancy, the latter due to a failing health care system, alcoholism and the spread of AIDS. Indeed, while living standards in Russia in general are rising, health and mortality indicators have continued, at least until recently, to deteriorate. Gender-based inequalities are persistent and gender-based violence has become a significant problem, often linked to alcohol abuse. Increases in male mortality in Russia are unprecedented for modern economies, and the persistently low life expectancy for both men (58 years) and women may have a considerable impact on Russia's economic growth in the future.

HIV/AIDS has not been given the sustained priority required to blunt its spread. In addition to overwhelming the health care system, HIV/AIDS will, under a pessimistic scenario painted by recent World Bank estimates, reduce Russian GDP by up to 4.15% and 10.5% by 2010 and 2020 respectively. Citizens and officials alike remain reluctant to acknowledge the spread of the disease owing to strong social and cultural norms. HIV/AIDS still is associated with prostitution, drug use, and homosexuality or marginal populations such as prisoners.

Diseases and poisoning from heavy metals and other toxic materials, often through the water supply system, are another factor in the decline in life expectancy.

In 2003 Russia's economically active population amounted to around 71.1 million people. Ways need to be found to counter problems of unemployment (standing at an average of around 8%, ranging from 34.9% in Ingushetia to 2.1% in Moscow), underemployment, latent unemployment and secondary employment, as well as growing youth unemployment, and a burgeoning informal sector. In order to meet labour force needs in the construction, industry, the services sector and education and health sectors, Russia needs to provide sustained encouragement of lifelong learning, the reskilling of the unemployed, and in general raise the quality and competitiveness of its human resources. Yet over the period 1995-2004 enrolment in general education shrunk by 13.2%, and is expected to decrease by a further 36.4% (1995 baseline). Numbers in Vocational Education and Training are expected to contract within the range of 26-36% by 2010. Although in higher education numbers will grow until 2006, by 2010 they will have dipped by 16% (2006 base).

The recent fall in the Russian population would have been more marked had it not been for a net inflow of 6 million immigrants over the period 1989-2002. Russia in recent years has become a country of origin, transit and destination for migrants. Immigration has been made up of mainly ethnic Russians from the CIS and Baltic States, but has now fallen off. Some 378,000 migrant workers were legally registered in 2003, yet there are an estimated 3.5 million illegal migrants in Russia, equivalent to around 6% of the total work force.

Annex 2

The implementation of the roadmaps to the four Common Spaces – summary of objectives

COMMON SPACE ONE	OBJECTIVES
Trade and economic cooperation	
<i>Regulatory dialogue on industrial products (standardisation, technical regulations and conformity assessment procedures)</i>	Development of harmonised and compatible standards, regulations and conformity assessment procedures, where appropriate, including through enhanced regulatory dialogue and cooperation between responsible institutions and a reinforcement of the institutional capacities.
<i>Public procurement</i>	Development of transparent, competition-based systems of public procurement at all levels including mutual access to tender databases
<i>Intellectual, industrial and commercial property rights</i>	Improvement of the legislative and law enforcement systems for the protection of intellectual, industrial and commercial property rights in order to enhance competitiveness and improving the investment climate through the approximation of regulatory systems with the highest international standards and agreements
<i>Competition</i>	Approximation of competition legislation systems and strengthening of implementation of competition policy of the sides
<i>Investment</i>	To improve the investment climate, including by ensuring transparency, predictability and simplification of regulation and its application; to promote and facilitate two-way investments
<i>Enterprise policy and economic dialogue</i>	The development of in-depth dialogue on economic reform and enterprise policy, including an exchange of information on economic issues and policies, aiming at the improvement of the framework conditions for economic operators and their competitiveness, including dialogue in industrial policy
<i>Interregional and cross-border cooperation</i>	Deepening and diversification of interregional cooperation
<i>Financial services (banking, insurance, securities)</i>	To ensure <i>inter alia</i> the stability of the financial system, support consolidation of a sound financial sector and an effective system for protection of financial services consumers through improvement of the legislative base, effective supervision and implementation in accordance with the highest international standards and norms, applicable to financial service suppliers
<i>Accounting/auditing and statistics</i>	Enhance the transparency of the economy and share-holder protection, create favourable conditions for investment by implementation of the highest international standards and norms in these areas and give economic actors access to the necessary statistical information
<i>Agriculture, forestry, timber, fisheries, sanitary and phyto-sanitary measures</i>	To intensify cooperation to promote regulatory convergence in agriculture, notably with regard to issues related to sanitary and phyto-sanitary measures and animal health and welfare
Trade facilitation and customs	To facilitate, to standardise and to automate procedures, connected with external trade, including transit operations; to increase the parties' capacity to combat fraud, smuggling and other irregularities; to improve consultation mechanisms of the trading community on its needs with regards to the development and implementation of trade facilitation measures, with particular attention to small and medium enterprises
Networks: telecommunications and transport	
<i>Telecommunications, information society and e-business</i>	Co-operate towards the creation of a common EU-Russia Information Society area
<i>Transport</i>	To intensify cooperation, through a structured dialogue on issues of common interest in the <u>transport field</u> , with a view to promoting the complementarity of the Russian and EU transport

	sectors and gradual integration of transport networks, removing technical and administrative bottlenecks and ensuring transport infrastructures' interoperability by way of approximating respective legislation
Energy	<u>To intensify EU-Russia co-operation, in the framework of the EU-Russia Energy Dialogue; with particular emphasis on addressing issues related to the sustainability and continued reliability of the production, distribution, transportation and use of energy, including energy efficiency, energy savings and the use of renewable energies.</u> In order to reach these objectives, it is important to promote and protect investments in the energy sector, to facilitate the improvement of the investment climate, promote regulatory convergence and a high standard of environmental protection
Space	To build an effective system of cooperation and partnership between the EU and the Russian Federation in the following fields of space activities: - Access to Space: Launchers and Future Space Transportation systems; - Space Applications: Global Navigation Satellite Systems (GNSS); global monitoring by satellites and satellite communications (see also section 3.1.) - Space exploration and the use of the International Space Station (ISS) - Space Technologies Development
Environment	Promote respect of the environment and commitment to international environmental agreements, such as the United Nations Framework Convention on Climate Change and the United Nations Convention on Biological Diversity, and regional conventions, such as the UNECE Convention on the Protection and Use of Transboundary Watercourses and International Lakes, in order to foster sustainable development, with particular emphasis on stepping-up cooperation on climate change and the marine environment. Environmental issues should be integrated into and 'mainstreamed' in all sectors.
COMMON SPACE TWO	
OBJECTIVES	
Freedom	
<i>To facilitate the movement of persons/readmission</i>	In accordance with the St. Petersburg Joint Statement: a) <u>conclude ratification of agreement on visa facilitation and agreement on readmission</u> b) continue and intensify the visa dialogue at expert and political level to examine the conditions for a mutual visa-free travel regime as a long-term perspective.
<i>To cooperate on border issues</i>	a) <u>demarcate borders</u> between the EU Member States and Russia that are presently not demarcated, according to international standards, following signing and ratification of pending border agreements b) intensify discussions on border management , including border protection, and continue to support improvements of border crossing points, notably on the common border, and to improve cooperation between units on the common border c) discuss issues of common interest in relation to the strengthening of Russia's southern border d) explore the possibilities of cooperation at operational level, where appropriate, between the EU and Russia in the framework, principally of the EU's border management agency e) develop cooperation projects to step up the efficiency of border management, by strengthening the institutional and administrative framework and the capacity to implement border controls as well as improving border surveillance

<i>To support an efficient migration policy</i>	<ul style="list-style-type: none"> a) implement the Protocol against the Smuggling of Migrants by Land, Sea, and Air, supplementing the UN Convention against Transnational Organized Crime assess jointly the scale of illegal migration by exchanging information of migratory flows b) exchange information on migration management policies and best practices, and cooperate as appropriate in this field in relation to third countries c) develop an appropriate legislative framework related to migration management d) provide appropriate support to the Border Guards Service with the possibility to set up Joint Training Programmes and Training Centres for Customs Officers and Border Guards e) examine the possibility of cooperation projects to improve the management of migration flows, including the assessment of statistics and measures to fight against illegal migration
<i>To develop cooperation in the field of asylum policy</i>	<ul style="list-style-type: none"> a) implement the 1951 UN Convention relating to the status of refugees and i.a. its 1967 Protocol, including the right to seek asylum and respect for the principle of 'non-refoulement' by all countries in accordance with UNHCR recommendations b) implement standard procedures relating to treatment of asylum applications, in accordance with UNHCR recommendations c) protect individuals in the territory of EU Member States and Russia against possible threats to their life or freedom on account of race, religion, nationality, political opinion or membership of a particular social group d) not to subject permanent residents in EU Member States and Russia to expulsion contrary to the principle of 'non-refoulement'
Security	
<i>To intensify EU-Russia cooperation in the field of counter-terrorism, and to identify ways to work together to prevent and combat terrorism</i>	<ul style="list-style-type: none"> a) <u>implement the Joint Statement on the fight against terrorism</u> adopted at the EU – Russia summit in November 2002, and regularly review its implementation in existing appropriate EU-Russia formats b) sign, ratify and implement all 12 UN counter-terrorism conventions and protocols; fully implement relevant UN Security Council resolutions, including UNSCR 1373, 1540, 1267 and 1566 c) pursue efforts to seek the early finalisation of the draft UN Comprehensive Convention against international terrorism and to sign and ratify the International Convention Against Acts of Nuclear Terrorism d) continue to cooperate within the Council of Europe including by finalizing and implementing the draft European Convention on the Prevention of Terrorism e) develop cooperation including through exchange of know-how and typologies / models to strengthen the fight against the financing of terrorism, including by freezing of funds and other terrorist assets, in accordance with the relevant international instruments f) exchange legislation models in due course on the fight against the financing of terrorism, including on the abuse of non-profit/charitable sector and the confiscation of assets g) <u>implement the agreement on cooperation between Europol and the Russian Federation</u> signed in Rome on 6 November 2003, in order to enhance cooperation to fight terrorism h) enhance cooperation in all relevant international and regional fora to improve the capacity of third countries to fight terrorism i) cooperate fully in the fight against terrorism, in accordance with obligations under international law, in order to find, deny safe haven and bring to justice, on the basis of the principle to extradite or prosecute, any person who supports, facilitates, participates, or attempts to participate in the financing, planning, preparation, or commission of terrorist acts or

	<p>provides safe havens (this point equally applies to asylum in 1.4)</p> <p>j) discuss within existing structures specific measures to fight against international terrorism in new areas, such as the use of internet for terrorist purposes and recommendations for selfregulation of mass media</p> <p>k) explore the possibility of an EU-Russia agreement on Mutual Legal Assistance, based on the experience gained from the implementation of the Second Additional Protocol to the 1959 European Convention</p> <p>l) consider the possibility of a Memorandum of Understanding on the fight against terrorism between EU and Russia, taking account of the Joint Statement of 2002 on the fight against terrorism</p>
<i>To improve the security of documents, and prevent the use of multiple identities, and falsified/stolen documents, which authorise the crossing of borders (travel documents)</i>	<p>a) discuss at expert level how the security of travel documents can be improved</p> <p>b) promote cooperation, including through exchange of experience, on possible measures to stop the malpractice of multiple identities in regard to the production, control and storage of documents</p> <p>c) apply legislation and rules to support criminalisation of the use of multiple identities</p> <p>d) explore the possibility of using the Interpol database on lost and stolen blank and issued travel documents (ASF-STD) by national law enforcement agencies, in accordance with the Interpol Constitution, and to transfer data currently contained in national databases about lost and stolen, issued and blank travel documents to the Interpol database</p> <p>e) exchange information about the introduction of biometric features in travel documents, based on ICAO standards</p>
<i>To combat transnational organised crime</i>	<p>a) <u>implement the EU-Russia Action Plan on Organised Crime and agreed priorities</u></p> <p>b) implement the UN Convention against Transnational Organised Crime and the relevant Protocols that have entered into force</p> <p>c) expand and intensify the use of the EU-Russia Liaison Officers' network</p> <p>d) <u>implement the agreement on cooperation between Europol and the Russian Federation</u> signed in Rome on 6 November 2003, in order to enhance cooperation to fight organised crime</p> <p>e) prepare for the next Europol/Russia agreement to include data protection enabling the exchange of personal data (this point equally applies to fight against terrorism in 2.1)</p> <p>f) <u>as an important step towards an Europol-Russia operational agreement, ratify and implement the Council of Europe Convention from 1981 for the Protection of Individuals with regard to Automatic Processing of Personal Data</u> (this point equally applies to fight against terrorism in 2.1)</p> <p>g) increase the exchange of information related to terrorism and organised crime between EU Member States and Russian law enforcement agencies as well as Europol within the existing legal framework, e.g. by using the EU-Russia Liaison Officers' network as an intermediary step before the conclusion of an operational agreement between Europol and Russia.</p> <p>h) develop cooperation based on the contact points established in Eurojust and the General Prosecutor's Office of the Russian Federation</p> <p>i) establish reliable channels of information exchange between competent services of the Customs of the EU Member States and Russia coordinated by the European Anti-Fraud Office to improve coordination and increase effectiveness of joint efforts</p> <p>j) build up the capacity of law enforcement authorities by developing structures and procedures for improved information exchange in crime investigations through organising remote access to information resources using the Interpol network</p>

	<p>k) cooperate in new crime areas, e.g. Information and Communication Technology related crime, in particular child pornography</p> <p>l) invite each other to participate in bilateral law enforcement operations organised by individual EU Member States or Russia</p> <p>m) foster cross-border cooperation with neighbouring Member States, by promoting national interservice cooperation between different ministries and law enforcement agencies, starting with regions with intensive border traffic</p> <p>n) explore the possibility of using the working practices of the Baltic Sea Task force to improve in particular operational law enforcement cooperation between the EU and Russia</p> <p>o) explore the possibility to sign, ratify and implement the UN Protocol against illicit manufacturing of and trafficking in firearms, their parts and components and ammunition, supplementing the UN Convention against Transnational Organised Crime</p> <p>p) improve the legal framework regulating the acquisition and possession of firearms</p> <p>q) exchange information, through Europol, to prevent activities of organisations, groups and/or individuals involved in international terrorist and organised crime activities</p>
<i>To promote a comprehensive anti-money laundering regime</i>	<p>a) improve relevant legislation and regulations as well as their effective implementation, taking into account recommendations from specialised and regional organisations</p> <p>b) continue to provide support for the training of judges, prosecutors, customs officers, law enforcement staff and other concerned professionals</p> <p>c) promote the effective functioning and interaction of Financial Intelligence Units (FIU) of the EU Member States and the Russian Federation, including on the basis of bilateral interagency agreements, in line with relevant FATF and Egmont Group standards</p> <p>d) explore possibilities for enhanced exchange information about suspicious transactions between the FIUs of the EU Member States and the Russian Federation taking into account the necessary requirements on confidentiality and data protection</p> <p>e) support a FATF style Euroasian group to assist in tackling criminal money laundering and financing of terrorism in conformity with international standards</p> <p>f) exchange legislation models on money laundering to improve legislation to ensure effective identification, freezing, seizure and confiscation of proceeds of crime, property, equipment or other instrumentalities used in or destined for use in offences as well as to promote effective cooperation in this field, and exchange experience on investigation, prosecution and other relevant legal proceedings</p> <p>g) cooperate within FATF and between relevant EU Member States and Russian authorities to fight money laundering through off-shore zones</p> <p>h) explore possibilities to develop a best practice paper on mechanisms for cooperation within the FATF and FATF Style Regional Bodies, such as Moneyval, that would promote cooperation between supervisory authorities to prevent the use of the financial sector for laundering of profits received from crime through the exchange of information on structures of beneficial ownership, the owners of credit and financial institutions, and violations by the credit and/or financial institutions of anti money laundering and related legislation</p>
<i>To tackle the narcotic drug problem (including the supply and trafficking of drugs, the prevention of diversion of precursors and drug demand prevention and harm reduction)</i>	<p>a) cooperate within international and regional fora, as regards production and transit countries, paying particular attention to trafficking routes</p> <p>b) promote international and internal efforts, and coordinate activities within existing fora and particularly the UN framework, to combat the global drug threat and drug trafficking, inter alia through the signature and ratification of relevant international agreements</p> <p>c) <u>increase cooperation in the field of combating illegal drug trafficking based on the</u></p>

	<p><u>agreement between Europol and the Russian Federation</u>, notably through the exchange of experience, as well as statistical and other information.</p> <p>d) develop cooperation to fight drug trafficking, including the production and traffic of synthetic drugs and precursor's diversion, in particular within the Paris Pact Process and the framework of the Europol-Russia agreement, and in accordance with the United Nations Convention against illicit traffic in narcotic drugs and psychotropic substances 1988</p> <p>e) work together in existing formats, as well as in and through international fora to combat the drug threat originating from Afghanistan, through strengthening the capacities of the states directly bordering with Afghanistan and main states of transit, in cutting short smuggled supply of Afghan drugs abroad and precursors for their production. Pay attention to the tasks of revealing and cutting short activities of transnational criminal groupings involved in illegal trafficking of Afghan drugs, as well as of providing assistance to the Afghan law enforcement structures</p> <p>f) conduct exchange of experiences on reduction of demand for drugs, including the prevention, treatment and rehabilitation of drug addiction, paying particular attention to high-risk groups so as to prevent the spread of HIV/AIDS and other diseases</p> <p>g) promote the work of relevant NGOs to tackle social aspects of the drug problem, including prevention and rehabilitation of the victims of drugs addiction</p> <p>h) exchange information on data collection and drug information systems between the Federal Service on the Control over Traffic in Narcotic Drugs of the Russian Federation, the Ministry of Public Health and Social Development of the Russian Federation and the European Monitoring Centre on Drugs and Drug Addiction</p> <p>i) exchange information on relevant legal instruments in the field of control over the traffic in narcotic drugs and their use</p> <p>j) consider cooperation to train personnel of relevant law enforcement authorities of Russia and the EU, including study programmes and joint seminars</p> <p>k) encourage, where appropriate, operational projects between national law enforcement agencies to fight illegal drug trafficking across state borders including through the use of the control delivery techniques, to suppress illegal transportation channels and to disrupt criminal activities in this field</p>
<i>To combat trafficking in human beings</i>	<p>a) promote cooperation in international and regional law enforcement operations to combat trafficking in human beings, especially in women and children</p> <p>b) promote information exchange between Europol, interested Member States and Russia as regards trafficking of human beings</p> <p>c) implement the UN Protocol against trafficking in persons, especially women and children, including adoption of further legislation to support the fight against trafficking in human beings</p> <p>d) provide potential victims of human trafficking with reliable and easily available information to raise their awareness on risks and threats of illegal migration, and possibilities of legal migration, as well as mechanisms of assistance to victims</p> <p>e) cooperate with relevant NGOs, other relevant organisations and other elements of civil society in prevention of trafficking in persons and, in appropriate cases, in assistance to and protection of victims of trafficking in persons</p> <p>f) provide necessary professional skills to relevant authorities via specialized training, aiming at appropriate assistance to victims of trafficking</p>

	g) exchange regularly statistical data to assess the scope of the problem
<i>To fight corruption</i>	a) sign, ratify and implement UN and Council of Europe conventions on corruption , including ratification and implementation of the UN Convention against Corruption b) participate in anti-corruption work, and to cooperate on the fight against corruption within the Council of Europe, including through participation in work in GRECO once the Council of Europe Criminal Law Convention on Corruption has been ratified c) cooperate with relevant elements of civil society to fight corruption d) exchange experience in the field of the fight against corruption, and take additional measures through further incorporation of anti-corruption elements in national legislation and practices
<i>To fight trafficking in stolen vehicles and items of cultural and historic value</i>	a) improve measures to detect vehicles with altered VIN or forged vehicle registration documents, i.a. by using the Interpol Automatic Finding System , to prevent the possibility of registration and customs clearance of vehicles which are stolen, misappropriated or lost b) develop cooperation with a view to improve procedures of return of seized stolen vehicles to legal owners c) develop cooperation in combating illicit trafficking in items of cultural and historic value d) promote exchange of information on legislation on combating illicit trafficking in items of cultural and historic values and the exchange of experience to counter this crime as specifically mentioned in the Europol-Russia agreement on cooperation
Justice	
<i>To contribute to the efficiency of the judicial system</i>	a) cooperate, including through exchange of experience, on judicial reform in order to ensure the independence and the effectiveness of judiciary in the EU Member States and Russia based on the rule of law b) organize professional training for contact points, judges, prosecutors and law enforcement officials, as appropriate c) make efforts to invite each another to workshops on justice organized by EU and Russian structures d) examine the possibility of cooperation projects aiming at strengthening the judiciary
<i>To enhance cooperation on criminal matters</i>	a) develop cooperation based on the contact points established in Eurojust and the Russian General Prosecutor's Office , and explore the possibility to establish a wider network of contact points on mutual legal assistance and judicial co-operation , in order to co-ordinate proceedings related to cross-border offences b) explore the possibility to conclude an agreement between Eurojust and Russia c) promote the early entry into force of international instruments of particular importance in combating organised crime d) cooperate with a view of bringing the legislation of the EU Member States and Russia in compliance with the provisions of the Rome Statute of the International Criminal Court
<i>To develop cooperation on civil matters</i>	a) promote nomination of central authorities, and exchange experience between them, as regards legal assistance in civil matters according to the Hague Convention on Taking of evidence (1970) and implement the Hague Convention on Service of documents (1965) b) promote cooperation in protection of rights of children , including by exploring the possibility to accede to international conventions and protocols on i.a. inheritances, enforcement of maintenance decisions, as well as abductions and parental responsibility c) explore the possibility of an EC-Russia agreement on judicial cooperation in civil matters

COMMON SPACE FOUR	OBJECTIVES
Research	
<i>In order to intensify the dialogue in the field of research and development launch Permanent Partnership Council in the short-term</i>	
<i>Implement the renewed Science and Technology Cooperation Agreement</i>	<p>The Joint Committee is expected to address the following issues:</p> <ul style="list-style-type: none"> - Overseeing and promoting the activities envisaged under the Agreement; - Making recommendations; - Proposing activities; - Advising the Parties on ways to enhance cooperation consistent with the principles set out in the Agreement; - Providing annual reports on the status and effectiveness of cooperation undertaken under the Agreement; - Reviewing the efficient and effective functioning of the Agreement including the regional aspects of cooperation.
<i>Pursue on a regular basis an expert level interaction through working groups to enhance science and technology cooperation between the European Commission and Russia</i>	
<i>More effectively use available and appropriate mechanisms of interaction (PCA institutions, EC Framework Programmes (INTAS, ISTC, TACIS and EUREKA and the Russian federal research programmes) to accomplish the objectives of Common Space Four in the field of research and innovation</i>	
<i>Implement a range of measures to facilitate cooperation in research and innovation</i>	<p>Through utilization of the mechanisms mentioned above, implement the following measures:</p> <ul style="list-style-type: none"> a) Identify jointly areas of the thematic priorities in the EU Framework suitable as specific fields of cooperation b) Determine main short- and medium-term research tasks for each agreed field of cooperation included in the EU Framework Programme and elaborate a plan of practical actions c) Develop and implement measures to support the participation of Russian research oriented organisations or scientists in EU/Russia cooperation in research and innovation, in particular within jointly agreed fields and in on – going projects (IPs and NoEs) , including through Russian funding for participation of Russian research actors d) Identify prime actions including in particular the availability of timely information for the remaining period of FP6 aimed at strengthening proposal submission with Russian participation in order to favour a positive evaluation : <ul style="list-style-type: none"> i. Establish an effective information exchange and analysis of Russian participation in the calls for proposals and further implement projects of the current and future Framework Programmes;

	<ul style="list-style-type: none"> ii. Enhance the effectiveness of the participation of National Contact Points of Russia in the existing network of NCPs in particular through the current INTAS ININ activity; iii. Encourage integration of leading Russian research institutions and teams in European research networks; iv. Promote networking and access to the electronic services between research libraries and data archives; v. Integrate the work of researchers (through the 6FP, INTAS, ISTC, EUREKA etc.) to achieve common objectives in the identified fields and also related in environment civilian security and non-proliferation, with an emphasis on the promotion of scientific excellence. <p>e) Encourage the Russian participation in the preparatory consultative process for FP7 that is currently open, with a special emphasis on its international dimension and development of appropriate instruments to support EU/Russia cooperation</p> <p>f) Review all issues regarding supporting measures to increase the mobility of researchers and students:</p> <ul style="list-style-type: none"> i. Identify fields of specific mutual interest to enhance mobility; ii. Consider the instruments of coordination and the mechanisms of consultations in this field; iii. Make recommendations for an improved and enhanced use of existing instruments to support mobility of both Russian and EU researchers iv. Facilitation of visa issuance by the EU MS for Russian researchers, using the flexibilities within the Schengen acquis and on the basis of reciprocity by Russia for European researchers; v. Promote the participation of EU-based researchers in Russian programmes
Education	
<i>Encourage integration and closer cooperation within the framework of the European Higher Education Area in accordance with the main provisions of the Bologna Process</i>	<ul style="list-style-type: none"> a) Stepping up university cooperation between Russia and European Union; b) Promoting student and teacher mobility between the said universities; c) Assisting in training Russia's national promoters of the Bologna Process; d) Support of cooperation aimed at a closer link of awarding degrees by encouraging collaboration at the masters level and awarding joint or double diplomas; e) Cooperation in the setting up in Russia of a system of monitoring and check-up of the quality and certification (accreditation) of curricula and higher education institutions as a whole; f) <u>Provision of the Russian participation in the Erasmus Mundus Programme;</u> g) <u>Investigating means of promoting studies and training in Russia in the field of European Union law, EU economy, EU general and interdisciplinary studies, including training and retraining for government officials and post-graduate students;</u> h) Investigating means of reciprocally promoting Russian studies and Russian language in the EU and EU languages and studies in Russia at the appropriate level of competence.
<i>Encourage closer cooperation in the field of non-formal education for young people</i>	<ul style="list-style-type: none"> a) Promoting youth exchanges between Russia and the EU; b) Promoting cooperation between youth organizations and youth leaders from Russia and the EU;

	c) Promoting exchange of information and know how between youth organizations and youth structures.
<i>Promote the development of life skills education programmes for youth (on smoking, physical exercise, drugs, alcohol, HIV/AIDS etc.)</i>	a) Exchange of information, expertise, and best practices through joint seminars and work shops between the Russian Federation and the EU; b) Human capacity building through seminars and twinning programmes between the Russian Federation and the EU.
Culture	a) Assessing the possibility of developing a cooperation programme within the framework of the relevant EU external relations instrument, which could include <i>inter alia</i> : <ul style="list-style-type: none"> the promotion of artistic and cultural projects with a European dimension (festivals, master classes, exhibitions, new productions, tours, translations and conferences); the promotion of short-, medium-, and long-term cooperation between museums to enhance cultural ties, conservation and research of common European heritage; the promotion of the links between artistic universities and institutions in order to create new cultural resources; the training of professionals in the audiovisual sector, promotion and distribution of cinematographic works and audiovisual programmes and support for film festivals. b) Fostering convergence with European standards in the broadcasting field c) Consultation and cooperation in relevant international fora, such as UNESCO, in order to defend common objectives and promote cultural diversity, especially through the UNESCO Convention on the Protection of the Diversity of Cultural Contents and Artistic Expression.

PARTNERSHIP AND COOPERATION AGREEMENT

Current or future
sectoral
agreements,
existing or agreed
but not yet started

TRADE IN STEEL PRODUCTS	TRADE IN NUCLEAR MATERIAL AND NUCLEAR COOPERATION	TRADE IN TEXTILE PRODUCTS	READMISSION	VISA FACILITATION	EUROPOL COOP. I	CIVIL PROTECTION ARRANGEMENTS	SCIENCE AND TECHNOLOGY
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Dialogues existing or agreed but not yet started

SPACE 1		SPACE 2		SPACE 3	SPACE 4
Regulatory dialogue on industrial products		Climate Change	Visa policy	Civil judicial cooperation	Political Dialogue
Counter- terrorism	Enterprise policy and industrial policy	Energy	Human rights consultations		
Transport					
Information Society					

Agriculture

Further dialogues on macro-economic policy and financial markets, intellectual property rights, public procurement, investment, on an early warning mechanism for trade issues, and on environmental issues, are in the making (early 2006).

ANNEX 4

Country Environment Profile: Russia

For most of the 1990s air and water emissions fell in absolute terms as industrial output declined, although amounts of hazardous waste increased in the late 1990s. However, measures of pollution intensity (i.e., emissions per unit of industrial output) increased for all pollutants indicating that the economy was operating less efficiently with respect to the pressure it put on the environment.

Since 1999 industrial output has increased and this has been accompanied by a decline in air and water pollution intensities, although the pollution intensity with respect to hazardous waste has continued to deteriorate. However absolute levels of emissions have increased with recent rapid GDP growth.

Ambient environmental pollution is severe in many industrial areas. Air and water quality continues to be a serious and growing problem in many cities, land contamination is a major issue that is not being tackled, hazardous waste is accumulating at a rapid rate and its storage is often in inadequate conditions, protected areas are often under funded and hence not effectively managed, and forest fires and illegal logging are a problem.

Environment policy

The Environmental Doctrine of the Russian Federation was approved by the government on 31/08/2002 and defines the long-term goals, directions, objectives and principles of Russian environmental policy.

Broadly speaking the political priority given to environmental policy in Russia, and the resources available, declined following the abolition of the Ministry of Environment in 1997. Frequent changes since then in the structure of environmental administration have resulted in considerable uncertainty over responsibility for enforcement and compliance, and have hindered the development of effective dialogue with the EU. However recently there have been more positive signs, notably the decision by Russia to ratify the Kyoto Protocol in 2004, and the adoption of environmental objectives in the EU-Russian Common Economic Space road-map.

Environment legislation and its implementation

The 2002 Federal Law on Environmental Protection of the Russian Federation is the basic framework legislation.

Other important framework legislation includes:

- The 1991 Law on Environmental Protection defines standards for environmental quality, provides for the protection of biota, established the basis for federal protected areas and the activities allowed in them.
- The 1995 Federal Law on Ecological Examination established a basis for environmental impact assessment.
- The 1995 Water Code and 1998 Law on Fees for Water Bodies' Use have supported and extended the use of economic instruments
- The legal basis for waste management is provided by the 1998 Law on Generation and Use of Waste.
- The 1999 Federal law on air protection specifies emission standards for stationary and mobile emission sources, technological processes and equipment.
- The 2002 Federal Law on Technical Regulation.

- Currently a new forest code is being enacted.

Administrative capacity

Responsibility for environmental policy in the Russian Federation is dispersed between several ministries and agencies at national level and is still somewhat fluid after changes following the Presidential Decrees on the organization of government in March and May 2004. Discussions on the possible establishment of a federal agency for environmental protection continue.

Since 2000, the Ministry of Natural Resources (MNR), which was restructured in January 2005, has been the main Russian counterpart for environmental policy dialogue. It is responsible for environmental policy, with three departments: Legal, Environmental Policy and International. The MNR is also responsible for policy and regulation of exploitation of natural resources including mining of minerals and felling of timber.

Four Federal Services/Agencies report to the MNR: on Supervision of Nature Resources, Water Resources, Forestry, and Management of Mineral Resources.

Separate from the Ministry and reporting to the Government as a whole is the Federal Service for Hydrometeorology and Environmental Monitoring (Roshydromet), which among other responsibilities, takes the lead on international negotiations on climate change.

There is also a Federal Service for Ecological, Technological and Nuclear Oversight, reporting to the government, which deals with nuclear and radioactive waste matters, and has a major role in environmental enforcement, having taken over these functions from the MNR.

The Ministry of Economic Development and Trade is responsible for the co-ordination of Russian implementation of the Kyoto Protocol (Department of Property and Land Relations and Environmental Management Economics).

The Russian Regional Environment Centre (RREC) established with Tacis funding in 2001 is playing a useful role in promoting public awareness and stakeholder dialogue (central and local authorities, business, academia, NGOs).

Participation in regional and international processes

Russia has ratified relevant international and regional conventions with the notable exception of the following: Cartagena Protocol on Biosafety, PIC convention on trade in dangerous chemicals, recent protocols under the UNECE Conventions on Long-Range Transboundary Air Pollution on Trans-boundary Environmental Impact Assessment (Espoo) and Public Participation (Aarhus), the Bonn Convention on Conservation of Migratory Species, and the Bern Convention on Conservation of European Wildlife and Habitats.

Russia ratified the Kyoto Protocol on climate change in November 2004, but has not made any commitment regarding further measures after 2012.

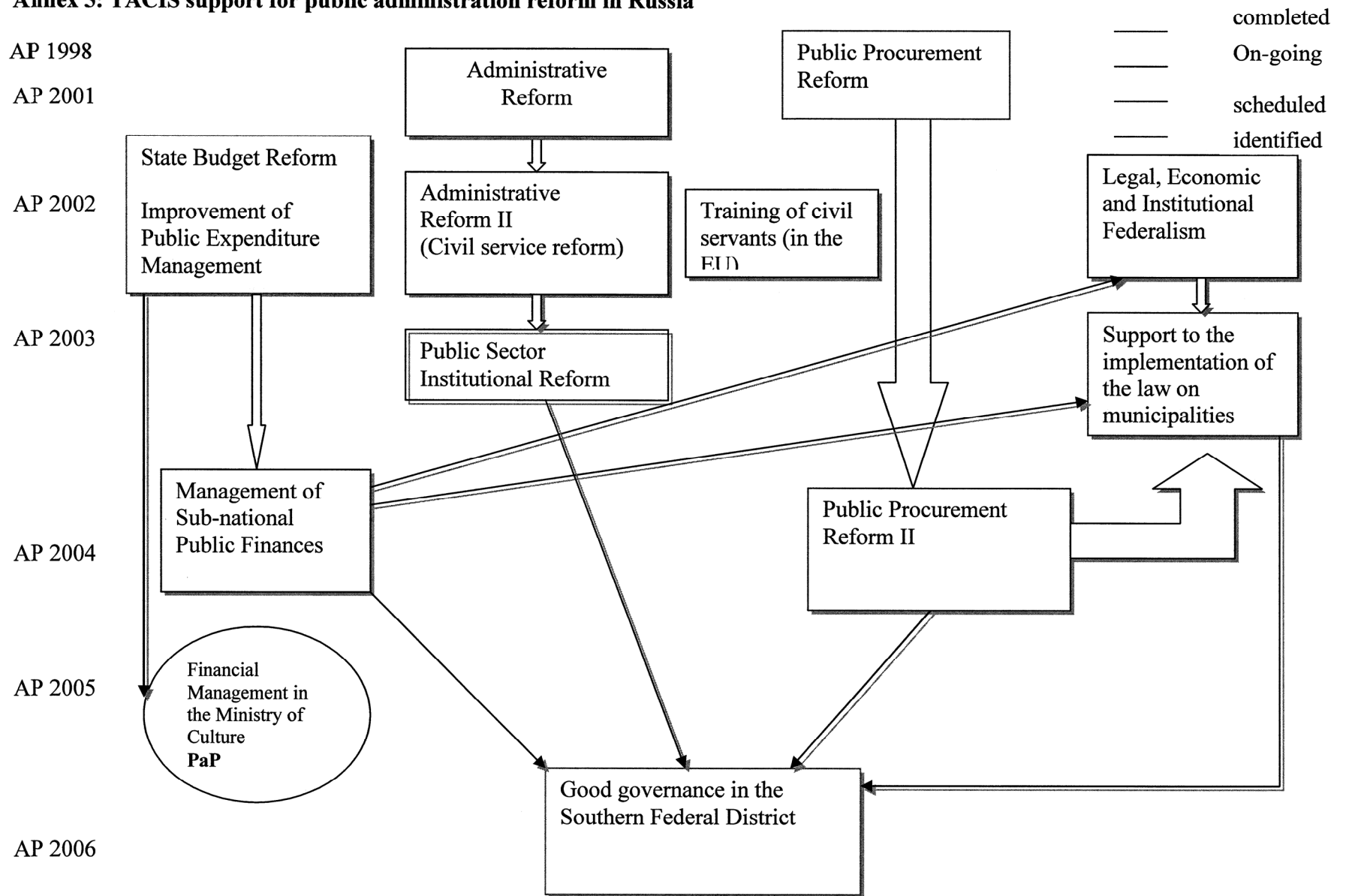
Key environmental areas where action is needed

The EU-Russia Common Economic Space roadmap identifies the following environmental priorities:

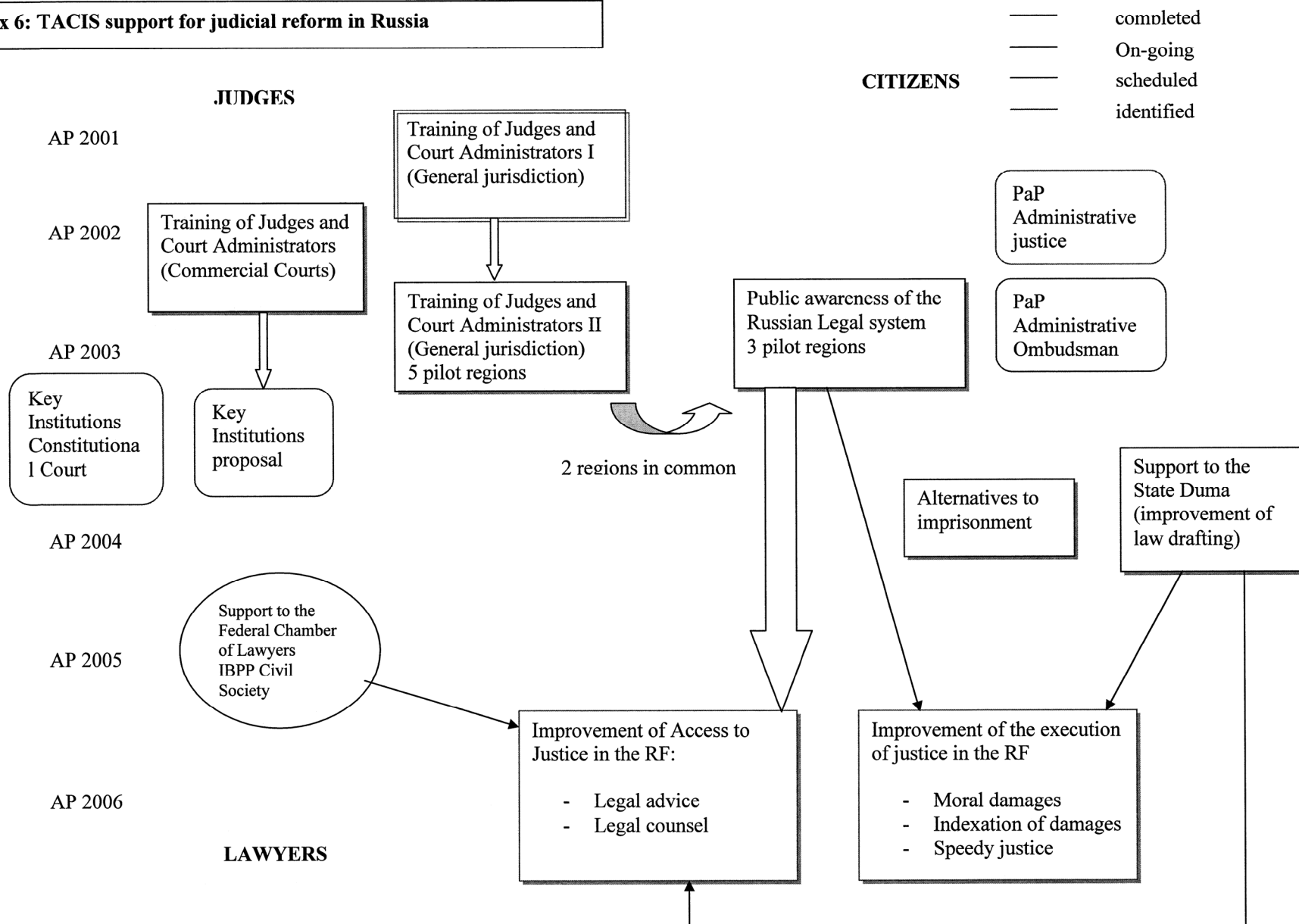
- Promote respect and greater public awareness for the environment, and better environmental information and education

- Promote commitment to and implementation of multilateral environmental agreements
- Support implementation of the Climate Change Convention and the Kyoto Protocol
- Co-operate on cleaner production and more efficient use of natural resources
- Co-operate on conservation of biodiversity including protected natural areas
- Co-operate on water policy, including trans-boundary water basins and the EU water initiative
- Protect, conserve and encourage the sustainable use of marine environments
- Reduce risks of accidents and pollution, especially in seas and inland waters
- Support compliance with the Espoo Convention on trans-boundary environmental impact assessment
- Intensify co-operation to combat illegal logging, taking account of the Forestry Law Enforcement and Governance (FLEG) initiative
- Promote convergence of legislation towards higher standards.

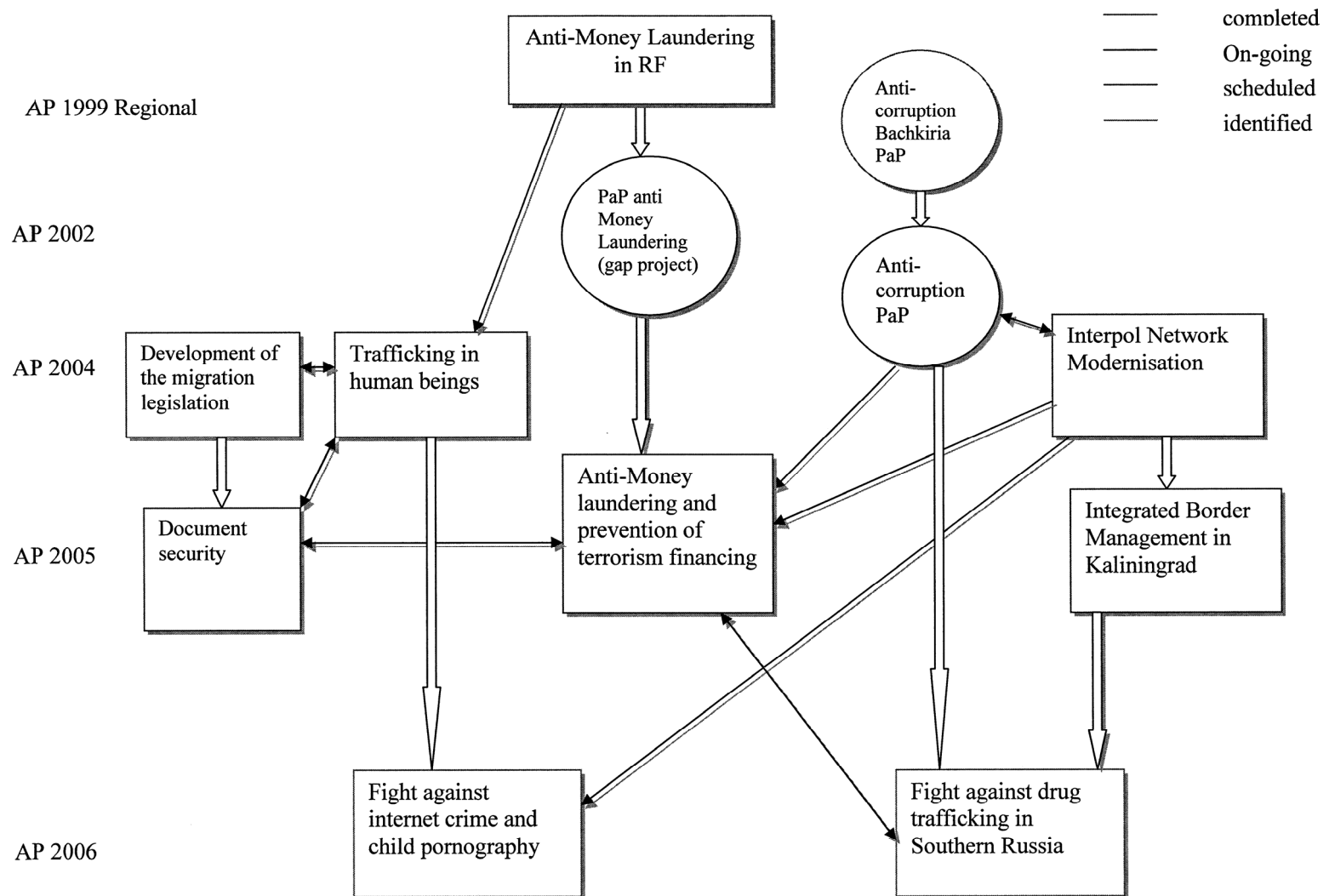
Annex 5: TACIS support for public administration reform in Russia



Annex 6: TACIS support for judicial reform in Russia



Annex 6 (cont): TACIS support for the fight against organised crime in Russia



HOME AFFAIRS

