

Natural Gas Transit Tariffs to Armenia via Georgian Main Gas Pipeline

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Main objective of former soviet countries is to find a place in international labor distribution, looking for the priorities for the economic development that would fit real-life distribution of international labor.

Given unique geographical location and clear orientation toward Europe Georgia is recognized as one of the main competitors for the export of Caspian power resources. The country is involved in global projects and looks forward to gain big profit in terms of political stability and economic development. Therefore, any mistake or inaccuracy in this matter might involve vital risk for the country.

Apart from prospective projects there are operating projects related to the transit corridor; e.g. Georgia has been conveying as transit natural gas from Russia to Armenia since the collapse of the Soviet Union, when Georgia was announced as a proprietor of the Main Gas Pipeline running on its territory. Proprietary right means that the country had to gain particular profit out of the Main Gas Pipeline, but Georgia accumulates debts instead of gaining profit.

It is notable that “transit tariff” and “transportation tariff” are different concepts, they might not correspond to each other as conveying different meaning: transit tariff reflects economic interest of a county, i.e. what is the cost for using the territory of a county for transit; while transportation tariff has more technical/economic meaning and is established considering all expenses, profitability of operations and payment of taxes. Therefore, as a rule transit tariff for the similar service should exceed transportation tariff operating in the country.

The analysis of studied materials shows that Georgian government has not established gas transit tariff service from Russia to Armenia. According to law currently in force the state has to undertake certain activities to resolve this issue, though actually it is solved by Ltd-s. The state has voluntarily introduced in-kind reimbursement of the tariff service within the regulated regime (natural gas transit). This is definitely disadvantageous for Georgia, as transit cost in this way is less than transportation net cost and can not cover even the expenses. It is even less than local transportation tariff for the similar service in Georgia. The loss is partially covered from the local transportation tariff, i.e. natural gas transit to Armenia is financed by Georgian side. Transit tariff actually does not exist; it was not defined at national level and was not approved according to the law currently in force.

Since 1 October 1993 to 1 September 1995 JSC Saktransgazmretsvi has been conveying as transit natural gas from Turkmenistan to Armenia. Agreements on transit service have not been concluded at all. During this period JSC Saktransgazmretsvi has applied to lots of organizations regarding following issues: who has to conclude an agreement and reimburse transit costs to Georgian side; nevertheless, nobody has covered transit costs. Then for several months Georgian side has been voluntarily confiscating and distributing natural gas intended for the transit. As a response Itera International Group of Companies (JSC Gazprom's distributor company) commenced the agreement with Georgian side.

In the agreements with Itera IGC (1996 – 2002) and Gazinvest (2002-2003) Georgian side registered 10% of transported gas volume as transit tariff (as in-kind payment). The tariff was established in a following way: a meeting was held in Moscow, in the building of the JSC Gazprom in 1996, attended by representatives of the JSC Gasprom, Itera IGC, State of Armenia and the enterprises supplying natural gas to Georgia - JSC Saktransgazmretsvi and Rustavi Metallurgy and Chemical Industrial Complex. According to the protocol of the meeting natural gas transit cost to Armenia through Georgia

was established as 10% of the transit gas volume (as in-kind payment). The protocol's decision also stated that this amount should have been transferred to Georgian side at the northern border. Surprisingly, not only the natural gas transit tariff to Armenia was established by the protocol decision, but also the tariff of natural gas transportation to the JSC Saktransgazmretsvi and Rustavi Metallurgy and Chemical Industrial Complex on the territory of Georgia – similarly as 10% of the transit gas volume. Moreover, according to the same document Itera IGC was assigned to submit to one of the research institutes of Russia a letter regarding calculation of the natural gas transit tariff rate to Armenia. The conclusion of the Institute was obligatory to fulfill for all parties. Mentioned protocol was signed by all parties involved. It is obvious, that Russian side actually possessed and controlled transit sector of Georgian Main Gas Pipeline ever since.

It should be mentioned that in 1996-2000 transportation tariff for every 1000 cubic meters of natural gas on the Georgian territory was GEL 12.9. Since 1996 JSC Saktransgazmretsvi has been repeatedly applying to Georgian government and “Itera” IGC regarding unprofitable of in-kind payment. Provision of Georgian legislation also increased losses, namely it stated that in-kind supply of natural gas to the country was VAT taxable at its border, while paying tariff could liberate Georgian side from VAT.

In 1998 the issue was considered by the Ministry of Fuel and Energy of Georgia that sent an official letter to “Itera” IGC explaining and instructing that according to Georgian law currently in force tariff rate for the transportation of 1000 cubic meters of natural gas was GEL 12.9. The letter stated that for transportation of natural gas through the territory of Georgia everybody had to pay this tariff, either had to approve different tariff and payment rules in accordance with the law currently in force. Simultaneously, other types of payment should not have been reducing the amount of the expenses and taxes included in the tariff. Unfortunately, this letter had no response.

ცცორდინგ ტო ტჰე რელევანტ დეცრეე ოფ ტჰე რესიდენტ ოფ ეორგია უნლაწფუულ ცონფისცატიონ ოფ ტჰე აინ ას იპელინე ნეტწორკ ფრომ ტჰე ჟშჩ “Saktransgazmretsvi” and its handover to the newly established “Georgian International Gas Company” წას ცომმენცედ ინ 1998. ს ტჰოუგჰ ტჰე აგრეემენტ ბეტწვენ ეორგია ანდ თურკეე წას ტჰე ბასის ფორ ტჰე ესტაბლისჰმენტ ოფ ტჰე ცორპორატიონ: “Georgian International Gas Corporation” ჰად ტო იმპლემენტ ტჰე ოპერატიონ, იფ ლუსსია ტრანსპორტედ ნატურალ გას ტო თურკეე ტჰროუგჰ ეორგია. ცტუალლე იტ ტურნედ ოუტ ტჰატ სუცჰ აგრეემენტ ბეტწვენ ეორგია ანდ თურკეე ჰას ნოტ ბენ ცონცლუდედ, წჰილე ტჰე ჩორპორატიონ წას ჰანდედ ოვერ ტჰე წჰოლე იპელინე ნეტწორკ ინსტეად ოფ ტჰე ტრანსიტ სეცტორ.

In 2000 mentioned Corporation established JSC “Georgian Gas Transportation Company” that concluded an agreement with “Itera” IGC regarding natural gas transit; in the agreement the transit tariff was again registered as 10%. An interesting fact: starting from 2000 disputable issues had to be considered in Moscow, by the Arbitration Court of Russian Federation, while previously Stockholm International Court had to consider them. Court decision was obligatory to fulfill for the both parties.

It should be emphasized that since 2000 natural gas transit tariff per 1000 cubic meters in Georgia has increased from GEL 12.9 to GEL 16.6 in order to avoid losses, while transit volume was the same. This increased losses; moreover, on the border the price per 1000 cubic meters of natural gas was reduced from USD 65 (1998) to USD 40 (2000), and then increased to USD 50 (2001) and USD 60 (2003).

It should be mentioned that only transportation expenses in the natural gas transit tariff (GEL 16.6) exceed GEL 11, whereas the price for natural gas transit per 1000 cubic meters was: in 2000 – GEL 9, in 2001 – GEL 10; i.e. even if the in-kind 10% of transported natural gas goes to Georgian side, it is still unprofitable and cannot cover even the expenses. The loss

is increased by the fact that on the border Georgian side pays customs duties for the natural gas transit tariff – 20% of natural gas cost is paid as VAT.

What's important, 10% of transported natural gas paid as transit tariff is accepted as transit cost for the Georgian side; then the losses occurring during the transportation of Armenian natural gas are compensated out of these 10% - losses are compensated by natural gas already cleared at customs by Georgian side. In 2002-2003 Georgian side has paid millions of GEL as VAT for the customs clearance only, motivating this by the compensation of losses.

Additional damage is caused by the fact that Georgian company covers transportation costs from the northern border to the southern one in order to compensate losses. Considering that the net cost for the transportation of 1000 cubic meters of natural gas is 11 GEL, losses amount to millions of GEL.

This operation is supported by the fact that the gas transit service normative for losses are not approved; besides, Georgian side has accepted losing obligations of the contract, according to which Georgian side was obliged to deliver to the southern border same amount of natural gas that was received on the northern border, whereas transportation of natural gas is associated with standard losses and this should have been acknowledged from the beginning. Therefore, if Itera IGC would like to deliver the same amount of natural gas to the southern border it has to leave excess amount of gas, equal to the amount of standard loss, at the northern border and this amount should not be regarded as transit tariff.

The topic of losses should be considered separately: the amount and the dynamics of losses also need clarification. If we believe and assume that in 2001-2003 annual losses were equal to 50-126 million cubic meters, then the territory adjacent to the gas pipeline should have been announced as the explosive zone. The conclusion of the Ministry of Environment and Natural Resources of Georgia recognizes the discharge of 7.5 million cubic meters of

natural gas into the atmosphere as unlimited. In our case the discharge of 50-126 million cubic meters of natural gas into the atmosphere is absolutely unacceptable and goes beyond any standard. Please, note: JSC Tbilgazi on average utilizes 250 million cubic meters of natural gas annually.

Substantial losses are registered and documented during natural gas transit to Armenia. Actually such amount of losses is unrealistic, i.e. this amount of natural gas is not lost. Due to disorderly registration system and particular private interests actually accessible natural gas is registered as loss and is delivered to the certain group of consumers on the basis of unofficial contracts. The cost of this natural gas makes up the debt of Georgian side. Consequently, grows indebtedness of Georgian enterprises to natural gas suppliers and eventually these enterprises are handed over to Russian side (the supplier) to compensate “accumulated debts.”

Actually existing losses are compensated from the 10% received by Georgian side as a transit tariff. The cost of the rest of natural gas is too small to cover expenses of Georgian side; therefore, the loss is partially covered from the revenues generated from the local transportation tariff, i.e. natural gas transit to Armenia is financed by Georgia.

The investigation of the issue showed that JSC Itera undertakes “suffocation with gas” plan in Georgia: it makes an enterprise of its interest accumulate suspicious debts in a form of unpaid cost for utilized gas (using natural gas that was purchased, customs cleared and transported by Georgian side); then it threatens to cut off gas supply and buys the enterprise to compensate debts (and does not spend additional gas for this). In this way Itera has already purchased large enterprises in Georgia, including Rustavi Chemical Industrial Complex.

There are also talks about selling the Main Gas Pipeline to Russia. . .

The issue of selling of the აბ ახ აპელობე goes far beyond the economic concerns - it is an important political problem.

Definitely, the Constitution of Georgia prohibits selling of strategic objects such as the აინ ას იპელინე, but the study showed that Russian side actually owns and controls აინ ას იპელინე ბელონგინგ ტო ეორგია. იუ ეხისტინგ სიტუატიონ რემაინს უნცკანგელ, წე ტპინკ ტპატ ტპე სუსტაინაბილიტყ ოფ Shah-Deniz Gas Pipeline Project should be investigated thoroughly.

Main factor facilitating this economic crime was the fact that the state let the pricing issue of this central strategic sector, representing national monopoly, take its course. Unfortunately, this was very efficiently used against the interests of the country.

If the country had established tariff on mentioned services in a hard currency, these violations could have been avoided; moreover, it would have ensured influx of hard currency to the country, efficient operations of the company and revenues to the budget.

We believe following recommendations would be reasonable to change the situation:

1. The Ministry of Economic Development together with the Ministry of Fuel and Energy should prepare the issue for the consideration at the government's meeting in order to resolve the situation and undertake appropriate activities.

It would be reasonable for the future to conclude an agreement between Georgia and Armenia. The issue of the transit cost exchange on electric power import from Armenia could be considered.

2. ასელ ონ ტპე სტუდყ ოფ ეხისტინგ მატერიალს ჰიგჰლიგჰტინგ ტპე პრობლემ, ტპე გოვერნმენტ სპოულდ ფილე ტპე ცასე რეჩუესტინგ ტპე რეტურნ ოფ რეციევაბლე მონეყ, ას Iტერა I ნ ჰად ან ოფფიციალ ინსტრუცტიონ ფრომ ტპე გოვერნმენტ ოფ ეორგია (ტპე ინისტრყ ოფ უელ ანდ ნერგყ) ტო პროვიდე რეიმბურსემენტ აცკორდინგ ტო ტპე ტარიფფ ესტაბლისჰედ ბყ ეორგიან ლეგისლატიონ; წჰერეას ტპე ცონტრაცტ ცონცლუდედ ბეტწეენ ტწო ეკონომიც უნიტს ოპერატიონგ ონ ტპე ტერიტორიეს ოფ

ეორგია ანდ ღუსსია ლეგალლე ცან ნოტ ოვერრიდე ეორგიან ლეგისლატიონ, წჰიციჰ ის ჰიერარციკალლე ტჰე დოკუმენტი წიტიჰ პრევალენტი ლეგალ ეფექტი.