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# RUSSIA'S ROLE IN FOSTERING THE CIS TRADE REGIME \*

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## Abstract

The CIS trade regime can be characterised as a mix of, partly overlapping, weak, bilateral, sub-regional, and multilateral agreements. This is a result of the design of the CIS, which was explicitly constructed to allow its member states to participate in only those parts that they deemed in their best interest and not to participate in other parts.

The dissolution of the Soviet Union forced the successor states to create a trade regime. Initially, they turned to one another not to disrupt trade any more than needed. However, Russia carried most of the financial burden of the initial arrangements and started to push for bilateral agreements. The others followed this example, but were careful not to commit too much sovereignty in these agreements. At a later stage, sub-regional agreements substituted for the CIS framework as well.

The CIS states remained ambivalent, however, to submit too much sovereignty, whereas Russia formally stayed out of the multilateral free trade agreements altogether. The countries did work together multilaterally and committed themselves to these agreements where it concerned specific issues.

In this paper, we look for causes of the myriad of agreements in the actual economic developments. We will therefore present and discuss the major trade agreements with economic arguments. We will also briefly discuss the developments in the volume and direction of trade. Although we expect the gradual improvement of the agreements and the 'rationalisation' of the complex arrangement, we do not foresee a consolidated 'hard' multilateral framework in the short or even medium term.

**JEL-classification:** F15, F53, K33, P48

**Keywords:** trade agreements, economic integration, CIS

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## **Introduction**

Fifteen years into independence, the 12 successor states of the Soviet Union that formed the Commonwealth of Independent States (CIS) are still working out a new equilibrium for their mutual relations. It is unclear, however, whether there actually is a role for the CIS in that new equilibrium. Member states feel weary of Russia's dominant position within the CIS and they are afraid that Russia will use its economic importance to establish a political and strategic dominance in the region, and undermine their newly acquired independence (Larrabee, 2001, Sushko, 2004). Russia also shows an ambivalent attitude towards the CIS.

The ambivalent attitude towards the CIS in the member states and their inexperience in developing an institutional regime for economic cooperation, as well as the continuously changing external and domestic environment resulted in a myriad of multilateral and bilateral agreements of very diverse quality between the CIS states. Grinberg (2005) estimates that 90 per cent of all multilateral documents that create the legal base of the CIS, and there are more than 1,000 of them, are ineffective. According to many observers, the CIS seems to have failed in becoming an effective framework of economic cooperation and (re)integration (Stroev et al., 1999). The fascination with the failure of the CIS, however, distracts the attention from the economic cooperation that does occur between the former Soviet republics, and from the institutional forms that it takes.

The agreements that are concluded often are partial and selective, while their ratification and implementation also is a mixed affair; but this does not imply that they do not have any value. What can be observed in the CIS is that economic cooperation takes the form of overlapping bilateral and multilateral agreements of very distinct legal quality. From an economic point of view it does not make sense that countries that have concluded a multilateral free trade agreement, as the CIS countries did in 1994, an agreement that they amended in 1999, subsequently conclude bilateral free trade agreements with their partners as well. It creates overlap, it increases transaction costs, and it obfuscates the status of both the multilateral and the bilateral agreement. In this paper, we seek to discuss the functional value of such an approach. We look for reasons for the behaviour of the CIS countries. First, we will summarise the legal framework. We will also discuss the economic questions that trade agreements seek to address. We will continue by discussing the rationale that might explain why the CIS countries continue to work together and the forms they seek to do so. Because Russia is the most important country in the CIS, we will focus on Russia's position. We conclude that the CIS still provide benefits to the CIS countries, but that it is still open whether or not that will continue to be so.

### **A summary of the legal framework<sup>1</sup>**

One of the declared goals of the CIS was to maintain the pre-existing economic unity while placing inter-state relations on the basis of respect of sovereignty and mutual benefit. Since the CIS no longer was a single legal unity, the legal nature of the CIS trade regime had to be based on the international law of treaties and the mechanism for their transformation into the respective domestic legal orders.<sup>2</sup> There are a number of qualifications of particular importance in the CIS context. First, the CIS applies the 'interested party' principle, which implies that a state could choose not to participate in a certain agreement or decision without afflicting its validity. Each member is thus able to construct for itself a regime that corresponds best to its interests. However, the lack of even a minimum set of instruments which members are required to join works against the logic of common commitment needed for a robust

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<sup>1</sup> This section is based on Dragneva and DeKort (2007).

<sup>2</sup> All CIS members are party to the Vienna Convention on the International Law Treaties of 1969.

regional economic integration. Second, many of the CIS multilateral agreements are signed under reservations. These are a legitimate international law instrument used to limit the binding effect of agreements for the party that makes them. Third, the CIS members prefer to conclude a large number of international agreements – framework or general agreements as well as more specific-issue ones – rather than to adopt a limited number of comprehensive, detailed agreements. This approach allows the CIS members to pursue a project by gradually building consensus for the next steps, which is particularly important in a setting with a pronounced diversity of members. With the ‘interesting party’ principle it allows the member states a greater possibility to pick and mix with reference to their differing sensitivities and concerns, while keeping the whole project on course. On the other hand, the fragmentation poses a danger of rule clashes, patchy implementation, and a non-transparent and complex administration of the regime. Finally, the founding documents of the CIS refer to both multilateral and bilateral agreements as instruments for cooperation. In case of overlap, such as in case of the trade regime, this gives rise to the question about the interaction of the bilateral and multilateral regimes, and about the legal device that need to be put in place to deal with possible conflicts.

The charter of the CIS did not create an extensive organisational structure. Initially, only the Council of Heads of State and the Council of the Heads of Government were given the power to adopt decisions. As indicated above, the member states have options to selectively adopt decisions. Therefore, the Councils need to ‘rule’ by consensus and use a political road to enforcement rather than a legal one. The evaluation of the decisions by the Councils is complicated because decisions sometimes have the status of an international agreement, but more often, decisions are of a declaratory and political nature (Dragneva, 2004). The distinction between ‘normative’ decisions and ‘political’ decisions often is quite fuzzy in the CIS. Other CIS bodies were initiated at a later stage and include the Inter-State Economic Committee (IEC) and the Economic Council and a number of branch organisations. The IEC existed between 1994 and 1999 and reflected the short-lived impulse for an enhanced EU style cooperation. It did receive the right to adopt executive decisions in the area of transferred competence, but its successor, the Economic Council reverted back to the consensus rules. Its most important task relates to preparing draft international agreements in the area of trade cooperation to be approved by the Councils of Heads of State and Government. Two branch organisations deserve mentioning. The Intergovernmental Council on Standardisation, Metrology and Certification is charged with decision making powers related to the harmonisation of CIS standards and their adaptation to international requirements, and the Council of the Heads of Customs Services was entrusted with powers related to the coordination of customs policies and the work of national customs services, the harmonisation of customs legislation and the preparation of the common customs tariff for the attainment of a customs union. The latter one had the scope of its powers reduced in 2002, reflecting the mitigated agenda for economic cooperation in the CIS.

As indicated above, the CIS presents a mix of, often overlapping, bilateral and multilateral agreements. The picture gets even more complicated as bilateral and multilateral agreements often differ in the strength of commitment they require from the signatories. Bilateral agreements rarely envision a mechanism for resolving disputes between its parties, relying on negotiations to do so. Multilateral agreements on the other hand often do attempt to strengthen the bindingness of the commitments undertaken. In 1993, the Treaty of the Economic Union even went as far as to strengthen the role of the Economic Court, by requiring that ‘if the Economic Court recognises that [...] a member state has not fulfilled its obligation ensuing from the Treaty, this state is obliged to take measures connected with the implementation of the decision of the Economic Court’.<sup>3</sup> A year later, in 1994, a Free Trade Agreement (FTA) was concluded which ‘undermines’ the position of the Economic Court as it introduces alternative

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<sup>3</sup> Treaty on the Economic Union, 1993, art. 31. The Economic Court itself was created in 1992, by a special agreement with the mandate of ensuring the uniform application of the agreement of the CIS and the economic obligations and contracts based on them. Its decisions were not binding, but were recommended for adoption by the country found in violation.

instruments, conciliation and international juridical procedures, for dispute settlement. The FTA of 1999 avoids any explicit reference to the Economic Court altogether. Not many cases have been brought to the Economic Court and its future position is unclear. The CIS Heads of State announced, in 2005, an initiative to enhance the institutional profile of the Economic Court, but only one year earlier, one of the most pro-integrationist politicians in the CIS, Kazakh president Nazarbayev, declared that nobody anyway pays any attention to the decisions adopted by the Court.

Agreements on specific issues often, but definitely not always, contain conflict avoiding clauses, whereby their provisions 'do not affect' the provisions of other international agreements in which the parties participate. The 1994 and 1999 FTA contain a conflict clause, whereby nothing in these agreements 'prevents any of the contracting parties from implementing the obligations under other agreements in which the contraction parties participate or can participate as long they do not contradict the provisions and objectives of this agreement'. They thus allow for supplementing agreements, adopted either earlier or later.

The CIS trade regime can be described as a symbiosis between bilateral and multilateral regimes, both of which can be described as weak regimes. Bilateral agreements cover some key free trade rules, such as tariffs, but remain minimal and quite basic. Non-tariff barriers, for instance, are generally left out, as are liberalisation of services or intellectual property to name a few issues that have become important in international trade agreements. Disputes are generally resolved through consultations. Over the years, some improvements of the quality of the provisions of bilateral agreements can be observed, most clearly in the increasing number of references to related GATT/WTO regulations. Multilateral agreements, as indicated, reached further from the beginning, both in terms of comprehensiveness, quality of rules and the provision for greater credibility of commitments. But the dispute settlement again is left to consultations. Here too, improvements can be observed over the years, most notably in the 1999 revision of the FTA of 1994.

## **A civilised divorce**

In the Soviet Union, foreign trade was part of the central plan and foreign trade organisations negotiated with exporters about the terms of delivery. Because the rouble was inconvertible, trade was concluded in foreign currencies or in barter. With the partners in the Council of Mutual Economic Assistance (CMEA), trade was concluded in so-called transfer roubles and most trade balances were cleared bilaterally. Trade between the Union Republics, of course, was not registered as foreign trade, but was part of the annual planning process. It is difficult to evaluate the intra-republican 'trade balances' as prices did not reflect scarcity and transport costs were negligible. In an attempt to determine the intra-republican trade balances, Van Selm (1997) reports that Russia and Turkmenistan registered a trade surplus, but all others registered trade deficits.<sup>4</sup> These trade surpluses did not lead to financial claims on the other republics, the surplus countries effectively subsidising the deficit countries. Furthermore, to facilitate the planning process production had been concentrated in large production units and to minimize the dependency on the procurement system, ministries had developed a conglomerate structure, with little respect for efficiency considerations, nor for the borders between the republics.

With the dissolution of the Soviet Union, intra-republican trade became trade between sovereign states. The ministerial conglomerates were also broken up, leaving their parts scattered over the new countries, and to continue production, the enterprises needed to trade internationally. The absence of a centrally planned foreign trade regime furthermore reduced the opportunity to balance the balance of payment.

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<sup>4</sup> Van Selm uses world market prices for the trade balances. He acknowledges that calculations in domestic prices would give trade surpluses for Russia, Ukraine and Belarus, but not for Turkmenistan.

Trade balances were to result in financial claims or obligations. Therefore, the successor states needed to create a financial system to process all payments related to foreign trade. To facilitate trade, the CIS countries, in a multilateral agreement, decided not to break up the monetary union and to continue the rouble as their common currency.<sup>5</sup> (With due notice, countries could leave the rouble zone.) Maintaining the rouble, however, proved to be detrimental to Russia's anti-inflation policy. The central banks of the newly independent states extended unlimited credits to importing firms and Russia continued to have balance of payment surpluses. Effectively, the situation that existed in the Soviet Union, where trade deficits did not result in a financial obligation for the importing union-republics (now countries), continued to exist. The trade credits of the other CIS central banks ended up with the Central Bank of Russia (CBR) thus fuelling Russia's inflation. In response, Russia tried to reign the automatic crediting by introducing so called 'technical credits', which were subject to negotiation as an alternative for the automatic credits to the other CIS states that resulted from the trade surpluses (Granville, 1995). This Russian policy marked the beginning of the end for the rouble zone. To become independent of Russia's credit conditions, the other states started to create their own currencies. The end of the rouble zone signalled Russia's interest in an independent trade policy and an independent monetary policy. It also forced the other countries to rethink their trade policies as they could no longer shift the bill for trade deficits to Russia.

The governments of the successor states anticipated that the liberalization of prices and trade, at the beginning of 1992, would give rise to steep price increases. To ease the adjustment of enterprises and consumers to higher prices, many countries issued price controls. Because the level of controls differed between the countries export restrictions were placed on price controlled commodities to prevent these goods from being exported (Tarr and Michalopoulos, 1994). This, together with the deep economic crises that substantially reduced demand overall, reduced trade considerably. The successor states reacted by setting up a network of intergovernmental, bilateral barter trade for a number of important products on a so-called obligatory list. Products included energy, raw materials and foodstuffs. This system was similar to the one used for trade within the CMEA, and tried to establish bilateral current account equilibrium. For a further, indicative, list of products that was deemed important for domestic consumption and for hard currency exports, export licenses and quotas were introduced. This list included intermediate products and consumer goods. Within the limits of the licenses and quotas, enterprises could trade these products and determine the conditions for sale. Both the products on the obligatory list and the indicative list and the conditions for those products were negotiated in bilateral agreements to fit the trade relations between both countries. Trade for products that are not on the obligatory or the indicative lists became unrestricted.

The return to bilateral barter agreements and the end of the rouble zone enforced Russia's position. Given its trade surplus with all other CIS countries, Russia already had a dominant position in the trade relations with the other countries and Russia found it easier to get its ways in bilateral agreements than in a multilateral setting. In the second half of 1992, Russia concluded bilateral agreements with eight of the other 11 CIS countries. See table 1.

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<sup>5</sup> The IMF also advised, in October 1991, to maintain the ruble zone. See for a discussion on the IMF and the Ruble Zone a collection of papers in a Symposium Issue of Comparative Economic Studies, Vol XLIV, No. 4 Winter 2002.

**Table 1: Bilateral Free Trade Agreements between CIS countries**

	<i>AM</i>	<i>AZ</i>	<i>BY</i>	<i>GE</i>	<i>KZ</i>	<i>KG</i>	<i>MD</i>	<i>RU</i>	<i>TJ</i>	<i>TM</i>	<i>UA</i>	<i>UZ</i>
<i>AM</i>	X	-	2000	1995	yes	1994	yes	1992	yes	-	1994	yes
<i>AZ</i>		X	-	1996	1997	-	1995	1992	-	1996	1995	1996
<i>BY</i>			X	-	1997	1996	1993	1992	1998	-	1992	-
<i>GE</i>				X	1997	1995	1997	1994	-	1996	1995	1995
<i>KZ</i>					X	1995	yes	1992	yes	-	yes	1997
<i>KG</i>						X	1995	1992	-	-	1995	1998
<i>MD</i>							X	1993	yes	yes	2003	yes
<i>RU</i>								X	1992	1992	1993	1992
<i>TJ</i>									X	-	2001	1996
<i>TM</i>										X	1994	1996
<i>UA</i>											X	1994
<i>UZ</i>												X

*Sources:* Authors compilation from accession reports on the WTO website; national sources; and World Bank studies. For some of the FTA's, it is not clear when they are concluded.

The abbreviations used read as follows: AM – Armenia, AZ – Azerbaijan, BY – Belarus, GE – Georgia, KG – Kyrgyzstan, KZ – Kazakhstan, MD – Moldova, RU – Russian Federation, TM – Turkmenistan, TJ – Tajikistan, UA – Ukraine, UZ – Uzbekistan.

With Moldova and Ukraine such agreements were concluded in 1993, while an agreement with Georgia followed in 1994. These bilateral agreements were free trade agreements (FTA) that included abolition of customs duties, taxes and levies of equivalent effect on the export and import of commodities, but allowed for quantitative restrictions and measures with equivalent effect. Protocols were added to negotiate exemptions. The above mentioned bilateral agreements regarding products on the obligatory and the indicative list became part of so-called Trade and Cooperation Agreements that were signed together with the FTAs and were to be renewed on an annual basis to allow for changes in the obligatory and indicative lists.

The events in 1992 also marked a significant change from the intended multilateral cooperation towards a Russian induced bilateral approach. The CIS member states concluded several multilateral agreements to preserve the benefits of a single economic space, but they were unsuccessful. Some elements of multilateral cooperation, however, continued to exist. The break-up had forced all newly independent states to build an entirely new customs regime. They had to develop customs procedures and a nomenclature for their products as enterprises became free to source their inputs and sell their outputs irrespective of a central plan. They also had to decide whether or not to introduce import tariffs and for which products if they did. As part of this exercise, CIS countries, in 1992, concluded several specific multilateral agreements to facilitate trade and transit, among which the agreement on Standardisation, Metrology and Certification.

In response to Russia's policy of bilateralism, the other CIS states also started to conclude bilateral agreements to create a network of bilateral free trade agreements. (See table 1.) Initially, these agreements followed the Russian format, with a free trade agreement and accompanying trade and cooperation agreements. Because in these accompanying agreements, countries excluded the most important sectors of their economies, it was impossible to link the network of bilateral agreements into a single free trade area. It is important to note that the wave of bilateralism did not end multilateralism. A multilateral free trade agreement was concluded in 1994. In it, the signatories agreed to eliminate the exemptions that were part of the bilateral agreements and to adopt a single list of exemptions. In this way, the bilateral agreements would gradually merge into a single multilateral free trade agreement. The countries, however, were not willing to give up their reservations and, therefore, the 1994 FTA remained a paper agreement mainly. It is to be noted that Russia failed to ratify the agreement altogether, although it did declare temporary application. In this way, Russia was unbound to the FTA and could decide whether and when to adhere to the obligations of the agreement. The CIS member states also continued to conclude specific issue agreements.

## Increased independence

The Soviet Union had been a closed economy. At the time of the break up, trade predominantly was with other CIS countries; almost 90 per cent of all trade was within the CIS. See table 2.

**Table 2: Share of CIS trade (exports plus imports) in total trade**

	1988*	1994	1996	1998	2000	2002	2003
Armenia	0.89	0.62	0.35	0.27	0.21	0.27	0.21
of which to RF		0.61	0.55	0.75	0.74	0.65	0.73
Azerbaijan	0.86	0.54	0.40	0.38	0.21	0.23	0.23
of which to RF		0.41	0.43	0.47	0.57	0.42	0.45
Belarus	0.86	0.72	0.66	0.69	0.66	0.63	0.63
of which to RF		0.81	0.80	0.85	0.86	0.92	0.94
Georgia	0.86	-	0.44	0.39	0.37	0.42	0.37
of which to RF		-	0.46	0.56	0.48	0.37	0.39
Kazakhstan	0.86	0.65	0.61	0.43	0.36	0.32	0.32
of which to RF		0.73	0.79	0.78	0.82	0.77	0.76
Kyrgyzstan	0.87	0.73	0.65	0.50	0.48	0.46	0.47
of which to RF		0.31	0.35	0.43	0.39	0.40	0.45
Moldova	0.88	0.80	0.64	0.53	0.43	0.54	0.46
of which to RF		0.61	0.60	0.66	0.61	0.52	0.49
Russia	0.58	0.22	0.23	0.21	0.19	0.17	0.18
Tajikistan	0.86	0.51	0.50	0.55	0.64	0.50	0.44
of which to RF		0.28	0.21	0.21	0.39	0.34	0.31
Turkmenistan	0.89	0.74	0.51	0.39	-	-	-
of which to RF		0.07	0.20	0.26	-	-	-
Ukraine	0.79	0.65	0.58	0.44	0.44	0.38	0.38
of which to RF		0.80	0.77	0.82	0.75	0.71	0.74
Uzbekistan	0.86	0.62	0.40	-	-	-	-
of which to RF		0.50	0.57	-	-	-	-

Sources: own calculations on CIS statistical yearbooks, 1994, 1996, 1998, 2000, 2002, 2003. Tables: Eksportno-importnie operatsii gosudarstv sodruzjestva; \*Van Selm, 1997, table 4.3

An exception has to be made for Russia, which already traded more extensively with other countries, although mostly with the partners of the CMEA. As is indicated in table 2, the share of CIS trade in total trade gradually declines in the 1990s. In 2003, the share of CIS trade in total trade was between 21 per cent (Armenia) and 63 per cent (Belarus) with Russia again being the exception at a level of 17 per cent. As before, Russia still is the most important trading partner within the CIS and its share of CIS trade remains fairly constant since the dissolution of the CIS. Using a gravity approach towards trade, several authors expect an even larger decline of intra-CIS trade (Djankov and Freund, 2003, Elborgh-Woytek, 2003) Trade shares, however, seem to have stabilised, with some countries actually trading relatively more with other CIS countries in recent years. The gravity approach seems to underestimate the importance of the historical and institutional commonness of the CIS.

This notwithstanding, intra-CIS trade has declined considerably and the member states are trading more in the world market than ever before. It is, therefore, not surprising that all but Turkmenistan have applied for WTO membership. Armenia, Georgia, Moldova and Kyrgyzstan already have acquired membership. Neither is it surprising that the member states have become more selective with respect to obligations that they are willing to accept within the CIS. But it did not stop them entirely. Although a multilateral free trade area itself was not created in 1994, the CIS states continued to work together to move towards that end. They concluded several multilateral agreements that all member states signed and ratified, but continued to follow a pragmatic approach. They accepted what they considered beneficial and

did not participate if it did not service their goals. It is interesting to note that it became more difficult to get unanimous support for agreements, even if they were of a technical nature. Initially, the more technical trade issues such as standards and certification, simplification and unification of procedures for customs clearance at borders, the single commodities nomenclature, transit through the CIS countries, and so on were accepted unanimously. Later agreements generally are not ratified by all CIS members, even if they are of a more technical nature. See table 3.

**Table 3: Key multilateral agreements in force related to CIS free trade**

<i>Multi-lateral agreements</i>	<i>AM</i>	<i>AZ</i>	<i>BY</i>	<i>GE</i>	<i>KG</i>	<i>KZ</i>	<i>MD</i>	<i>RU</i>	<i>TM</i>	<i>TJ</i>	<i>UA</i>	<i>UZ</i>
<b><i>General (framework) agreements</i></b>												
On the Principles of Customs Policy, 13.03.1992	s	–	R	–	–	s	s	s	s	R	–	R
Treaty on the Economic Union, 24.09.1993	R	R	R	R	R	R	R	R	R	R	–	R
On the Free Trade Area, 15.04.1994	R	R	R	R	R	R	R	s	s	R	R	R
Protocol Amending the Agreement on the Free Trade Area, 2.04.1999	R	R	R	R	R	R	R	s	–	R	R	R
<b><i>Specific issue agreements</i></b>												
On Standardization, Metrology and Certification, 13.03.1992	R	R	R	R	R	R	R	R	R	R	R	R
On Rules of Origin, 24.09.1993(Decision)	R	R	R	–	R	R	R	R	R	R	R	R
On the Re-export of Goods, 15.04.1994	R	R	R	s	R	R	s	R	s	R	s	R
On Co-operation in Customs Affairs, 15.04.1994	R	R	R	s	R	R	R	R	s	R	R	R
On the Foundations of Customs Legislation, 10.02.1995 (Decision)	s	R	R	s	R	R	s	R	–	R	s	R
On the Single Commodities Nomenclature, 3.11.1995	R	R	R	R	R	R	R	R	R	R	R*	R
On The Principles of Indirect Taxation, 25.11.1998	R	R	R	s	R	–	R	–	R	R	–	–
On Rules of Transit, 4.06.1999	R	R	R	s	s	R	R	R	–	R	R	s
On the Procedure for Customs Clearance and Customs Control, 8.10.1999	R	R	s	s	R	R	R	R	–	R	R	s
On the Technical Barriers in the Free Trade Area, 20.06.2000	R	R	R	s	R	R	R	s	–	R	s	s
On Rules on Origin, 30.11.2000 (Decision)	R	R	R	R	R	R	R	R	–	R	R	–
On the Rules for Licensing Imports, 30.11.2000 (Protocol)	R	R	R	s	s	s	–	s	–	R	R	–

*Source:* Own compilation.

s – signed (acceded); R – ratified (or other transformation procedure); – neither; R\* - denounced participation

In 1999, a second attempt to a multilateral free trade agreement was agreed upon, when the CIS member states signed a protocol amending the 1994 FTA. This protocol is more explicit with regard to the elimination of exemptions than the FTA of 1994 in that it requires the member states to conclude new bilateral protocols within twelve months with the purpose of agreeing schedules for gradual elimination of existing exemptions. It prohibited the introduction of any barriers in addition to the ones agreed in earlier bilateral documents. Furthermore, it shows that the CIS members are becoming part of the world economy. In line with rules of GATT/WTO, the 1999 FTA laid down that exemptions to the trade regime should not be applied on an arbitrary or discriminatory base. Finally, the protocol defines

quantitative restrictions and other measures of equivalent effect, which in the FTA of 1994 were left out. The 1999 FTA shared the same destiny as its predecessor because Russia, still the most important member of the CIS, again preferred to keep its options open and did not ratify the agreement. Russia again did declare temporary application.

Russia's reservation towards common policies is illustrated very well in its policy towards indirect taxation. With respect to the Value Added Tax (VAT), the international practice is to apply the destination principle; taxes are levied in the country of final consumption. Exporting countries, therefore, have to reimburse the VAT that they may have collected already if a product crosses its border. Of course, it may collect taxes on the full value of the imports. For countries with a balance of payment equilibrium, the loss of taxes through exports is compensated by the gain of taxes on imports. Using the destination principle creates a level playing field between imported goods and locally produced goods. Russia, however, has a large balance of payment surplus and therefore prefers to use the origin principle, in which the country in which the product is produced collects the VAT. Its exports then are taxed. Any value that is subsequently added to the imports in the importing country automatically fall in the new tariff regime of the importing country and the tax authorities only have to monitor the value that is added in domestic companies (Baer et al., 1996, Shiells, 2005). If indirect taxes are similar between trading partners and there is balance of payment equilibrium it does not make a difference which principle prevails, but, as indicated above, Russia has a balance of payment surplus with the CIS countries. Applying the destination principle in the VAT, would allow the importing countries to tax value that was actually added in Russia. In that way Russia indirectly subsidises the importing countries.

The application of the destination principle does, however, require a well functioning customs registration to enable the products to leave a country free of VAT. As indicated above, the CIS countries started their existence without any borders at all and without such a customs registration system. It, therefore, made sense that the CIS countries decided to introduce a dual system. They applied the origin principle for trade to and from other CIS countries, and used the destination principle for trade with the rest of the world. With the introduction of a customs regime it became possible to apply the destination principle and gradually, during the 1990s, the CIS countries switched to the destination principle for trade with the CIS as well. Given its trade surpluses, Russia was reluctant to follow and continued to use the origin principle until 2001, and then only for its non-energy exports. This resulted in Russian imports often being taxed twice, depressing trade. In 2004, energy trade was brought under the destination principle as well. This did not prevent Russia to levy export taxes on its energy exports.

The increased independence of the CIS member states towards each other and towards Russia also shows in sub-regional undertakings. Georgia, Ukraine, Uzbekistan, Azerbaijan and Moldova, in 1996 created GUUAM with the intention of creating a free trade area. Belarus, Kazakhstan, Kyrgyzstan, Russia and Tajikistan, in 2000, created the Eurasian Economic Community with a similar goal, and Belarus, Kazakhstan, Russia and Ukraine, in 2003 created the Single Economic Space, with the signatories disagreeing on the ultimate goal. We will leave the discussion of these regional agreements and their importance for the CIS for another paper. Suffice it at this point, that these sub-regional agreements further complicate the view on the trade regimes in the CIS.

## A view of the future

The confusing pattern of multilateral and bilateral trade agreements induced the UNECE (2005) and Freinkman et al. (2004) to advise renegotiation of free trade agreements, particularly moving from a system of bilateral free trade agreements to an effective multilateral agreement and to replace the 'spaghetti bowl' of transit and customs agreements by straightforward and clear multilateral ones. That is easier said than done. The Soviet Union was a union after all, even if it was economically inefficient, and both the legal and the economic ties needed to be dissociated. This required a multilateral approach and the CIS is often regarded as the best institution to oversee such a civilised divorce. The member states acknowledged the benefits of economic cooperation much in the same way that member states of numerous free trade agreements do.

The CIS was burdened with ambivalent goals. On the one hand, it aimed to assist the newly independent countries to gain economic independence, while on the other hand it was the intended institution to bring the newly independent states together in an economic union. The ambivalent character of the CIS, and the increasing self-consciousness, both politically and economically, of the newly independent states, resulted in numerous bilateral and multilateral agreements at the same time. It will be interesting to see whether the more recently concluded sub-regional agreements will circumvent the ambiguous character of the CIS.

Arguably, Russia was and is the most important country in the CIS. It continued to be the major trading partner for all other CIS countries and it continued to subsidise the other member states. Initially, the rouble zone allowed the trade deficit countries to pass the bill to Russia, but even after the rouble zone was broken up, Russia continued to subsidise the other CIS member states as it still exported energy to its CIS partners at favourable prices.<sup>6</sup> Russia's position was crucial in the developments of the CIS. It put an end to the rouble zone, it did not ratify the FTA's, it was the first to conclude bilateral FTA's, and it was the last to change to the destination principle in its treatment of indirect tax on exports. It does so in its economic interests, and it is powerful enough to get its way. The other countries cannot afford to ignore Russia's position. It is still unclear what type of economic cooperation will remain between the CIS countries and what the level and direction of trade between them will be. More research is needed to discuss the economic relations between the member states.

The ambivalence that is built in the CIS, with its pick and mix construction, and the importance of Russia's position in the CIS induced the mixture of agreements that many observers find disturbing. But there are benefits as well. The plethora of options in cooperation and the weakness of the agreements allow member states to dissociate themselves from their past and at the same time associate themselves with their partners. Whether developments in the trade regime will evolve towards the advised increase in coherence is to be awaited. The evidence is mixed. The CIS countries are reluctant to commit themselves to 'hard' arrangements and remain wary of Russia's dominance. Russia itself seems to dissociate itself from its partners, without severing the ties. But new initiatives for cooperation keep appearing and the CIS countries seem to realise that there are still gains in regional cooperation. We do not, however, expect any consolidated multilateral cooperation either in the short or medium term. It is to be noted though, that, for example, the WTO took 50 years to gradually develop into its current structure, and that its structure still evolves.

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<sup>6</sup> In 2004, CIS states pay a little over 50 US\$ (contractual prices including tax and charges) per 1000 cubic meter (cm) for Russian gas, whereas western European countries pay 140 US\$ per 1000 cm. This includes excise tax and customs duties (see Stern, 2005).

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