Hacettepe University Graduate School of Social Sciences

Faculty of Economic and Administrative Sciences

Department of International Relations

THE ROLE OF ENERGY IN EU-RUSSIAN RELATIONS

Aida SULEJMANOVIĆ

Master's Thesis

Ankara, 2014

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To Rasema and Sulejman

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ÖZET

SULEJMANOVIĆ, Aida. *AB-Rusya İlişkilerinde Enerjinin Rolü*, Yüksek Lisans Tezi, Ankara, 2014.

Sözkonusu tez çalışması, Vladimir Putin'in 2000 yılında Rusya başkanı olması ve enerji fiyatlarında süregelen artışla birlikte yeni milenyumda, AB-Rusya ilişkilerinde enerji faktörünün belirleyici rolünü irdelemektedir. Yeni nesil enerji güç politikaları, AB'nin perspektifinden enerji güvenliğini önceledi̇ği, Rusya'nın ise Soğuk Savaş döneminden devraldığı büyük güç konumunu sürdürme hedefi bağlamında AB-Rusya ilişkilerini tanımlayan bir noktaya evrilmektedir. Mevzubahis araştırma, AB-Rusya ilişkilerindeki temel ihtilafın enerji meselesi olduğunu savlamaktadır. Aynı zamanda, AB'nin Rus enerji ürünlerine bağımlılığını ve AB'nin ortak bir enerji politikasından yoksunluğunu irdelemesinin yanısıra Rusya'nın iddialı enerji politikasının AB-Rusya çatışmasına katkıda bulunduğunu varsaymaktadır. Realist paradigma, güç kazanma yarışındaki Rusya ve AB arasında enerji ilişkilerinin neden olduğu çıkar çatışmalarını ve enerji ilişkilerini analiz etmek için kullanılacaktır.

Anahtar Sözcükler

Rusya, AB, Rusya'nın Dış Politikası, AB Enerji Güvenliği, AB Ortak Enerji Politikası, Rekabet, Etki Alanı, Boru Hatları, Gaz Krizler

ABSTRACT

SULEJMANOVIĆ, Aida. *The Role of Energy in EU-Russian Relations,* Master's Thesis, Ankara, 2014.

This thesis aims to study the importance of energy for the EU-Russian relations, with focus on the new millennium when Vladimir Putin became the President of Russia in 2000 and when energy prices increased substantially. The link between energy and power politics has come to characterize EU-Russian relations which are seen through energy security pursuit by the EU and Russia's pursuit to sustain its great power status from the Cold War era. This study argues that the main area of contention in EU-Russian relations is energy. It will analyze how the EU's dependence on Russian energy imports, lack of EU's common energy policy, and Russia's energy foreign policy assertiveness is contributing to EU-Russian conflict. It will be argued that Russia uses energy as a political instrument which prevents the EU from having a common energy policy. Realist paradigm will be used to analyze energy relations and the clash of interests it produces between Russia and the European Union which are seen as rivals that seek to gain power at each other's expense.

Key Words

Russia, EU, Russia's Foreign Policy, EU Energy Security, EU Common Energy Policy, Rivalry, Spheres of Influence, Pipelines, Gas Crises

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LIST OF ABBREVIATIONS

AB:	Avrupa Birliği
APERC:	Asia Pacific Energy Research Centre
BBC:	British Broadcasting Corporation
bcm:	billion cubic meters
BTC:	Baku-Tbilisi-Ceyhan
CEPS:	Centre for European Policy Studies
CER:	Centre for European Reform
CFSP:	Common Foreign and Security Policy
CIEP:	Clingendael International Energy Programme
CIS:	Commonwealth of Independent States
CPB:	Central Planning Bureau
CRS:	Congressional Research Service
CSDP:	Common Security and Defense Policy
CSIS:	Center for Strategic and International Studies
CSS:	Center for Security Studies
DOE:	Department of Energy
DTI:	Department of Trade and Industry
EC:	European Commission
ECT:	Energy Charter Treaty
EEC:	European Economic Community
EIA:	Energy Information Administration
ESCS:	European Coal and Steel Community
EU:	European Union
EURATOM:	European Atomic Energy Community
FOI:	Totalförsvarets forskningsinstitut (Swedish Defence Research Agency)
FRIDE:	Fundación para las Relaciones Internacionales y el Diálogo Exterior (Foundation for International Relations and Foreign Dialogue)
FSB:	Federal Security Service of the Russian Federation
GDP:	Gross Domestic Product
HKPSA:	Hong Kong Pen Spinning Association
IEA:	International Energy Agency
IGU:	International Gas Union

ISAC:	International and Security Affairs Centre
KGB:	Committee for State Security
LNG:	Liquefied Natural Gas
LSE EUROPP:	London School of Economics European Politics and Policy
NATO:	North Atlantic Treaty Organization
NISA:	National Industrial Scale Association
OECD:	Organization for Economic Cooperation and Development
OPEC:	Organization of the Petroleum Exporting Countries
PCA:	Partnership and Cooperation Agreement
RFE/RL:	Radio Free Europe/Radio Liberty
SSI:	Strategic Studies Institute
TANAP:	Trans Anatolian Natural Gas Pipeline
TAP:	Trans Adriatic Pipeline
tcm:	thousand cubic meters
UK:	United Kingdom
UN:	United Nations
UNDP:	United Nations Development Programme
UNESCAP:	United Nations Economic and Social Commission for Asia and the Pacific
U.S.:	United States
USAID:	United States Agency for International Development
USGS:	U.S. Geological Survey
USSR:	Union of Soviet Socialist Republics
WRI:	World Resources Institute
WTO:	World Trade Organization

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CHAPTER 1: INTRODUCTION

The importance of energy supply security was highlighted effectively with 1973 oil crisis which led to global economic crisis. For the first time, shortage of supply fear, rising prices, and reality of energy dependence were felt globally. Importance of energy security became an integral part of national security for industrialized powers of the world which experienced energy shortages due to limits put on energy production by the Organization of the Petroleum Exporting Countries (OPEC). Like Middle Eastern states in oil, in the new millennium, it was suggested that Russia has been using gas as a foreign policy instrument.

The lack of oil and gas resources in the European Union is not a problem in itself. Like other goods, energy can be imported. The difference is that the shortage of energy resources would have far-reaching consequences for the EU economy. It is unlikely scenario, but still, EU institutions seem uneasy by the fact that approximately one third of EU oil and gas imports come from Russia which many Europeans see as reaching for the superpower status. Norway also supplies the EU with significant amount of natural gas but there is no literature that puts Norwegian energy in the negative context. The problem is that dependence on Russian energy is increasingly seen as negative dependence in many EU circles. Moscow has already demonstrated its readiness to halt gas supplies to countries like Ukraine and Belarus in order to achieve their economic and political goals. Many experts argue that energy gives Russia leverage to be seen as a great power.[1] With Vladimir Putin becoming the President in 2000, new age of energy power politics has come to characterize EU-Russian relations. Boris Yeltsin's 1990s and an easy access to Russian energy wealth were over, much to EU's dismay.

The European Union and Russia are not as powerful as they used to be.[2] The EU is struggling to maintain its unity and soft power status while Russia is attempting to translate energy wealth

[1] Javier Morales, "Russia as an Energy Great Power: Consequences for EU Energy Security," in *Energy Security: Visions from Asia and Europe*, ed. Antonio Marquina (New York, NY: Palgrave Macmillan, 2008), 26; Jeronim Perovic, "Introduction: Russian Energy Power, Domestic and International Dimensions," in *Russian Energy Power and Foreign Relations: Implications for Conflict and Cooperation*, ed. Jeronim Perovic, Robert W. Orttung and Andreas Wenger, CSS Studies in Security and International Relations (New York, NY: Routledge, 2009), 8; Viatcheslav Morozov, "Energy Dialogue and the Future of Russia: Politics and Economics in the Struggle for Europe," in *The EU-Russian Energy Dialogue: Europe's Future Energy Security,* ed. Pami Aalto, The International Political Economy of New Regionalisms Series (Aldershot: Ashgate, 2008), 55.

[2] Roderic Lyne, "Russia at the Crossroads: Again?," *The EU-Russia Review* 1 (Brussels: EU-Russia Centre, 2006), 9, http://www.isn.ethz.ch/Digital-Library/Publications/Detail/?ots591=0c54e3b3-1e9c-be1e-2c24-a6a8c7060233&lng=en&id=48824; Douglas Webber, *Declining Power Europe? The Evolution of the European Union's World Power in the Early 21st Century*, Working Paper Series 2014/1 (Melbourne: Monash University European and EU Centre, 2014), http://artsonline.monash.edu.au/europecentre/download/Working%20Papers%202014%2001.pdf.

into political influence. The stage for conflict is set by the fact that they mostly exercise their power in the former Soviet Union countries which are forced to choose alignment with either the EU or Russia. EU institutions have engaged in attempts to decrease the Union's dependence on Russian energy (mainly gas) given the fact that Russia's budget is greatly supplied by energy earnings from EU markets. On the other hand, Russia is attempting to translate this energy wealth into political influence. Collecting substantial wealth from its energy exports to the EU and building its power, Russia has come into position to play one European power against another due to the fact that profits are not always Moscow's main objective. The EU Member States keep playing Moscow's game by signing long-term bilateral deals with Russia and building new pipelines for Russian gas to reach Europe, therefore effectively undermining Eastern European countries' national security (including the EU Member States) by leaving them exposed to Russia's political influence because with new pipelines circumventing their territories, they lose transit leverage over Russia.

This thesis studies EU-Russian relations seen through energy security pursuit by the EU and Russia's pursuit to sustain its great power status from the Cold War era. It first examines the EU's attempts to have common internal and external energy policies within the Union. It then continues with examination of Russia's energy policy and whether it is used as a foreign policy instrument, followed by the conflict between the EU's and Russia's energy policies and what this means for the region, and finally, general prospects for the future of EU-Russian energy relations.

The main research question of the thesis is "To what extent are the energy security pursuit of the EU and the great power pursuit of Russia conflicting?" The dependent variable is the conflict between the EU and Russia. The independent variables are the energy policies of both shaped by their energy security understandings. But, since what they understand from energy security is different, they base their energy policies on different grounds. Questions complementing the main research question are:

- How dependent is EU on Russian energy?
- Does Russian energy constrain the EU's ability to have common energy policy?
- Why does Russia see energy as a tool of foreign policy? How does Russia use energy as a tool?
- How is energy influencing EU-Russian relations?

1.1. SCOPE AND OBJECTIVE

By way of historical background, this thesis will briefly mention the decade of 1950s which was the beginning of the European Union as we know it today. It will be shown that at its origin, energy considerations played an important part in the unification of Europe. The thesis will also briefly focus on decades of 1960s, 1970s and 1980s which were the beginning of energy relations between Russia and Europe. Those decades saw the construction of gas pipelines, connecting the Soviet Union and countries which will later become the EU. In 1993, the Maastricht Treaty was signed, establishing the European Union. There have been attempts to arrive at common energy policy within the Union for the past 20 years.

In 1991, the Russian Federation emerged following disintegration of the Soviet Union in the same year. EU-Russian energy relations during 1990s were shaped by the fact that the EU was experiencing economic prosperity while Russia was going through severe economic crisis. The EU had an easy access to cheap energy resources coming from Russia while Russia was struggling with economic crisis. Analysis will continue with Vladimir Putin becoming the President in 2000, the rise in energy prices in the new millennium, and the rise of resource nationalism in Russia. It will be argued that this set the stage for political conflict in EU-Russian energy relations. It will be shown that while there are attempts to strengthen the Union from within in energy matters, Moscow is attempting to promote EU disunity in order to achieve their geopolitical goals.

There are two views on EU-Russian energy relations. One group of authors is of the opinion that Russia has the upper hand in EU-Russian energy relations.[3] There is no mutual dependence. The EU's dependence on Russian energy imports transcends mere energy dependence. The EU's dependence on Russian energy has the risk of turning into political dependence as well. The other group of authors argues that EU-Russian energy relations are characterized by mutual dependence.[4] As much as the EU needs Russian energy, Russia needs hard currency earnings from energy sales to the EU in order to stabilize its economy and country.

The first group is represented by authors such as Martin Malek[5] who explains that Russia's energy disputes of 2006, 2007 and 2009 with Ukraine and Belarus demonstrated Europe's

[3] Martin Malek, "The EU as a "Target" of Russia's "Energy Foreign Policy"," in *The European Union – A Global Actor?,* ed. Sven Bernhard Gareis, Gunter Hauser and Franz Kernic, Global Leadership Series (Leverkusen: Barbara Budrich, 2013).
[4] Stacy Closson, "Russia's Key Customer: Europe," in *Russian Energy Power and Foreign Relations,* ed. Perovic, Orttung and Wenger.
[5] Malek, "The EU as a "Target"."

weakness in its dependence on Russian gas exports. He also states that those gas disputes demonstrated the EU's weakness when put against increasingly assertive Russia's foreign policy. Malek finds it incomprehensible that EU states are openly promoting Russia's goals targeted at weakening the EU unity such as *Nord Stream* and *South Stream* pipeline projects. According to him, Russia's claim to being a superpower is drawn less from the military power and more from becoming an energy superpower. He states that Russia is pursuing policies that would make as many countries as possible dependent on its energy which could then be turned into political dependencies. Author states that there is no mutual dependence between the EU and Russia since Russia can afford to shut down gas deliveries for few days while many EU countries would find themselves in serious problems.

The second group of authors includes Stacy Closson.[6] Contrary to popular Western opinion that Russia is a threat to European energy security, she argues that Russia has a better chance of becoming more dependent actor in future EU-Russian energy relations. The EU is Russia's main trade partner in both imports and exports; therefore, the EU is Russia's main source of hard currency earnings. However, due to EU's inaction to properly address Russian assertiveness, Russia has managed to create an illusion of having an upper hand in EU-Russian relations. Russia has successfully created an appearance that there is a one-way dependency in EU-Russian energy relations in which the EU is dependent on Russia. This illusion is spread by the Western media as well. In reality, the author argues, EU-Russian energy relations are characterized by binding interdependence which is likely to promote conditions for future cooperation rather than confrontation. Just as the EU needs Russian gas, Russia needs EU markets because most of its export infrastructure is turned towards Europe. Closson does not exclude the possibility of confrontation, but she argues that middle ground approach of both conflict and cooperation existing together in EU-Russian energy relations is likely to continue.

1.2. ARGUMENT

This thesis argues that the main area of contention in EU-Russian relations is energy. The EU and Russia are attempting to strengthen their international status at each other's expense. This thesis illustrates the clash of opposing goals; energy security pursuit of the EU and great power pursuit of Russia. It will be argued that Russia uses energy as a political instrument which prevents the EU to have a common energy policy.

[6] Closson, "Russia's Key Customer."

Primary energy resources such as oil and gas have been identified as important elements of state power. More resources make state more powerful and influential. State power based on energy resources is conditioned on the state's ability to extract and supply those resources and on the global demand.[7] This view of identifying energy resources as material elements of power has led energy and security experts such as Gal Luft and Anne Korin to the conclusion that the most suitable way of analyzing energy resources in the field of foreign relations is through two theories: Realism or Idealism (Liberalism).[8]

This thesis will make use of the insights of Realism which treats energy resources as material objects, belonging to materialistic ontology.[9] Realist paradigm "suggests that energy resources are power elements included in states' foreign policy when states seek to expand influence abroad."[10] Given that this thesis will deal with conflict involving energy resources and foreign energy policies, it is the most suitable theory to analyze energy relations and the clash of interests it produces between two powers – Russia and the European Union. This thesis will show the EU and Russia as rivals that seek to gain power at each other's expense. During 1990s, the EU was able to experience economic prosperity due to low energy prices (including low price paid for Russian energy resources). While the EU was experiencing economic prosperity, Russia was facing severe economic downturn. In the new millennium, with high energy prices, the EU has become a major contributor to Russia's substantial energy profits, leading to Russia's economic prosperity. The EU economy, on the other hand, has become less competitive globally due to the high price it pays for energy resources (including energy resources from Russia).

All strands of Realism share the same core and this core consists of concepts such as power politics, security, self-help and anarchy. They recognize constraints on politics resulting from human egoism to some degree and the absence of international government to rule over states. This requires power and security to take primacy in all political life.[11] The EU faces many obstacles in acting together on some of the most important issues (such as energy) because the

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[7] Giedrius Česnakas, "Energy Resources in Foreign Policy: A Theoretical Approach," *Baltic Journal of Law & Politics* 3, no. 1 (2010): 31, http://www.degruyter.com/view/j/bjlp.2010.3.issue-1/v10076-010-0003-y/v10076-010-0003-y.xml.

[8] Gal Luft and Anne Korin, "Realism and Idealism in the Energy Security Debate," in *Energy Security Challenges in the 21st Century: A Reference Handbook*, ed. Gal Luft and Anne Korin, Contemporary Military, Strategic, and Security Issues (Santa Barbara, CA: ABC-CLIO, 2009), quoted in Česnakas, "Energy Resources in Foreign Policy," 31-32.

[9] Česnakas, "Energy Resources in Foreign Policy," 31.

[10] Ibid., 30.

[11] Robert Gilpin, "The Richness of the Tradition of Political Realism," in *Neo-Realism and Its Critics*, ed. Robert O. Keohane, New Directions in World Politics (New York, NY: Columbia University Press, 1986), 305, quoted in Jack Donnelly, "Realism," in Scott Burchill et al., *Theories of International Relations*, 3rd ed. (New York, NY: Palgrave Macmillan, 2005), 30.

EU still consists of sovereign states that look after their own national interests. However, in world affairs, more benefits could be gained by acting together. Also acting together with the United States under the widely used banner of "The West", they have more power to contain Russia and China in their open pursuit to spread their influence and gain access to natural resources in energy-rich region of Eurasia which the European Union sees as strategically important for its energy security.

The fundamental statement of the Realist paradigm is that pursuit of power is the principal objective of states.[12] The EU and Russia exercise their power in different ways. The EU prefers enlightened diplomatic influence whereas Russia frequently chooses coercion.[13] The EU prefers market approach for their energy security in which energy supply and demand decisions are mostly left to market forces. Russia prefers strategic approach in which Moscow decides on the flow of energy. Besides enjoying the benefits of power that energy wealth brings, Russia is also becoming more assertive in world affairs in addition to its permanent seat in the UN Security Council. This thesis will show how Russia is in the process of demonstrating its power in the existing international order while the EU is struggling to maintain its. It will be shown that energy relations between the EU and Russia play an important role in this process.

The tradition that Realism sometimes borrows from and which is important for understanding the struggle and conflict over energy between Russia and the EU is geopolitics, which studies the relationship between geography and politics, focusing on interaction among states and their foreign policies in a given geographical setting. Geopolitics attaches strategic value to air space, land and sea areas, and puts them in the context of struggle for power and territory.[14] The EU and Russia, besides having bilateral issues, are also engaged in the international struggle for influence and control of geographical and geopolitical spaces found in their proximity.[15] For Realists, energy is not an economic issue that should be left to market forces to be regulated by demand, supply and prices. In the Realist theory, government control over energy production and supply is the cornerstone of national energy security.[16]

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[12] Richard Ned Lebow, "The Long Peace, the End of Cold War, and the Failure of Realism," *International Organization* 48, no. 2 (1994): 263, http://www.jstor.org/stable/2706932.

[13] Antonio Marquina and Mely Caballero-Anthony, "Human Security: European and Asian Approaches," in *Energy Security*, ed. Marquina, 247.

[14] Francis P. Sempa, "Introduction: The Geopolitics of History," in Francis P. Sempa, *Geopolitics: From the Cold War to the 21st Century* (New Brunswick, NJ: Transaction Publishers, 2002), 3, 5.

[15] Roland Dannreuther, *International Relations Theories: Energy, Minerals and Conflict*, POLINARES Working Paper, no. 8 (Dundee: University of Dundee, Centre for Energy, Petroleum and Mineral Law and Policy, 2010), 2, http://www.polinares.eu/docs/d1-1/polinares_wp1_ir_theories.pdf.

[16] Christian von Campe, "Energy Security in the United Kingdom" (dissertation, University of Aberdeen, 2011), 36, http://archive.atlantic-community.org/app/webroot/files/articlepdf/UKenergy.pdf.

1.3. ORGANIZATION OF CHAPTERS

The first chapter of the thesis is an introductory one addressing scope, objective and argument of the thesis.

The second chapter will make use of the Realist theory to better understand energy security. The first part of the chapter gives general introduction on various strands of the theory. The second part focuses on the meaning of energy security found in literature, with emphasis on Realist interpretation.

The third chapter analyzes the EU's road to common energy policy which would lead to improved energy security within the Union. Common energy policy would improve the movement of energy resources within the Union, leading to better security for the majority of Member States which are not powerful enough to decide on channels through which their energy resources are delivered. The first part of the chapter maps two decades of attempts to arrive at common energy policy within the EU. The second part analyzes the importance of Moscow's energy policy for the efforts to have common energy policy in the EU. The third part looks at the EU's ongoing attempts to diversify energy supply sources. In this chapter answers to two research questions will be provided: How dependent is EU on Russian energy?; Does Russian energy constrain the EU's ability to have common energy policy?.

The fourth chapter examines the role of energy in Russian foreign policy. The first part of the chapter analyzes the link between energy sector and politics. The second part looks at challenges facing Russian energy sector. This chapter will provide answers to two research questions: Why does Russia see energy as a tool of foreign policy?; How does Russia use energy as a tool?.

The fifth chapter examines the EU's and Russia's energy policies and relation between them. The first part of the chapter looks at the history of EU-Russian energy relations. The second part of the chapter looks at the conflict of power aspirations. The third part analyzes the politics of gas pipelines and their overall importance. The fourth part examines the nature of EU-Russia energy conflict. The fifth part will give general evaluation, linking theory with the case of EU-Russia rivalry. In this chapter answer to the main research question and answer to additional research question will be provided: To what extent are energy security pursuit of the EU and great power pursuit of Russia conflicting?; How is energy influencing EU-Russian relations?

The sixth chapter is the final chapter in this thesis and it will summarize all the previously mentioned characteristics of EU-Russian energy relations. It will argue that energy is a major

point of contention in relations between the EU and Russia which are aiming to maintain (EU) and regain (Russia) their international prestige.

CHAPTER 2: THEORETICAL FRAMEWORK: REALISM AND ENERGY SECURITY

Since this thesis will utilize the Realist perspective to analyze EU-Russian energy relations, this chapter will provide historical background on the Realist theory, its main concepts will be defined, and its main strands will be outlined. Also important for the analysis is the concept of energy security. Broad meaning and various definitions and explanations will be provided of the concept since different international actors attach different meaning to it.

2.1. REALISM

Traditionally, Realism has been focused on defining international security.[17] It is a theory dedicated to explaining state behavior in the international system because for Realists, structure of the system dictates behavior of states in international relations.[18] Mixture of human egoism and anarchy which leads to power politics provides the core of Realism.[19] It is a theory preoccupied with states, anarchy, power, security, self-help, and survival. Statesmanship entails, not eliminating, but managing the conflict.[20] It seeks to create less dangerous world instead of just and peaceful world.

Powerful nation-states are the central focus of Realist analysis. International organizations and other groups are thought to be instruments to serve interests of the most powerful states in the international system. States are assumed to be rational actors. They find themselves existing in the international system without higher authority. Self-help is the principle by which they operate in this system. National interests overthrow any other consideration in this environment. Each state is responsible for its own well-being and survival. Survival is not guaranteed because war is a legitimate instrument of state-craft.[21] Absence of government over and above states in international relations is called anarchy. Realists assume that anarchic system forces all states to

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[17] Andrei V. Belyi, ed., *Energy Security in International Relations (IR) Theories*, Course Reader (Moscow: National Research University, Higher School of Economics, 2007), http://webcache.googleusercontent.com/search?q=cache:Pqj5n7qhbMoJ:www.hse.ru/data/339/636/1233/ReaderforLecturesOnEnergySecurity.doc+&cd=1&hl=tr&ct=clnk&gl=ba.

[18] Kenneth N. Waltz, *Theory of International Politics*, Addison-Wesley Series in Political Science (Reading, MA: Addison-Wesley, 1979), 117; Robert Jackson and Georg Sørensen, "Realism," in Robert Jackson and Georg Sørensen, *Introduction to International Relations: Theories and Approaches*, 5th ed. (Oxford: Oxford University Press, 2013), 79.

[19] Donnelly, "Realism," 30.

[20] Ibid., 31.

[21] Tim Dunne and Brian C. Schmidt, "Realism," in *The Globalization of World Politics: An Introduction to International Relations*, 2nd ed., ed. John Baylis and Steve Smith (New York, NY: Oxford University Press, 2001), 142.

adjust their foreign policies to this worldview and act rationally.[22] The alternative would be ceased existence. Anarchy does not mean chaos however. It means that there is no higher authority ruling over states. Due to uncertain nature of the anarchic system, Realists do not believe in the possibility of permanent alliances. Any form of dependence therefore is a weakness that jeopardizes independence of state's policies and national interests. Dependences should be managed carefully.

Due to condition of anarchy in which they exist, states are preoccupied with survival and struggle for power. More powerful states have a better chance of survival in anarchical environment. States compete for power among themselves. It is a zero-sum competition. More power for one state means less for another. In short, Realists view international politics as an arena of conflict between sovereign states struggling to survive.[23]

Combination of anarchy and survival struggle leads to another highlight of Realism – balance of power. Balance of power is a mechanism described by Realists throughout the centuries as being essential to preserve liberty of states.[24] It is a mechanism in which relatively weak unite to counter the power of relatively strong.[25] However, Realists also agree that this is not a stable condition.[26]

Another distinguishing feature of Realism is its pessimism.[27] Realism has low regard for human reason, as such, it is highly skeptical of the possibility of any real progress in international relations. Timeless wisdom of Realism is that certain patterns repeat over time. In short, history repeats itself.

Realism has been identified as the oldest theory of international relations.[28] It can be traced back to ancient times and writings of Thucydides in ancient Greece. His account of the war between Athens and Sparta is considered a classic Realist analysis. Thucydides is considered to be the father of Political Realism and along with Hans J. Morgenthau, the most important thinker of Classical Realism.[29] Other thinkers such as Niccolo Machiavelli, Thomas Hobbes, Jean Jacques

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[22] Jackson and Sørensen, "Realism," 66.
[23] Ken Booth, *Theory of World Security*, Cambridge Studies in International Relations (New York, NY: Cambridge University Press, 2007), 158.
[24] Dunne and Schmidt, "Realism," 144.
[25] Jennifer Sterling-Folker, "Realism," in *Making Sense of International Relations Theory*, ed. Jennifer Sterling-Folker (Boulder, CO: Lynne Rienner, 2005), 14.
[26] Dunne and Schmidt, "Realism," 153.
[27] Sterling-Folker, "Realism," 13.
[28] Donnelly, "Realism," 29.
[29] Richard Ned Lebow, "Classical Realism," in *International Relations Theories: Discipline and Diversity*, 2nd ed., ed. Tim Dunne, Milja Kurki and Steve Smith (New York, NY: Oxford University Press, 2010), 60.

Rousseau, and later Edward Hallett Carr, have been identified as classical Realists as well, in order to claim timeless limitation of human reason and its ability to achieve moral progress.[30] This claim represents the linchpin for all strands of Realism. These thinkers identified security and self-interest as primary motives for both individual and interstate conflicts.[31]

As the study of International Relations evolved over 20th century, so did School of Realism. Original teachings and ideas that were developed within the school are now known under the banner of Classical Realism. It assumes that human lust for power is the motivation for conflict.[32] Flawed human nature creates insecurity that often leads to conflict. Classical Realists recognize the central role that power has in politics of all kind. They also stress limitations of power and how easily it can be made self-defeating.[33] Classical Realism points to similarities between domestic and international politics and concerns itself with questions of order, justice and change at both levels.[34] It stresses the importance of ethics and community in maintaining stability at both domestic and international levels.

By the end of the 1970s new strand of Realism has emerged under the name of Neorealism. Kenneth Waltz was its main thinker. He stressed the importance of the structure of the international system and marginalized domestic politics.[35] Keeping up with popularity of positivist philosophy of that time, Neorealism is the most scientifically conscious strand of Realism.[36] Considerations for justice and morality were found to be inappropriate for the study of international relations. Neorealism emerged at a time when apparent stability of bipolar world created by the Cold War needed explanation. Breaking up with the classical Realist tradition, Neorealism stresses that insecurity and conflict appear not because of the flawed human nature that craves power and domination, but because of the structure of the international system. Because structure of the international system is given as the main explanation for the occurrence of conflict, Neorealism is also known as Structural Realism.[37] Structural Realism posits that states are concerned with relative gains rather than absolute, meaning that they are also concerned with gains of other states besides their own.[38] Existing in a self-help world where relative gains are important, cooperation is difficult to achieve. The only way to achieve security

[30] Sterling-Folker, "Realism," 15.
[31] Jeffrey W. Taliaferro, "Neoclassical Realism: The Psychology of Great Power Intervention," in *Making Sense of International Relations Theory*, ed. Sterling-Folker, 41.
[32] Sterling-Folker, "Realism," 15.
[33] Lebow, "Classical Realism," 58.
[34] Ibid., 59.
[35] Waltz, *Theory of International Politics.*
[36] Lebow, "The Long Peace," 250.
[37] Dunne and Schmidt, "Realism," 148.
[38] Ibid., 154.

is through self-help.[39] But, in the process of ensuring one's own security, other states in the system will feel insecure. This is known as security dilemma. The mechanism through witch security dilemma can be lessened is balance of power.

Within school of Neorealism debate has emerged between defensive structural Realists led by Kenneth Waltz and offensive structural Realists led by John J. Mearsheimer. The debate is about whether security maximization (Defensive Realism) or power maximization (Offensive Realism) is the main concern of states. Defensive Realists recognize that states compete for power, but being more concerned with security maximization they strive to acquire only so much power as they deem appropriate for their security needs. Offensive Realists see states as being concerned with power maximization. In this view, international system is composed of revisionist states that wait for convenient opportunity to engage in expansionist policies in order to increase their power.

The end of the Cold War ended the popularity of Neorealism since it was a theory mainly concerned with explaining the bipolar stability during the Cold War. Peaceful system change encouraged Realists to turn back to the wisdom of Classical Realism. Neoclassical Realism emerged as a fusion of Neorealism and Classical Realism.[40] Neoclassical variant of Realism stresses the importance of anarchy, relative power, and security,[41] but it also brought back the effects of prestige motivation and status into Realist analysis.[42] While Neorealism seeks to explain international political outcomes resulting from actors interacting in the international system, Neoclassical Realism seeks to explain why states pursue particular strategies.[43] Therefore, Neoclassical Realism is a theory of foreign policy. It states that relative distribution of material powers shapes foreign policy behavior of states.[44]

School of Realism does not have a clear definition of national power. Many experts consider Morgenthau's analysis of national power to be the most elaborating. Morgenthau reviewed physical and political capabilities of states that make up national power. These are: size, population, morale, military preparedness, natural resources, industrial capacity, national character, and the quality of diplomacy and government.[45] Morgenthau maintains that all these

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[39] Ibid., 153.
[40] Taliaferro, "Neoclassical Realism," 40.
[41] Scott D. Sagan and Kenneth N. Waltz, *The Spread of Nuclear Weapons: A Debate Renewed*, 2nd ed. (New York, NY: W.W. Norton & Company, 2003), 210, quoted in Taliaferro, "Neoclassical Realism," 40.
[42] Taliaferro, "Neoclassical Realism," 41.
[43] Ibid., 40.
[44] Ibid., 38.
[45] Hans J. Morgenthau, *Politics Among Nations: The Struggle for Power and Peace* (New York, NY: Alfred A. Knopf, 1948), 106-144, quoted in Lebow, "The Long Peace," 255.

components are important parts of national power, however, he does emphasize that industrial capacity (for his lifetime at least – 1904-1980) is defining characteristic of great powers.

In Realism, if power is treated as influence, then power is defined as the ability to influence the behavior of others – to make them do what they otherwise would not have done. This is achieved through military force and economic sanctions. Power does not equal influence, but rather, it is the potential to influence others. Many Realists believe that this potential rests on specific characteristics of states, such as state size, national income, GDP, and military preparedness. In this way, power is defined as capability.[46] "Capabilities give a state the potential to influence others only to the extent that political leaders can mobilize and deploy these capabilities effectively and strategically."[47] This depends on national will, diplomatic skill, and government's legitimacy.[48] Some Realists highlight power of ideas, defining it as "the ability to maximize the influence of capabilities"[49] through a process that includes "the domestic mobilization of capabilities"[50] through religion, ideology, and nationalism.[51] "International influence is also gained by forming the rules of behavior"[52] and values, which, if widely shared among other states, will influence others. This kind of power has been called soft power.[53] Power is also described as a relational concept, meaning that state has power only relative to other states' powers – relative power.[54] Long-term elements of state power are GDP, population, territory, geography, natural resources, political culture, patriotism, education of the population, strength of the scientific and technological base, and credibility of its commitments.[55] Short-term elements of state power are military force, military-industrial capacity to produce weapons, the quality of state's bureaucracy, with economic strength, diplomatic skill and moral legitimacy counted as factoring into military power.[56] "The use of geography as an element of power is called geopolitics."[57] States increase their power by using "geography to enhance their

[46] Joshua S. Goldstein and Jon C. Pevehouse, "Realist Theories," in Joshua S. Goldstein and Jon C. Pevehouse, *International Relations*, 10th ed. 2013-2014 update (New York, NY: Pearson/Longman, 2014), 45, http://www.pearsonhighered.com/assets/hip/us/hip_us_pearsonhighered/samplechapter/0205972152.pdf.
[47] Ibid., 46.
[48] Ibid.
[49] Ibid.
[50] Ibid.
[51] Ibid.
[52] Ibid.
[53] Joseph S. Nye, Jr., *Bound to Lead: The Changing Nature of American Power* (New York, NY: Basic Books, 1990), quoted in Goldstein and Pevehouse, "Realist Theories," 46.
[54] Goldstein and Pevehouse, "Realist Theories," 46.
[55] Ibid., 47.
[56] Ibid., 48.
[57] Ibid., 49.

military capabilities."[58] This is done "by securing allies and bases close to a rival power or along strategic trade routes, or by controlling key natural resources."[59] For example, control of pipelines in Central Asia has become a major geopolitical issue.[60]

Although this study will utilize the theory of Realism, it will be useful to briefly introduce Liberalism. Realists argue that without common power and law there cannot be progress and justice.[61] Liberal theorist Stanley Hoffmann has stated that "The essence of liberalism… is self-restraint, moderation, compromise and peace."[62] However, Liberal ideas have found it difficult to take root in international politics which mostly subscribes to the logic of power politics. In contrast to Realist approach to politics, Liberals believe in the possibility of progress. In general, Liberalism is concerned with the liberty of the individual. This liberty is preserved by the establishment of the state. For Liberals, the state is there to serve the collective and this will be guaranteed by establishment of democratic institutions.[63] Liberalism advocates limited government intervention and freedom of individuals. More specifically, it advocates political freedom, democracy, constitutional rights, people's liberty and equality before the law. Liberalism also champions individual competition in civil society and market capitalism which would ensure that scarce resources are efficiently allocated. This is considered as the best way to promote the welfare in the society.[64] By being a global promoter of those Liberal ideals, the EU has staked its claim on being considered a legitimate "actor" in international relations.

As early as late 17th century, William Penn was advocating Parliament of Europe. Nowadays, his Liberal ideas are compared to the institutions of the European Union. The common Liberal theme in Penn's plans and the Treaty of the European Union is "the importance of submitting the separate wills of individual states to a general will agreed by states acting collectively."[65] Even the ongoing debate about level of European integration can be seen through clash of Liberal principles – integration versus right of state to retain sovereignty over key elements of its social and economic policies.[66]

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[58] Ibid.
[59] Ibid.
[60] Ibid.
[61] Tim Dunne, "Liberalism," in *The Globalization of World Politics*, ed. Baylis and Smith, 163.
[62] Stanley Hoffmann, *Janus and Minerva: Essays in the Theory and Practice of International Politics* (Boulder, CO: Westview Press, 1987), 396, quoted in Dunne, "Liberalism," 163.
[63] Dunne, "Liberalism," 163.
[64] Scott Burchill, "Liberalism," in Burchill et al., *Theories of International Relations*, 55.
[65] Dunne, "Liberalism," 165.
[66] Ibid.

There are three identified patterns of thought of Liberalism: Liberal Internationalism, Idealism, and Liberal Institutionalism.[67] Two main Liberal Internationalists were Immanuel Kant and Jeremy Bentham. Over two centuries ago, they put forward Liberal Internationalist ideas that are still relevant today, more specifically, the belief that freedom and justice in international relations can be achieved through reason. Liberal Internationalists believe that federal contract between states could abolish war and lead to permanent peace.[68] They are also of the opinion that "law-governed international society could emerge without a world government."[69]

Idealism became popular after World War I when it became apparent that peace is not a natural condition in international relations but it must be constructed. In the interwar period, former U.S. President Woodward Wilson promoted an idea that international anarchy can only be managed and peace secured with the creation of the powerful international institution. The League of Nations was such institution, as envisioned by Idealists, to preserve international peace. This institution was supposed to provide collective security to all its members,[70] however, it was not sustainable and the result was World War II and the end of popularity of Idealism.

Liberal Institutionalism became popular after the World War II and the creation of the United Nations. The main Liberal Institutionalist idea was put forth by David Mitrany who argued that "transnational co-operation was required in order to resolve common problems."[71] Cooperation in one sector would make governments desirous to extend cooperation in other sectors as well. This would lead to states becoming more integrated, resulting in more costly withdrawal from such cooperation. This argument has been identified as the core element of Liberal Institutionalism and the key element explaining European integration which started in 1950s. Cooperation in energy sector led to European Economic Community, and finally in 1992, to the European Union.[72]

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[67] Ibid.
[68] Ibid., 165-166.
[69] Ibid., 166.
[70] Ibid., 167.
[71] David Mitrany, *A Working Peace System: An Argument for the Functional Development of International Organization* (Oxford: Oxford University Press, 1943), quoted in Dunne, "Liberalism," 169.
[72] Dunne, "Liberalism," 169.

2.2. DEFINING ENERGY SECURITY

Energy security means different things to different states, organizations, and people. Different actors attach different economic, political, military, technical, and environmental meaning to energy security, depending on their interests, and they attach different policies to it.[73] If energy issues are argued as economic issues then securitization will focus on sufficient energy supply and demand under reasonable prices. If energy issues are argued as a political problem then securitization will focus on political aspects of energy dependence and subsequent danger to state sovereignty.[74] Energy security is difficult to define because it is highly politicized issue. This means that the concept of energy security is broader than merely economic aspect of energy supply, demand, and energy prices.[75] Energy is frequently associated with dependence relationships with political aspects which create security threats.

Narrow and widely used definition of energy security in literature is that it refers to uninterrupted supply of energy under reasonable prices.[76] There are dozens of variations of this definition given by various organizations, state agencies, and institutes. Frequently included in the definition are popular issues such as environment, social quality, competitive markets and research in new technologies.[77]

International Energy Agency (IEA) defines energy security in the following terms:

> … uninterrupted availability of energy sources at an affordable price. Energy security has many aspects: long-term energy security mainly deals with timely investments to supply energy in line with economic developments and environmental needs. On the other hand, short-term energy security focuses on the ability of the energy system to react promptly to sudden changes in the supply-demand balance.[78]

[73] Felix Ciuta, "Conceptual Notes on Energy Security: Total or Banal Security," *Security Dialogue* 41, no. 2 (2010): 133, http://sdi.sagepub.com/content/41/2/123.
[74] Mikko Palonkorpi, "Energy Security and the Regional Security Complex Theory," presentation at the NISA "Power, Vision, and Order in World Politics" conference, University of Southern Denmark, Odense, 23-25 May 2007, 12-13, http://busieco.samnet.sdu.dk/politics/nisa/papers/palonkorpi.pdf.
[75] Ibid., 2.
[76] APERC, *Energy Security Initiative: Some Aspects of Oil Security* (Tokyo: APERC, 2003), 4, http://aperc.ieej.or.jp/file/2010/9/26/Energy_Security_Initiative_2003.pdf.
[77] Benjamin K. Sovacool, "Introduction: Defining, Measuring, and Exploring Energy Security," in *The Routledge Handbook of Energy Security*, ed. Benjamin K. Sovacool (New York, NY: Routledge, 2011), 6.
[78] "Energy Security," IEA, http://www.iea.org/topics/energysecurity/.

United Nations views on energy security are expressed as follows:

> Ensuring energy security will require diversification of types and sources of energy, with increasing focus on consumer needs, on indigenous energy supplies, energy efficiency and regional interconnections.[79]

Asia Pacific Energy Research Centre (APERC) defines energy security in a way that puts emphasis on performance of the economy:

> … ability of an economy to guarantee the availability of energy resource supply in a sustainable and timely manner with the energy price being at a level that will not adversely affect the economic performance of the economy.[80]

World Bank Group defines energy security as follows:

> … energy security means ensuring countries can sustainably produce and use energy at reasonable cost in order to facilitate economic growth and, through this, poverty reduction; and directly improve the quality of peoples' lives by broadening access to modern energy services.[81]

World Resources Institute (WRI) broadens the definition from simply markets and economics explanations to include environmental, geopolitical and social issues:

> The traditional definition of sufficiency, reliability, and affordability now seems incomplete. Environmental sustainability, geopolitical factors, and social acceptability are clearly elements that need to be added to our energy security calculus. A country's energy system is not secure, after all, if it consumes water supplies unsustainably, fuels political instability internationally, or results in strong local opposition.[82]

World Economic Forum defines energy security as follows:

> … conceptualize energy security as having four objectives: *Autonomy*: energy supply that is within the control of a country and is not vulnerable to disruption by external agents; *Reliability*: energy distribution that is safe and secure in both the short and long term and meets demand without interruption; *Affordability*: energy prices that are commensurate with the buying power of domestic and business consumers – at the same time this objective is, however, often difficult to achieve in a manner consistent with the final objective; *Sustainability*: energy use that is sufficient to support a high quality of life but does not damage the environment to an unacceptable degree.[83]

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[79] "Sustainable Energy," UNDP, http://www.undp.org/content/undp/en/home/ourwork/environmentandenergy/focus_areas/sustainable-energy.html.

[80] APERC, *A Quest for Energy Security in the 21st Century: Resources and Constraints* (Tokyo: APERC, 2007), 6, http://aperc.ieej.or.jp/file/2010/9/26/APERC_2007_A_Quest_for_Energy_Security.pdf.

[81] World Bank Group, *Energy Security Issues* (Moscow and Washington, DC: World Bank Group, 2005), 3, http://siteresources.worldbank.org/INTRUSSIANFEDERATION/Resources/Energy_Security_eng.pdf.

[82] Jeffrey Logan and John Venezia, *Policy Note: Weighing U.S. Energy Options: The WRI Bubble Chart* (Washington, DC: WRI, 2007), 1, http://www.compete.org/images/uploads/File/ESIS%20Progressive%20Downloads/WRI%20-%20Weighing%20U.S.%20Energy%20Options,%20July07%202.pdf.

[83] World Economic Forum, *Global Risks 2009: A Global Risk Network Report* (Geneva: World Economic Forum, 2009), 20, http://www.weforum.org/pdf/globalrisk/2009.pdf.

As seen from above definitions, every organization defines energy security depending on type of agendas they are pursuing. There are 39 more definitions collected from various authors, organizations, and state agencies on the topic of energy security.[84] There is not one definition agreed upon by everyone because the pursuit of energy security (however it is defined) is a powerful excuse for states and organizations to justify their actions and policies.

Energy is established as a security issue by the abundant literature that can be found on the topic. There is a distinct vocabulary found in public documents, media reports and academic writing on the topic of energy security that involves frequent references to weapons, conflicts, wars, struggles, blackmail, superpowers, dominance, losers and winners.[85] In this way, energy security is more frequently than not reduced to the mere ownership and control of oil and gas fields and pipelines. Stefan Bouzarovski describes pipeline networks as embodiment of international relations of power because pipelines are not simply carriers of oil and gas from producer to consumer; pipelines represent "a direct physical connection fixed in space" between producer, transit and consumer countries.[86] Pipelines are a major component in geopolitics of energy where countries engage in the "competition for, control of, and securing reliable access to those supplies." Geopolitics represents "the interplay between power and interests, strategic decision-making, and geographic space."[87]

After 1970s energy crises, five different views on energy and energy security were identified.[88] Those views are considered to still be legitimate today. *Scientific view* sees energy as property of heat, motion, and electrical potential. Energy security is simply a matter of thermodynamics and physics. In *economic view*, energy is a commodity (electricity, coal, oil, natural gas) traded on the market. Consumers and producers are presented with a choice and it is assumed that marketplace allocates those choices efficiently. Energy security in this view becomes a matter of analyzing transactions between buyers and sellers. *Ecological view* classifies energy resources as renewable or non-renewable, clean or polluting, and inexhaustible or depletable. Value of sustainability is given priority in this view. Energy security is a matter of recognizing that energy resources will eventually run out and that present use will have negative consequences for the planet, and consequently, for future generations. In *social welfare view*, energy services

[84] Savacool, "Introduction," 3-6.
[85] Ciuta, "Conceptual Notes on Energy Security," 130.
[86] Stefan Bouzarovski, "Post-Socialist Energy Reforms in Critical Perspective: Entangled Boundaries, Scales and Trajectories of Change," *European Urban and Regional Studies* 17, no. 2 (2010): 176, http://eur.sagepub.com/content/17/2/167.
[87] "Geopolitics of Gas in New World of Energy," *Pipeline and Gas Journal*, August 2012, http://www.pipelineandgasjournal.com/geopolitics-gas-new-world-energy?page=show.
[88] Paul C. Stern and Elliot Aronson, eds., *Energy Use: The Human Dimension* (New York, NY: W. H. Freeman & Company, 1984), quoted in Sovacool, "Introduction," 6-7.

are social necessity. In this view, people have a right to use energy for home activities, transportation and other essential purposes. Energy security becomes a matter of providing energy services to all social classes. Lastly, *political view* deals with geography of energy resources, stability of producing and consuming countries, and fuel substitutes. Energy security is seen as important component of national security.

Jonathan Elkind identifies energy security as being composed of four elements which are availability, reliability, affordability, and environmental sustainability.[89] *Availability* refers to the ability of consumers to secure all the energy they need. They will secure their energy needs in commercial energy markets where buyers and sellers interact by agreeing on terms of trade. There needs to be sufficient resources, investment, technology as well as legal framework to support this extensive interaction. *Reliability* refers to energy services being protected from disruption. *Affordability* refers to stable prices relative to income. *Sustainability* refers to minimizing the damage to society, environment, and economy that may be induced by energy infrastructure.

Several reasons have been put forward to explain why energy security became a common subject of debate in the field of international relations as well as major economic and political problem in recent times.[90] First, there is rising global demand for energy which creates fear for future supply. Rapid industrialization of the large regions of the world is increasing the demand for fossil fuels. Anxiety stems from the fact that besides significant increase in demand, rate of new oil fields being discovered is steadily declining. Second, energy-rich regions are politically unstable which again creates fear for future supply. Attacks by disenfranchised groups are rising in frequency. Besides putting in place very expensive infrastructure, issues of its protection need to be considered as well. And third, fossil fuels are identified as culprits for bringing about climate change and potential future devastation.

Energy security represents a complex mix of geopolitical and strategic concerns as well as economic considerations.[91] Michael T. Klare explains that for industrializing and industrialized states which rely on imports for most of their energy needs, energy security entails important foreign policy dimension.[92] Main objective of overseas diplomacy becomes establishing friendly

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[89] Jonathan Elkind, "Energy Security: Call for a Broader Agenda," in *Energy Security: Economics, Politics, Strategies, and Implications*, ed. Carlos Pascual and Jonathan Elkind (Washington, DC: Brookings Institution Press, 2010), 121-130.
[90] Sam Raphael and Doug Stokes, "Energy Security," in *Contemporary Security Studies*, 2nd ed., ed. Alan Collins (New York, NY: Oxford University Press, 2010), 379.
[91] Ibid., 391.
[92] Michael T. Klare, "Energy Security," in *Security Studies: An Introduction*, 2nd ed., ed. Paul D. Williams (New York, NY: Routledge, 2013), 539.

and sustainable relations with states that provide energy. Friendly relations for industrialized states mean that their energy companies will have an access to take part in lucrative energy projects. This responsibility is frequently executed by senior government officials such as presidents and prime ministers.

Klare further elaborates that energy security will have a different meaning for different states, depending on their general outlook.[93] For the present and near future it means having sufficient energy to meet vital needs of the state. Diversifying types of energy used is one of the ways to feel more secure. Diversifying suppliers is another, as well as investing in climate-friendly energy alternatives. States importing great amount of energy products to meet their energy requirements will need to have significant foreign policy dimension to their energy security. Military always needs to be in a stand-by mode because the need for military force to protect energy infrastructure is always a possibility.

Furthermore, energy security challenges for different states will differ according to "geographic size, resource endowment, level of economic development, and type of energy market."[94] *Geographic size* indicates that large countries have the capacity and technology, small countries usually do not. Their bargaining power is therefore limited. *Resource endowment* means that energy security challenges will depend on whether country is importer, exporter, or transit country. Importing countries look for alternative fuels, low prices, diversity of imports and energy sources. Exporting countries look for security of demand and high prices for their exports.[95] For transit countries, dependence and the lack of diversification are beneficial because what matters is the amount of energy flowing through their transmission networks and transit fees collected. *Level of economic development* means that energy security challenges will be different for developed and underdeveloped states. States with poor economies usually spend significant amount of their revenues on energy imports and even then they do not consume much energy.[96] They do not possess resources and power of the developed states. Lastly, energy security challenges depend on the *type of market*. Well-functioning markets where prices can

[93] Ibid., 540-541.
[94] Benjamin K. Sovacool and Tai Wei Lim, "Conclusion: Exploring the Contested and Convergent Nature of Energy Security," in *The Routledge Handbook of Energy Security*, ed. Sovacool, 424-425.
[95] Andrei Konoplyanik, "Energy Security and the Development of International Energy Markets," in *Energy Security: Managing Risk in a Dynamic Legal and Regulatory Environment*, ed. Barry Barton et al. (New York, NY: Oxford University Press, 2004), 47-84, quoted in Sovacool and Lim, "Conclusion," 424.
[96] UNESCAP, *Energy Security and Sustainable Development in Asia and the Pacific* (Bangkok: UNESCAP, 2008), http://www.unescap.org/sites/default/files/energy-security-ap.pdf, quoted in Sovacool and Lim, "Conclusion," 424-425.

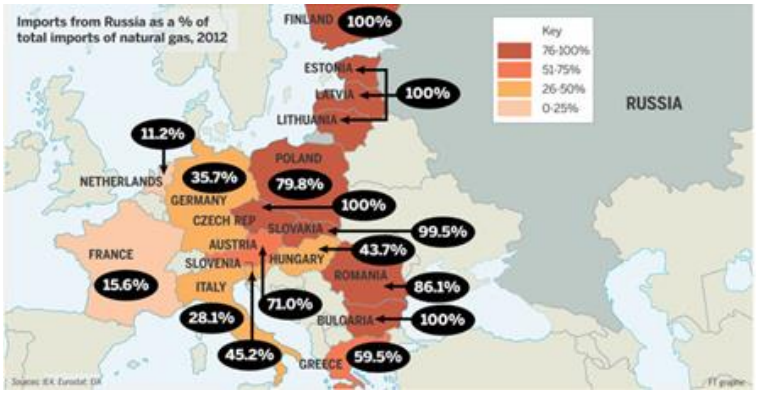
adjust according to supply and demand trends are preferable over markets that are regulated where prices cannot adjust to balance supply and demand.[97]

Energy security is also a psychological issue based on perceptions.[98] The perception that there might be future supply interruptions can lead to major policy changes even though in reality the probability of this happening is very low. As much as energy consumers are dependent on suppliers, suppliers are dependent on consumers to generate revenues. In this dependent energy relationship, consumers always perceive themselves at a disadvantage.

2.2.1. Energy Security Challenges in Practice

One of the popular topics on energy security is the Eurasian energy security challenges, mostly involving the EU, Russia, and transit countries found between Russian and EU territories. One of the major challenges for the EU's energy security is gas transported by pipelines. There are three main suppliers of pipeline gas to EU: Russia, Norway, and Algeria. In 2012, 36.5% of EU gas imports came from Russia, 34.2% came from Norway, and 14.2% came from Algeria.[99] The EU Member States' dependence on Russian gas imports is illustrated in Figure 1 below.

Figure 1: Imports from Russia as a % of total imports of natural gas for 2012[100]



Sources: IEA, Eurostat, EIA

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[97] IEA, *Energy Security and Climate Policy: Assessing Interactions* (Paris: OECD/IEA, 2007), http://www.iea.org/publications/freepublications/publication/energy_security_climate_policy.pdf, quoted in Sovacool and Lim, "Conclusion," 425.

[98] Sovacool and Lim, "Conclusion," 424.

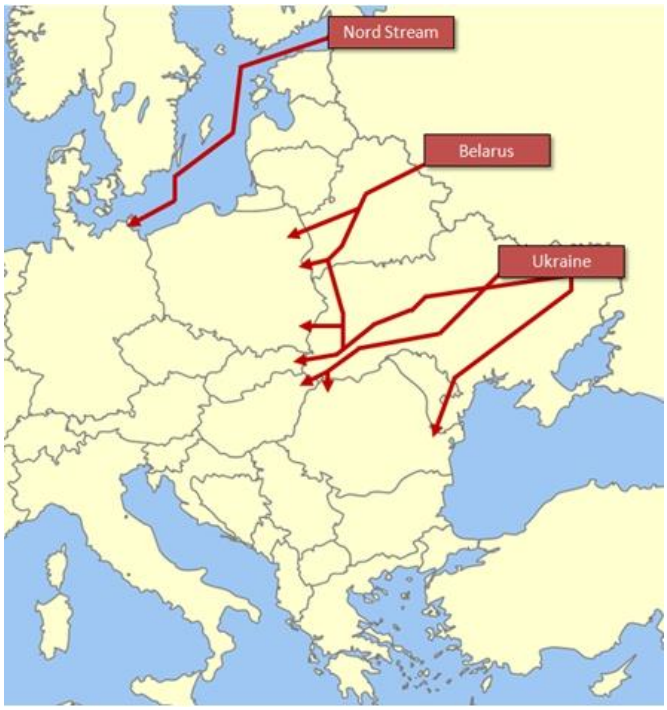
[99] Jack Sharples and Andy Judge, "Bulgaria and Macedonia would be hardest hit by a suspension of Russian gas exports through Ukraine," *LSE EUROPP Blog*, 13 March 2014, http://blogs.lse.ac.uk/europpblog/2014/03/13/bulgaria-macedonia-and-romania-would-be-hardest-hit-by-a-suspension-of-russian-gas-exports-through-ukraine/.

[100] David Burkart, "Managed Futures News: March 2014 Global Macro Recap," *aiSource.com*, 24 April 2014, http://www.aisource.com/managed-futures/news/aisource-news/2014/04/24/march-2014-global-macro-recap.

As seen from Figure 1, The EU Member States in Eastern and Central Europe are highly dependent on Russian gas deliveries to satisfy their gas import needs. For reasons that will be elaborated later in the thesis, other channels for pipeline gas supply are not available to them. Member States in the West are less dependent on Russia because Norwegian energy exports (gas and oil) go almost exclusively to Western Europe (France, Germany, The Netherlands, UK)[101]. Gas deliveries from Algeria are mostly supplied to countries in the Western Europe as well.

There are four main routes through which Russian gas reaches the EU. The first route is represented by direct pipelines from Russia to Finland and the Baltic States who import their gas only from Russia. The second route is represented by the *Nord Stream* pipeline which passes under the Baltic Sea, delivering Russian gas directly to Germany. The third and fourth routes are represented by transit pipelines through Belarus and Ukraine.[102] Excluding the direct pipelines to Finland and the Baltic States, pipeline routes are drawn in Figure 2 below, with capacity and total flow of those three routes outlined in Table 1 below.

Figure 2: Map of gas pipelines from Russia to Europe[103]



Source: Sharples and Judge, "Bulgaria and Macedonia."

[101] Eurogas, *Statistical Report 2013* (Brussels: Eurogas, 2013), 6, http://www.eurogas.org/uploads/media/Eurogas_Statistical_Report_2013.pdf.
[102] Sharples and Judge, "Bulgaria and Macedonia."
[103] Ibid.

Table 1: Capacity and total flow for Nord Stream, Belarus and Ukraine transit routes for Russian gas exports to EU[104]

TRANSIT ROUTE	*EU ENTRY POINTS*	*CAPACITY (bcm)*	*TOTAL FLOW 2012*	*TOTAL FLOW 2013*
Nord Stream	Germany	55.0 (19.7%)	11.3 (9.2%)	23.5 (16.5%)
Belarus	Poland	41.3 (14.8%)	31.7 (26.0%)	37.0 (25.9%)
Ukraine	Hungary, Poland, Romania, Slovakia	182.9 (65.5%)	78.8 (64.7%)	82.3 (57.6%)

Source: http://www.iea.org/gtf/index.asp; http://www.nord-stream.com/.

Table 1 shows that the total flow through those pipelines is significantly less than the actual pipeline capacity. Another important point is that Ukraine is the most important transit country for Russian gas on its way to EU. If Russia cuts all gas deliveries to Ukraine (including transiting gas), many EU countries would experience serious national problems. Importance of Ukraine as a transit country for Russian gas on its way to the EU will be analyzed later in the thesis.

2.2.2. Energy Security in International Relations Theories (Liberalism and Realism)

The issue of energy security acquired global dimension with the first oil shock of 1973, followed by the second oil shock of 1979. Energy-importing developed states became aware of their energy vulnerability while exporting states of OPEC became aware of their power. This was enough of a reason for international relations theories to incorporate energy security discourse into their books.

In International Relations theory, two most popular views are given by Liberalism and Realism.[105] Liberalism supports free-market capitalism and market approach to energy security as explained by Andrews-Speed, Liao and Dannreuther:

> The market approach would rely on the national and international energy markets and would seek to reduce the risk of disruption by improving the efficiency of these markets.

[104]Sharples and Judge, "Bulgaria and Macedonia."
[105] Raphael and Stokes, "Energy Security," 382-383.

> The last 20 years have seen a tendency for the world's largest economies to prefer market approach for long-term measures to energy security.[106]

According to Liberalism, its spread to other regions of the world ensures that national interests increasingly take a backseat to transnational economic cooperation. Industrialized rich North is running out of energy resources and is increasingly depending on the South for its energy needs. Due to spread of globalization this fact is unlikely to lead to major conflict between great powers. Energy production, transportation and prices are regulated by the international energy market which creates stable arena for interaction between producers and consumers. Energy security of individual states is closely interlinked by international energy security. If this economic order is preserved, Liberal theory maintains that conflict between great powers is unlikely to occur.

Realism, on the other hand, is skeptical of the Liberal order. It takes strategic approach to energy security as explained by Andrews-Speed, Liao and Dannreuther:

> The strategic approach would combine state-sponsored economic measures with political initiatives. Economic measures would include direct government participation in both enhancing domestic energy production and in investing in overseas sources of energy. Political links with energy exporters would be of great importance, and these would be supported by a range of economic measures such as aid, inward investment and sales of key goods. Government pursuing this approach might not be overly concerned about the cost of implementation compared to the probability and impact of the disruptive event.[107]

Realism points out to several trends that may lead to an end of international cooperation and return of geopolitical struggle and conflict. According to Realism, states exist in an anarchic world with scarce resources. Realists consider resource wars over control of energy fields as real possibility, where great powers will first compete then engage in conflict over control of valuable energy regions.

In short, Liberal approach to energy security focuses on market mechanisms. Energy is another commodity traded in the market. Realist approach to energy security focuses on the role played by the state. Unlike other commodities, energy is considered as a strategic resource that should not be left to markets.[108] Where Liberals see interdependence, Realists see dependence.

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[106] Philip Andrews-Speed, Xuanli Liao and Roland Dannreuther, *The Strategic Implications of China's Energy Needs,* Adelphi Paper 346 (London: Oxford University Press for The International Institute for Strategic Studies, 2002), 19, quoted in Susan Fay Kelly and Sigve Reiertsen Leland, "Oil Actually" (master's thesis, University of Tromso, 2007), 93, http://munin.uit.no/bitstream/handle/10037/993/thesis.pdf?sequence=1.

[107] Ibid., 92.

[108] Brian C. Ventura, "International Structure of China's Energy Security," presentation at the HKPSA Second Annual Conference, Hong Kong Baptist University, Hong Kong, 26-27 August 2010, 3, http://brianventura.files.wordpress.com/2010/07/international-structure-and-chinas-energy-security.pdf.

2.2.3. EU's and Russia's Views on Energy Security

Current search for energy security has been compared to the arms race of previous decades.[109] Geopolitical struggle to secure energy resources and pipeline routes is present reality. Energy security turned into a race to secure control over regions that are rich primarily in oil and natural gas. This race threatens to become a zero-sum contest that may lead to conflict among great powers. Such state of affairs threatens to undermine free-market trade and bring about new international energy order that will be characterized by statism. Realists point out that this can already be observed in actions of such powers as China and Russia. They tightly control their countries' energy industries. China and Russia prefer bilateral agreements with other countries instead of relying on market mechanisms. In this view, it is argued that there is higher probability of the United States and the EU turning slowly to statism than Russia and China turning to free-markets to regulate their energy supplies. Chase has calculated that five largest international energy corporations are responsible for 14% of world's oil and gas production, but they own only 4% of oil and gas reserves. On the other hand, state controlled energy companies produce 60% of world's oil and gas production and own approximately 90% of oil and gas reserves. 77% of world's oil and gas reserves are located in countries in which national energy companies and their associates control production. They do not operate under market principles.[110]

There are two popular and polarizing views on energy security. IEA, the United States and the EU seemingly share the similar Liberal view on energy security. This view stresses the importance of competition and free markets. China and Russia, on the other hand, prefer Realist interpretation where economy is subordinate to politics. Because energy is an important component of national security, instead of relying on competition and market forces, they prefer their energy policies to be under tight state control.

The EU's view on energy security is revealed by the European Commission's presentation on energy security in Europe:

> January 2009, gas supplies from East are severed … This gas crisis exposed Europe's dependency on energy imports which at present include over 60% of its gas. Dwindling energy resources and increased demand mean that EU's energy dependency is set to get worse with gas imports rising to 70 to 80% by 2030. (…) As the gas crisis showed, energy dependency could be a major risk and lead to severe economic damage for those

[109] Michael T. Klare, *Rising Powers, Shrinking Planet: The New Geopolitics of Energy* (New York, NY: Metropolitan Books, 2008), 30, quoted in Raphael and Stokes, "Energy Security," 383.
[110] Howard Chase, "European Energy Policy," presentation at the Aleksanteri Institute "Challenges and Prospects for Development of the European Energy Sector" seminar, University of Helsinki, Helsinki, 15 June 2006, quoted in Palonkorpi, "Energy Security," 7.

> hit by supply cuts. Europe therefore needs to diversify its supplies … to avoid being dependent on a single exporter. Above all, to improve its energy security, Europe needs to develop a well-functioning EU internal energy market. At present, energy flows often stop at Member State borders because of lack of interconnected infrastructure, leading to inefficient supply and wasted resources. The solution – greater interconnectivity and flexibility of national gas and electricity grids. This will allow a permanent exchange of energy and additional security of supply for all EU Member States. Energy diversification also depends on developing new supply routes and interconnections. The EU supports major new gas and electricity infrastructure projects to link Europe to North Africa and gas rich countries of the Caspian and Middle East regions through strategic initiatives … Using energy more efficiently while diversifying EU's energy mix will also lessen the reliance on external supplies. The modernization of our networks is essential to make the change happen. The European way of life depends on plentiful supplies of energy and challenge for the future is to make sure that this energy is clean, reliable, and secure.[111]

European Commission's uneasiness with having Russia as a major gas supplier was expressed in this presentation. Having more supply routes and working on integrating European energy markets is seen as a way out of uneasy dependence on Russian energy imports. Escaping this dependence seems to be the essence of Commission's energy security pursuit.

Russia's view on energy security is revealed by the Ministry of Energy of the Russian Federation:

> The objective of the energy policy of Russia is to maximize the effective use of natural energy resources and the potential of the energy sector to sustain economic growth, improve the quality of life of the population and promote strengthening of foreign economic positions of the country. (…) Within the period up to 2030, export of energy resources will remain the major development factor for the Russian economy … (…) Energy security is one of the most important components of the national security. Energy security is the country's security, that of its citizens, society, state and economy from the threats to reliable supply of fuel and energy. These threats are determined by external (geopolitical, macroeconomic, market) factors, as well as by the condition and operation of the country's energy sector. (…) The strategic objective of the foreign energy policy is the maximum efficient use of the Russian energy potential for full-scale integration into the world energy market, enhancement of positions thereon and gaining the highest possible profit for the national economy. The global nature of energy problems, their rising politicization, as well as objective importance of the Russian fuel and energy complex in the world energy sector predetermine the important role of the foreign energy policy of the country. (…) Stable relationships with traditional consumers of Russian energy resources and shaping equally stable relationships on new energy markets are the most important vectors of the country's energy policy in the sphere of global energy security provision …[112]

Views expressed here stress the importance of Russia's energy wealth as a foreign policy instrument which will be used to improve not only Russia's economic position in the world but political position as well.

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[111] European Commission (EC), "Energy Security in Europe," EC video, http://ec.europa.eu/energy/fpis_en.htm.

[112] Ministry of Energy of the Russian Federation, *Energy Strategy of Russia for the Period up to 2030*, approved by decree no. 1715-r of the Government of the Russian Federation dated 13 November 2009 (Moscow: Institute of Energy Strategy, 2010), 10, 19, 22, 28, 55, http://www.energystrategy.ru/projects/docs/ES-2030_%28Eng%29.pdf.

In today's global energy system, China and Russia are concerned with securing the direct access to oil and gas supplies.[113] Controlling energy supplies and achieving energy independence has become a matter of national security. The EU, on the other hand, insists on energy interdependence supported by diversification of energy supply sources and decreasing reliance on oil and gas. The following chapter will examine in detail the EU's efforts to improve its energy security.

[113] Alexander Mirtchev, "The New EU External Energy Policy: an important move - if it is not too late," *European Energy Review,* 8 December 2011, http://krullcorp.com/en/inthenews/95-the-new-EU-external-energy-policy.html.

CHAPTER 3: EU'S ROAD TO COMMON ENERGY POLICY

This chapter will look at EU's attempts to have common energy policy within the Union and major obstacles that EU institutions face in this pursuit. First, it will analyze the EU's failure to properly address energy issues since the EU was established in 1993. Importance of energy in unification of Europe prior to 1993 will be briefly explained. Then, constraints to common energy policy due to dependence on Russian energy will be discussed, and the effects of natural gas crises on the perception of importance of common EU energy policy will be explained. Finally, the importance of diversification of energy supply sources for the common energy security policy will be investigated.

3.1. TWO DECADES OF FAILURE (1993-2013)

The issue of energy was at the forefront of European integration. European integration started with Schuman Declaration in 1950 and the creation of European Coal and Steel Community (ECSC) in 1951.[114] This was followed by the Treaty of Rome in 1957 and the creation of European Economic Community (EEC), followed by the European Atomic Energy Community (EURATOM). These were the beginnings of the European Union and first attempts to put energy production and related issues under joint regulation. At its beginnings, European Community's energy matters were under regulation of ECSC and EURATOM treaties which were meant to ensure stable supplies of coal and nuclear energy for the Community, therefore, increasing energy security and promoting self-sufficiency efforts. The two more important considerations which led to the creation of ECSC and EURATOM treaties were that first, as raw materials, coal and steel were major components in the weapons production; and second, to promote peaceful use of atomic energy.

However, the Treaty establishing the EEC did not include plans for common energy policy.[115] Although energy issues, their relative importance and language used have changed over time, the issue of energy was given great importance in the 1950s as well. By putting energy production under joint regulation, European countries hoped to check Germany from growing

[114] Desmond Dinan, *Europe Recast: A History of the European Union* (Basingstoke: Palgrave, 2004), 5; John Gillingham, *Coal, Steel and the Rebirth of Europe, 1945–1955* (Cambridge: Cambridge University Press, 1991), quoted in Pami Aalto, "The EU-Russia Energy Dialogue and the Future of European Integration: From Economic to Politico-Normative Narratives," in *The EU-Russian Energy Dialogue*, ed. Aalto, 31.

[115] EC, *Green Paper: Towards a European Strategy for the Security of Energy Supply*, COM (2000) 769 final (Brussels: EC, 2000), 10-11, http://ec.europa.eu/energy/green-paper-energy-supply/doc/green_paper_energy_supply_en.pdf.

too powerful again. At its beginnings, the EU equated controlling energy with checking and controlling power.

The need for coherent energy policy strategy was first felt after the oil crisis of 1973. Members of the European Community became united in efforts to decrease their dependence on external energy supplies (mostly oil supplies).[116] Those efforts consisted of measures to support domestic energy production which was considered uncompetitive earlier, policy of stockpiling, promotion of energy efficiency and technological development. Between 1973 and 2000, the EU decreased its energy dependence from 60% to 50% thanks to energy conservation, development of the North Sea energy fields, and increased diversification due to developments in nuclear and renewable energies.[117] In 1970s, oil was responsible for more than 60% of primary energy supply. In 2000, this number fell to 44%.[118]

For remainder of the century, energy policy discussions were mostly preoccupied with reducing the impact of possible oil supply crises. There were attempts to include energy chapter in Maastricht and Amsterdam treaties, however, those negotiations were unsuccessful. Amsterdam Treaty (signed in 1997) only mentions energy in its opening. Up until the new millennium, there were never serious discussions among the Member States on the topic of main objectives of the EU energy policy. Energy problems in the EU have usually been dealt with by internal market mechanisms, environmental policy and taxation.[119]

Initially, energy was not put into European single market concept. It was added in 1988. Since then, EU energy policy has been described as a constant struggle between the Commission and Member States' governments who refuse to give up some of their sovereign rights and put them under Commission's control.[120] However, there are three identified principles of internal EU energy policy pursued by both the Commission and Member States' governments.[121] The first principle of *market rules and competitiveness* emphasizes the cornerstone of EU integration which is the single market concept. One of the major setbacks for the development of external energy policy of the EU is slow progress on the development of internal energy policy. Gas and electricity markets were liberalized by EU directives of 1996, 1998, 1999, and further improved

[116] Ibid., 28.
[117] Ibid., 21.
[118] Ibid., 84.
[119] Ibid., 11.
[120] Janne Haaland Matlary, "The Nordic Countries and EU Membership: the Energy Factor," in *The European Union and the Nordic Countries*, ed. Lee Miles (London: Routledge, 1996), 239-241, quoted in Pami Aalto and Kirsten Westphal, "Introduction," in *The EU-Russian Energy Dialogue*, ed. Aalto, 8-9.
[121] Aalto and Westphal, "Introduction," 9-10.

in 2003.[122] There is no market regime for the oil sector because this sector developed before the EU trade regime.[123] The Member States are slow in implementing regulations put in place by EU institutions because they are anxious to protect their powerful national monopolies. This became apparent in 2006 when Germany's energy company *E.ON* was prevented by national measures to acquire Spanish *Endesa*, and Italy's *Enel* was prevented to acquire French *Suez* company.[124] Internal actions such as these are having negative effect on EU's external energy policy.

The second principle is *sustainable development*, linking energy and environmental policy. It was recognized as a common EU goal in 1997 when it appeared in the Amsterdam Treaty.[125] Unlike many other policies regarding energy, environmental and climate change policies are policies in which EU Member States have managed to reach strong consensus. There is an agreement on the improvement of energy saving, energy efficiency and increased use of renewable energy in the EU energy mix. Strong agreement between EU Member States on the issue of sustainable development has resulted in EU becoming a global promoter of environment-friendly energy technologies.

The third principle of *security of energy supply* recognizes the reality of EU's increasing dependence on energy imports due to depletion of Union's energy resources and slowly rising domestic demand. In case of energy supply emergency, EU is following IEA's guidelines (mainly regarding oil) for keeping national energy stocks. Those guidelines are being criticized because they were set in response to 1970s oil crises.[126] In the new millennium, the Commission has taken an active role in promoting solidarity, coordination and infrastructure interconnectedness within the EU. It is thought that this would lead to better integrated internal energy market which would give EU a better position to incorporate energy issues into foreign policy challenges, leading to improved energy supply security. While some EU institutions are working hard to consolidate EU energy policy, some of the most influential Member States are stalling the process by not fully committing to the common energy policy, but not rejecting it either.

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[122] EC, "The Commission to Act over EU Energy Markets," MEMO/06/481, 12 December 2006, http://europa.eu/rapid/press-release_MEMO-06-481_en.htm?locale=en, quoted in Aalto and Westphal, "Introduction," 9.
[123] Belyi, *Energy Security*.
[124] Aalto and Westphal, "Introduction," 9.
[125] Matlary, "The Nordic Countries," 241., quoted in Aalto and Westphal, "Introduction," 10.
[126] Aalto and Westphal, "Introduction," 10.

3.1.1. EU Internal Energy Market

In order to move closer to the possibility of the common EU energy policy, genuinely competitive internal energy market needs to be achieved first. Internal energy market is comprised of European gas and electricity markets. Between 1996 and 2009, three legislative packages of directives and regulations were adopted with the aim to harmonize and liberalize internal energy market. Legislative packages were put together by the European Parliament and the EU Council. They created common rules for the internal energy market, to be followed by all Member States. These packages were prepared with the aim to improve market access, transparency, regulation, consumer protection, EU market interconnection and sufficient levels of supply. However, Member States left room for maneuver considering that regulations were directly applicable while directives needed to be made into national law. Legislative measures freed new gas and electricity suppliers to enter Member States' markets and consumers to choose suppliers. It is understood that this would increase consumer protection and improve security of supply. Internal energy market has been further improved by EU policies addressing the development of trans-European networks for electricity and gas transportation.[127]

The first legislative package consisted of Directive 96/92/EC addressing common rules for the internal market in electricity and Directive 98/30/EC addressing common rules for the internal market in natural gas. They came into force in 1997 and 2000 respectively. The aim of these directives was to resolve conflict of interests between producers, suppliers and network operators, and to achieve market transparency. The second energy package was adopted in 2003. It replaced previous package and consisted of a regulation and Directive 2003/54/EC on gas and Directive 2003/55/EC on electricity. This package led to industrial and domestic customers becoming free to choose gas and electricity suppliers. However, in 2007, Commission concluded that there were still obstacles preventing consumers to truly reap all the benefits of free and open national gas and electricity markets. This led to third energy package being adopted in 2009. It consisted of three regulations, Electricity Directive 2009/72/EC and Gas Directive 2009/73/EC. The main aim of third package was to separate production and supply activities from activities of transmission network operation.[128] In whole, the aim of those packages was to stabilize and reduce wholesale gas and electricity prices, to give consumers more choices of suppliers, to improve energy infrastructure interconnectedness in EU, to promote cross-border trade in gas and electricity, and to promote fair competition between

[127] "Internal Energy Market," European Parliament, http://www.europarl.europa.eu/aboutparliament/en/displayFtu.html?ftuId=FTU_5.7.2.html; "The 3rd Energy Package," *Gas in Focus*, http://www.gasinfocus.com/en/focus/the-3rd-energy-package/.
[128] "The 3rd Energy Package," *Gas in Focus*.

energy companies. However, Commission recognizes that there is still more work to be done in enforcing already existing rules, modernizing energy infrastructure, and preventing interventions by Member States which distort markets.[129]

3.1.2. European Commission's Views on EU Energy Policy during 1990s with Emphasis on External Dimension

The European Commission's earlier position on energy policy efforts (during 1990s) was illustrated in 1995 White Paper.[130] Energy policy was visualized as being part of the EU's overall economic policy, based on market principles such as market integration, deregulation, and limited public intervention. Energy policy would have to embrace competitiveness, supply security pursuit and protection of the environment. It should be formed with due consideration of EU's central concerns which are job creation, increased business efficiency and environment protection. External dimension of energy policy was stressed as being important since the Union is a major energy importer. Relations with major energy suppliers to the EU rest on bilateral and multilateral agreements. Commission called for solidarity between Member States on energy matters in order to have fully integrated energy market. It also called for common energy policy objectives and common energy strategy to be discussed and prepared. Same calls are frequently sent nowadays as well. Furthermore, it is stated that Union-level coordination would improve the position of European energy companies in foreign markets by exporting energy technologies, services and investments. The Commission underlined the importance of the Union speaking with one voice internationally due to its concerns regarding changing geopolitics and increased energy import dependency. Those concerns are still valid today. The paper did not propose any harmonization of Member States' energy mix. Effective cooperation will mean that national energy policies will not interfere with common goals set by the Member States.

Low energy prices in 1995 were underlined as direct contributors to economic and social prosperity of the time and positive contributors to economic and monetary union.[131] However, the Commission warned that low energy prices may not last forever. Because of that, framework should be prepared to deal with possible future increases in energy prices at the EU

[129] "Single Market for Gas & Electricity: Internal Energy Market," European Commission, http://ec.europa.eu/energy/gas_electricity/internal_market_en.htm.
[130] EC, *White Paper: An Energy Policy for the European Union,* COM (95) 682 final (Brussels: EC, 1995), http://europa.eu/documentation/official-docs/white-papers/pdf/energy_white_paper_com_95_682.pdf.
[131] Ibid., 5.

level. The paper acknowledged that Member States have different energy policies. This means that increase in energy prices would lead to different responses from different Member States which would undermine Union's coherence and the Commission's efforts on energy matters.

In 1995, the Commission was still mostly concerned about the Union's heavy dependence on oil imports (but not gas). The importance of energy diversification was stressed several times. The Commission wrote that energy dependence "should be a point of concern given the political risks in some important supplier countries and growing world energy consumption"[132], but it does not say that it *is* a point of concern among the Member States. Proposals were made for the improvement of market rules, fuel diversification, improved energy efficiency, and use of renewable energy in order to improve supply security. To fight energy dependence, importance of new technologies, energy efficiency and savings were often stressed. Importance of technology was underlined several times because it gives EU the edge over the others in globalized world and the Commission connects this with another important EU goal which is job creation. Technological development is important because it will have positive effects on the labor market and energy supply security by improving extraction of energy resources, improving production of renewable energies, improving energy efficiency and energy savings.

In its 2000 Green Paper[133], the Commission acknowledged crippling effects of the non-existent EU energy policy for its activities on the international energy market:

> Unfortunately, the EU lacks the means to negotiate and exert pressure. The Union suffers from having no competence and no community cohesion in energy matters.[134]

This Paper was issued at a time when oil prices tripled within a year which was a major point of concern given the EU's growing energy dependence. Commission saw this as a danger to European economy and called for active European energy policy in order to help the Union deal with increasing energy dependency. In 2000, EU imported around 50% of its energy requirements. By 2030, this figure is projected to rise to 70%. In 1999, the Union spent €240 billion on energy imports which made up 6% of total imports and 1.2% of GDP. In 1997, the bill was €120 billion. Out of this, €94 billion was spent on oil imports. 45% of oil imports came from the Middle East and 40% of natural gas imports came from Russia. Overall, EU energy demand was covered with 41% of oil, 22% gas, 16% coal, 15% nuclear energy, and 6% renewables. With this in mind, Commission recognized that the EU does not have the power to bring about changes in the international energy market. It called for diversification of sources of

[132] Ibid., 21.
[133] EC, *Green Paper*, 2000.
[134] Ibid., 28.

supply and diversification of products in order to decrease risks of energy dependency and improve security of supply situation. The Commission stressed the importance of controlling energy demand and consumption in order to protect the environment and increase energy security.

As a major energy importer and consumer, Paper recognized the important role played by the EU in geopolitical developments of those countries through which energy deliveries to the EU are transiting. Like in 1995, in 2000 the Commission still considered external dependence on oil as "the most acute case of Community dependence."[135] 76% of oil demand was imported. It was stated that gas diversification is easier to achieve than oil diversification. In general, in 2000 the Commission was still more worried about security of oil supplies than gas supplies. Imported gas covered 40% of total gas consumption. At the time, Commission considered this as moderate dependence. It was stressed that both former Soviet Union and later Russia always fulfilled their long-term gas supply contracts even when they were facing various internal difficulties. In regard to increased dependence on Russian gas, following was stated in the Paper:

> …the continuity of supplies from the former Soviet Union, and then Russia, over the last 25 years is a testimony to an exemplary stability. A long term strategy in the framework of a partnership with Russia would be an important step to the benefit of supply security.[136]

With anticipated enlargement and increases in gas demand, in 2000, Union projected that 60% of gas imports would be coming from Russia. Commission did not seem concerned about such high dependence on Russian gas in 2000.

The 2000 Green Paper called for EU to actively pursue two strategies in order to improve its energy supply security.[137] First, it needs to form strategic partnerships with important energy suppliers. Second, the EU must provide financial aid to encourage further development of renewable energy which was considered as the best option for diversification in the long-run. It was stated that one of the best ways for the EU to reduce its dependence on external supplies is to have a strict policy on demand management. Managing demand side improves energy security at the Union-level. Controlled demand will reduce consumption. Commission was focusing on the demand side because "the European Union has very limited scope to influence the energy supply side."[138] Between 1975 and 1985, energy efficiency was improved by 24%.

[135] Ibid., 22.
[136] Ibid., 40.
[137] Ibid., 45.
[138] Ibid., 11.

Between 1985 and 1999, improvement was 10%.[139] The fall in the energy efficiency rate may be explained by low energy prices during that period.

Overall, with the 2000 Green Paper, Commission acknowledged the EU Member States' continued failure to arrive at common energy policy:

> Apart from the powers established by the ECSC and Euratom treaties, there is no explicit mandate for a European energy policy. As a result, over the last 40 years, Europe has failed to develop a consistent common energy policy (within both the EU and the International Energy Agency), as the OPEC countries have today, and as other producer groups may in the future. The lack of a real energy policy reduces the EU's bargaining power. In the face of powerful oil-exporting companies, European importers act without coordination on a market where prices are largely fixed. The development of the single market should help to curb the influence of exporting countries…[140]

3.1.3. EU Energy Policy in the New Millennium with Emphasis on External Dimension

The EU Members reached consensus on the point that, in the new millennium, they feel the need for common external energy policy more than ever. With Vladimir Putin becoming the President in 2000, the literature on EU energy challenges is divided between 2 periods: before 2000 and after 2000. After 2000, the EU has increased its efforts to include energy issues into broader foreign relations with third countries (especially Russia).

One of the highlights of EU energy strategy is its attempt to export its energy market model to other countries. The EU began new millennium with an image of international actor who has transcended traditional power politics and relies on markets and institutions approach in energy policy. Its main foreign policy instrument was promoting its trade rules and values and opening up of markets. In energy terms, this meant that control of energy supply would be taken away from state control and put under the control of investments and market rules.[141] With this in mind, the EU has been active in establishing new initiatives with its international energy partners.[142] In 2004, Black Sea and Caspian Sea Cooperation Initiative was launched. In 2005, The Energy Community of South East Europe Treaty was launched and bilateral political dialogue with OPEC was established. In 2006, Energy Partnerships with Azerbaijan and Kazakhstan were signed. The aim of these efforts was to incorporate energy-rich Central Asian

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[139] Ibid., 30.
[140] Ibid., 28.
[141] Richard Youngs, "Concepts of Energy Security and EU Foreign Policy," in Richard Youngs, *Energy Security: Europe's New Foreign Policy Challenge*, Routledge Advances in European Politics (New York, NY: Routledge, 2009), 15-16.
[142] Cao Hui, *Energy Security Strategy in the European Union: A Neo-Realism Approach*, Working Paper Series on European Studies 5, no. 2 (Beijing: Chinese Academy of Social Sciences, Institute of European Studies, 2011), 16-17, http://ies.cass.cn/en/UploadFiles_8765/201106/2011061609552045.pdf.

countries and neighboring Balkan countries into larger European regional market for energy products.

Reasons for heightened interest in energy security in the new millennium are both internal and external. Internally, the EU is experiencing slowly rising demand and declining domestic production. This led to anxieties about future availability of energy resources. Externally, unstable energy producing regions, unreliable transit routes and Russia aspiring to become energy superpower have led to anxieties about supply security.[143] Another reason for energy security rising on the EU agenda is due to the fact that oil price tripled between 1999 and 2000, and once again oil and gas prices more than tripled between 2002 and 2007. During this period there was substantial decrease in spare production capacity which was another point of concern.[144]

With energy prices rising in 2000s, EU energy policy has become increasingly preoccupied with Russia. Due to this, emphasis on energy policy has shifted from internal dimension of the 1990s, to external dimension of the new millennium. EU-Russia relations occupy a pivotal role in externally oriented energy policy of the Union. EU energy policy of the new millennium is characterized by failed attempts by the Commission to institutionalize EU-Russia energy relations with Energy Charter Treaty (ECT) and EU-Russia Energy Dialogue. Generally, EU gives great importance to institutions which are created to protect rules, norms and regulations. Therefore, the EU prefers to have relations with energy producer countries institutionalized in the form of ECT and Energy Community Treaty with South East Europe for example. By having energy relations institutionalized, EU hopes to replicate its internal market characteristics in other countries.

Russia-Ukraine gas dispute of January 2006, when Russian gas supplies to Europe were disrupted, shook Europe and resulted in energy security issue cementing its position as a priority on the EU level. Energy went from being a market issue to rising at the top of political agenda. This crisis exposed vulnerabilities and shortcoming of having more than twenty separate energy policies within the Union. In the first half of 2006, when Austria held the EU presidency, Energy Community Secretariat was established in Vienna, dealing with the creation of energy market between the Union and the Balkans. Succeeding Finnish and German presidencies also gave great importance to energy issues.[145] New proposals were made for the EU to increase its presence in Caucasus, Caspian region and Central Asia. With this in mind, Black Sea Initiative

[143] Ibid., 14-15.
[144] Richard Youngs, "Introduction," in Youngs, *Energy Security*, 1.
[145] Aalto and Westphal, "Introduction," 2.

was launched. In 2007, Central Asia Strategy was prepared. Failed attempts to promote European values meant that China and Russia took the opportunity and made deals that left little space for the EU to take action. Since 2007, Russia has taken control of pipelines and export routes from Central Asia. The EU could not properly respond to this turn of events because big European companies responded rationally by looking for profits and not to defend wider European interests. By not being able to respond to Russia's moves in Central Asia, the EU found itself in danger of having its energy market manipulated by Russia.[146] Popular belief is that although energy security has infiltrated European agenda, the real peak of European energy debates is yet to come. Pami Aalto and Kirsten Westphal concluded that what we have seen in the new millennium is increasing awareness of the great importance of energy for political, economic and social life and awareness of its scarcity.[147]

Following the Russia-Ukraine gas crisis of January 2006, which led to EU experiencing gas supply disruptions for several days, in March of the same year, the Commission issued a Green Paper in which it made the case for the common energy strategy of the EU.[148] Several problems were identified that would be resolved in the most effective manner if the EU had consolidated energy policy.[149] First identified problem is ageing infrastructure that requires estimated €1 trillion of new investments by 2025. Second, global energy demand is increasing, meaning that the Union will need to compete for energy resources from few energy-rich regions which are also politically or economically unstable. Third, import dependence is increasing because demand is increasing and domestic energy production is decreasing. Fourth, oil, gas, and electricity prices are increasing, putting strain on consumers and making EU industries less competitive on the global market. Fifth, internal energy market is not yet fully integrated, and as such, it is not yet competitive enough to enjoy lower prices for energy and security of supply. To deal with these challenges, Commission proposes further development of regulatory framework which needs to be applied in practice in full. By acting together in external energy policy challenges, the EU would have tools and power to protect collective EU interests when dealing with powerful energy suppliers such as Russia and OPEC. Consolidated external energy policy is needed for sustainable, competitive and secure energy to be delivered.

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[146] Antonio Marquina, "The Southeast-Southwest European Energy Corridor," in *Energy Security*, ed. Marquina, 60-61.
[147] Aalto and Westphal, "Introduction," 2.
[148] EC, *Green Paper: A European Energy Strategy for Sustainable, Competitive and Secure Energy,* COM (2006) 105 final (Brussels: EC, 2006), http://europa.eu/documents/comm/green_papers/pdf/com2006_105_en.pdf.
[149] Ibid., 3.

In May 2006, the European Commission and the Secretary-General/High Representative of the Union for Foreign Affairs and Security Policy delivered a report to European Council on external energy policy for Europe.[150] It is stated that increasing dependence on energy supply from unstable regions and countries presents a serious risk for Europe. Furthermore, the report says that some energy producers and consumers are using energy as a political tool. External actors not playing by the same market rules in their own countries present another serious risk, this time for Europe's internal energy market. In order to make energy supplies more secure, there should be more coherence between internal and external energy policies. This is an area where more action is needed at the EU level. The report does not directly question the right of individual Member States to pursue their own policies to secure energy supply and choose their energy mix but it makes the case for common energy policy:

> Nonetheless, the development of a coherent and focused external EU energy policy, drawing on the full range of EU internal and external policies, would enhance the collective external energy security of the Union. It would also help the EU face more effectively possible strategies by major external energy suppliers to adversely influence market fundamentals.[151]

The report considers how external relations may be used more effectively to make energy supply to Europe more reliable. It is stated that internal energy policy needs to be more developed in order to have more coherent external energy policy. Some of the objectives to be pursued by a coherent EU approach, as proposed by the Commission, in order to improve external security of energy supplies to Europe are: signing energy partnerships in order to improve legal conditions for energy investments by promoting transparency and good governance in the energy sectors of third countries; improving production, export, and transport capacities in producing and transit countries; opening up production and export business in third countries to EU industry; improving conditions for energy trade by opening up access to export pipeline infrastructure to third parties; promote energy efficiency, renewable energies and low emissions technology; diversifying energy imports by different products and different suppliers; promoting national reserve stocks and encouraging partnerships in this field in the form of joint stock holdings.[152]

The Commission underlines two cornerstones of EU energy security which are functioning markets and energy diversification.[153] Functioning markets are thought to be the best way to

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[150] EC, *An External Policy to Serve Europe's Energy Interests*, paper from the Commission and the Secretary-General/High Representative of the Union for Foreign Affairs and Security Policy for the European Council, 9971/06 (Brussels: EC, 2006), http://aei.pitt.edu/39623/1/st09971.en06.pdf.
[151] Ibid., 2.
[152] Ibid., 3.
[153] Ibid., 3-4.

secure safe and affordable energy supplies. Markets create responsive energy supply, promote investments, absorb shocks, and generally provide security for producers and consumers. In order to have well-functioning markets, there should be physical and legal infrastructure put in place, information and transparency should be provided, and major players should be engaged in active participation. Commission proposes to have EU's neighbors included in joint regulatory area with shared trade, transit and rules. Commission also maintains that the EU should be engaged in active promotion of market principles such as non-discrimination, competition, transparency and enforcement.

> We need to convince non EU consumer countries that world energy markets can work for them. If they were to conclude that the only route to security lay in bilateral deals, the risk of disruption of the energy system would grow.[154]

Diversification of energy sources by having different energy suppliers coming from different geographical areas with different transit routes is seen as imperative in an effort to enhance EU energy security. The Commission suggests that the EU should take active participation in helping transit countries, which are deemed important for EU energy flows, to upgrade their energy infrastructure, and the EU should participate in the development and construction of new infrastructure. Furthermore, EU energy security would be improved by the construction of LNG (Liquefied natural gas) terminals. The Commission also stresses the importance of developing new international pipelines which would bring energy resources from the Caspian region and Central Asia. European external energy policy, whose importance is demonstrated in this report, should be:

> …coherent (backed up by all Union policies, the Member States and industry), strategic (fully recognizing the geo-political dimension of energy-related security issues) and focused (geared towards initiatives where Union-level action can have a clear impact in furthering its interests). It must also be consistent with the EU's broader foreign policy objectives such as conflict prevention and resolution, non-proliferation and promoting human rights. (…) An effective external policy on energy depends on being able to harness our considerable collective resources and put them at the service of shared interests. That means engaging with producer, transit and consumer countries to produce results. And it means acknowledging that political challenges require dialogue at political level (including Heads of State and Government) on a bilateral, regional and multilateral basis.[155]

In January 2007, the Commission adopted a Communication in which it outlined energy policy for Europe.[156] The Commission stressed three challenges faced by all member states: climate change, increasing import dependence, and higher energy prices. In order to deal with these

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[154] Ibid., 4.
[155] Ibid., 4-5.
[156] EC, *Communication from the Commission to the European Council and the European Parliament: An Energy Policy for Europe,* COM (2007) 1 final (Brussels: EC, 2007), http://ec.europa.eu/energy/energy_policy/doc/01_energy_policy_for_europe_en.pdf.

challenges, the new EU energy policy must be ambitious, competitive and long-term. It also must be beneficial for all Member States. The Commission again stressed that the EU's energy import dependence is increasing. It was projected that import dependence will rise from 50% of total EU energy consumption in 2007, to 65% by 2030. Reliance on imported gas was projected to increase from 57% in 2007 to 84% by 2030. For oil, projected increase was from 82% to 93%.[157] This fact was characterized as political and economic risk, with added concern of intense pressure on global oil and gas resources. The IEA projected that global oil demand will increase 41% by 2030.[158] The Commission underlines that it is unknown how energy supply will keep up with energy demand and that the possibility of supply failure is growing. It maintains that Member States must form close partnerships and speak with one voice with meaningful external energy policy to battle energy challenges facing the EU. Energy must become a central part in all the EU's external relations with third countries. Commission considers this as follows:

> … crucial to geopolitical security, economic stability, social development and international efforts to combat climate change. The EU must therefore develop effective energy relations with all its international partners, based on mutual trust, cooperation and interdependence. This means relations broadened in geographical scope, and deepened in nature on the basis of agreements with substantial energy provisions.[159]

The EU Member States agreed to prepare the common energy policy for Europe, but by all accounts, they were never eager to implement it. It was prepared rather as a distant possibility than a possible reality. Energy remains a sensitive issue in the EU and as such, each country remains in charge of its own energy policy.

European energy insecurity, supported by the general public opinion, started with gas crisis in the first days of 2006. The Gas crisis of 2009 confirmed what became apparent to Europeans in 2006 – that Russia is willing to cut gas supplies to achieve their economic and political goals. Although crises were resolved in a couple of days and gas flows returned to their intended volumes, the gas crises of 2006 and 2009 for the EU meant the start of energy insecurity. More serious debates than before started within EU institutions about the possibility of a unified energy policy and about Russia, which was now more than ever viewed as a possible threat to European energy security. Before this maneuver by Russia that resulted in gas crises, as far as EU energy security goes, EU was mostly concerned with energy supply being threatened by underinvestment in infrastructure and new field developments in energy producing countries.

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[157] Ibid., 3.
[158] IEA, *World Energy Outlook 2006* (Paris: OECD/IEA, 2006), http://www.worldenergyoutlook.org/media/weowebsite/2008-1994/WEO2006.pdf, quoted in EC, *Communication*, 2007, 3-4.
[159] EC, *Communication*, 2007, 17.

Therefore, their main concern, as far as energy producers are concerned, was to export EU market rules and values in order to open up lucrative energy markets in third countries and make them suitable for foreign investments. However, with the rise of new powerful consumers and producers, adding diplomatic and strategic aspects to energy security has been seen as imperative in the EU.[160] Merely promoting market rules and values does not seem to be enough anymore.

In September 2011, the Commission issued a Communication regarding security of energy supply and international cooperation.[161] It was stated that EU imports over 60% of its gas and 80% of its oil requirements. With such high import dependency and the fact that by 2030 global energy demand is projected to rise by 40%, which will create intense global competition for energy resources, the Commission considers this as a serious threat to the Union's energy supply security. Again, it was calling for Europe to have a unified position on global energy stage because "secure, sustainable and competitive energy is of fundamental importance to the EU's economy, industry and citizens and a core goal of EU policy."[162] It was stressed that the EU needs to take strong position on the international stage in order to secure its energy needs. At the same time, it should promote free and open energy markets and EU policies beyond its borders. Commission considers systemic EU approach to energy as the only way for the EU to secure its energy supplies. Close connection between external energy policy and internal energy market was underlined again. One dimension of energy policy (internal or external) cannot be successful without the other. Bilateral energy relations between individual Member States and energy producer and transit countries are thought to be, concluding from the past experience, contributors to the fragmentation of internal EU energy market. Bilateral energy relations are thought to undermine EU energy supply security and competitivity. In order to increase energy supply sources and supply routes, Commission proposed several large-scale infrastructure projects such as LNG terminals throughout Europe and new gas pipelines. This is seen as an essential step for the future of EU energy security. A proposal was also put forward to have future energy deals institutionalized between the EU Member States and non-members. For itself, the Commission proposed the role of monitor to oversee such deals. It also underlined that the balance in energy markets is changing fast due to the fact that half of the energy demand for the next 25 years is projected to come from India and China. This presents a challenge for

[160] Michal Meidan, "Perceptions and Misperceptions of Energy Supply Security in Europe and the 'China Factor'," in *Energy Security*, ed. Marquina, 38.
[161] EC, *Communication from the Commission to the European Parliament, The Council, The European Economic and Social Committee and the Committee of the Regions: On security of energy supply and international cooperation – The EU Energy Policy: Engaging with Partners beyond Our Borders*, COM (2011) 539 final (Brussels: EC, 2011), http://aei.pitt.edu/39619/1/COM_(2011)_539.pdf.
[162] Ibid., 2.

the EU and in Commission's opinion, merits strong and unified response from the EU to deal with such challenge.

As observed by Alexander Mirtchev, the aim of external energy policy presented in 2011 Communication is to strengthen partnerships with external suppliers, therefore, making them one of the stakeholders in the European energy security.[163] He identified several advantages of EU having unified external energy policy. Common policy would unify clashing strategies of the large number of its Member States. This would lead to more efficient economic outcomes with reduced price volatility which would lead to increased regional energy security. Common policy would also strengthen political stability leading to increased influence of the EU in global energy market. A unified stance in energy matters would also protect the EU from external energy shocks.

Union-wide coordination on energy matters is difficult to achieve due to increasing differences in energy exposure between different countries within the Union.[164] If these differences could be put aside, natural understanding is that with larger country comes larger power and influence. Block of countries with more than 500 million people, consuming one fifth of world energy used,[165] and speaking with one voice, would put the EU in a position to become a very powerful player in global energy market. The problem of speaking with one voice in Europe comes from EU Member States pursuing relative gains in energy matters, hence popularity of bilateral energy deals. There is no significant solidarity among EU Member States. Therefore, joint EU position on energy matters is difficult to achieve. With each Member State being responsible for its own territory's energy security, it reserves the sole right to decide on energy mix and type and where that energy comes from.[166] Member States also have their own distinctive ways of formulating and implementing energy policies.[167] They have different energy sectors with different energy mix. They also have different views on European integration and how far this integration should advance. Some Member States are largely dependent on Russia for their energy imports, some are not. With such differences, it seems to be difficult to integrate 28 different energy policies into one EU energy policy.

All the recent efforts by the EU institutions, mainly the European Commission, to strengthen the EU's internal energy policy and to promote cooperation in external energy policy, can be

[163] Mirtchev, "The New EU External Energy Policy."
[164] *Africa Confidential* 47, no. 9 (2006), quoted in Youngs, "Concepts of Energy Security," 20.
[165] "EU Energy Policy," European Council press release, 4 February 2011, 1, http://www.european-council.europa.eu/media/171257/ec04.02.2011-factsheet-energy-pol_finaldg.en.pdf.
[166] Pami Aalto, "European Perspectives for Managing Dependence," in *Russian Energy Power and Foreign Relations*, ed. Perovic, Orttung and Wenger, 162.
[167] Ibid., 168-169.

described as too little too late. Many experts point out that the opportunity was missed during the 1990s when Russia was going through economic crisis and the EU was experiencing economic prosperity. Now, EU energy policy is preoccupied with Russia and what to do with it. Antonio Marquina emphasizes failed EU opportunities in energy-rich Central Asian republics.[168] When Soviet Union disintegrated, the EU missed an opportunity to become a leader in the East-West energy corridor while Russia was still weak and Central Asian republics were in need of help and guidance. Instead, the EU watched as the United States took the political lead. In 1999, it was Bill Clinton who participated in signing ceremony in Istanbul where legal framework was put in place for Caspian oil and gas to reach Turkey. Trans-Caspian Gas Pipeline Agreement was signed by Turkmenistan, Georgia, Turkey and the United States, although, the project has not been realized yet. Legal framework for *Baku-Tbilisi-Ceyhan* (*BTC*) oil pipeline was signed by the then Secretary of State Madeleine Albright and officials from Azerbaijan, Georgia and Turkey. The EU had signed the "Partnership and Cooperation Agreements" with Central Asian republics which showed some interest in this area. This mainly consists of promoting favorable conditions for investment and business.[169] European philosophy is that this would result in favorable conditions for market economies to develop, and this would lead to the development of energy sector. The energy sector did develop in Central Asian republics but mostly because China and Russia joined and developed it for their own benefit.

Since the Maastricht Treaty and the creation of the European Union in 1993, there have been attempts to form a Union-wide energy policy. 1990s were characterized by low energy prices. This led to little being done on having a common stance on energy issues. With price hikes starting in 2000s and Putin using energy to reassert Russian power, many Europeans saw the benefit of speaking with one voice. Still, the EU is far from reaching consensus on external dimension of energy policy. It mostly consists of weak reaction to Russia's action which does not bode well for the prospect of common EU energy policy. Richard Youngs identifies two ways for the EU to move forward in energy matters: either it will turn to Realist thinking with every state pursuing individual material interests, or Member States will strengthen cooperation.[170] Besides the Commission's calls for solidarity and common energy policy, there is nothing tangible to suggest that Member States have been working on strengthening their cooperation. On the other hand, bilateral deals and new Russian pipelines to Europe which strengthen energy security of some Member States and undermine national security of other Members can be taken as evidence of individual Member States turning to Realist thinking and

[168] Marquina, "The Southeast-Southwest European Energy Corridor," 58-61.
[169] Ibid., 59.
[170] Youngs, "Concepts of Energy Security" 20.

pursuing their individual material interests. Seemingly existing outside of its Member States' realities, EU institutions are still promoting solidarity and cooperation; however, the EU's most powerful Members are not. National energy giants from such countries as Germany, Italy, and France have signed lucrative deals with Russian energy companies which would need to be revised if they turned to solidarity and cooperation.

3.2. RUSSIAN ENERGY: DEPENDENCE AND CONSTRAINTS TO COMMON ENERGY POLICY

With the disintegration of the Soviet Union, the EU attempted to have Russia as a participating country in its common energy space based on market rules and regulations.[171] Central to this plan was the ECT which marked the beginning of the EU's attempts to institutionalize its energy principles. Russia signed it in 1994 but it was never ratified. Ratification would have taken exclusive control of pipeline networks away from Russia and weaken Gazprom monopoly. Gazprom controls around 70% of Russia's gas production and holds export monopoly on gas.[172] The EU complained but Russia pointed out that major energy suppliers to EU – Norway and Algeria did not ratify the ECT, either.

With failed attempts during 1990s to have Russia ratify the ECT, the EU proposed the EU-Russia Energy Dialogue which was accepted and commenced in 2000. EU's aim was to have official platform for EU-Russia energy relations that would see Russia cooperating with the EU on principles that were acceptable to it from the ECT. They could not agree on important transit protocol but they did agree to cooperate on less significant issues such as enhancement of infrastructure connections, creating stronger business links and improving conditions for foreign investment. Europeans hoped that eventually they would be able to secure access to substantial energy reserves in Russia[173] since it was projected that interdependence will grow between them.

The EU energy policy towards Russia is characterized by lack of coherence. Member States' relations with Russia range from friendly to hostile. European countries started developing energy relations with Russia several decades before the EU which began developing energy

[171] Richard Youngs, "Russia," in Youngs, *Energy Security*, 80-81.
[172] David Kernohan and Evgeny Vinokurov, *The EU-Russia WTO Deal: Balancing Mid-term and Longer-term Growth Prospects?,* CEPS Commentary (Brussels: CEPS, 2004), http://www.vinokurov.info/assets/files/WTOcommentary.pdf, quoted in "Geopolitics of EU Energy Supply," *Euractiv.com*, 10 January 2007, http://www.euractiv.com/energy/geopolitics-eu-energy-supply/article-142665.
[173] "Geopolitics of EU Energy Supply," *Euractiv.com.*

relations with Russia during 1990s.[174] In this situation, it seems difficult for EU institutions to promote solidarity and cooperation when dealing with questions regarding Russia. Russia's special relation with the biggest EU economies (Germany, France and Italy) is also contributing to the lack of solidarity within the EU. It took EU three weeks to put together a common response regarding gas crisis that befell Europe when Russia cut-off gas supplies to Ukraine in January 2006.[175]

While EU institutions were criticizing Russia's actions and calling for EU unity in the face of Russian energy supply risk, the EU Member States were making new bilateral deals with Russia. Germany and Russia continued preparations for the *Nord Stream* gas pipeline project which would bring Russian gas directly to Germany, bypassing other states such as Poland and Ukraine which were outraged at this turn of events. Many considered *Nord Stream* construction as being nothing more than an obvious geopolitical move since there were more profitable options available to transport Russian gas to Germany. However, goodwill existing between Germany and Russia translated into pragmatic relations at the expense of wider EU interests.[176] Construction on *Nord Stream* started in 2010. This project strengthened bilateral energy relations between Russia and Germany. Gazprom and German energy companies worked closely on realization of this project and agreed to swap assets as well. Even Vladimir Putin and German Chancellor at the time Gerhard Schröder formed close personal relationship.[177]

South Stream pipeline project was put together in 2006 and was announced in 2007. Bulgaria, Serbia, Hungary, Slovenia and Italy were fast to make bilateral deals with Russia. Construction on *South Stream* started in 2012. It is the direct competition to the proposed *Nabucco* pipeline which is a pipeline favored and heavily promoted by the Commission since Russian gas was not planned to be used in filling this pipeline. Preparations for *Nabucco* first started in 2002. After several route changes and many agreements signed and promises made, *Nabucco's* future is uncertain at best. While the Commission was making plans and relying on trade and business instruments to decide the fate of *Nabucco,* by the end of 2006, Russia struck lucrative bilateral deals with most EU Member States, some of which already made promises to support the *Nabucco* project. Member States expediently backtracked on their support for the *Nabucco* project as soon as Russia offered them new energy deals. In situations where Europeans leave

[174] Aalto, "European Perspectives," 157.
[175] Youngs, "Russia," 82.
[176] Katinka Barysch, *Russia, Realism and EU Unity*, CER policy brief (London: CER, 2007), 2, http://www.cer.org.uk/sites/default/files/publications/attachments/pdf/2011/policybrief_russia_final_20july07-800.pdf.
[177] Kirsten Westphal, "Germany and the EU-Russia Energy Dialogue," in *The EU-Russia Energy Dialogue,* ed. Aalto, 102, 105.

their profit-seeking companies to decide on pipelines, Putin engages personally in extensive lobbying and tough diplomacy. While Europeans are motivated by profits, Russians are motivated by geopolitical results.[178]

Russia signed new deals with Belgium, France, Italy, Hungary and Austria, with further deals with German companies being signed as well. With these deals Russian companies, mainly Gazprom, gained access to European markets. In return, Gazprom promised secure energy supplies to each country that signed bilateral deal with Russia. Several EU States such as Latvia and Hungary competed fiercely to become new energy hub – a country which would be managing Russian gas on its way to other markets, by supporting projects that gave them best advantage over others.

Construction of new pipelines in Northern and Southern Europe has contributed to Central and Eastern European states losing importance and Northern and South-Eastern states becoming new energy hubs.[179] For example, in 2008, 80% of Russian gas on its way to Europe passed through Ukraine.[180] Nowadays that number is around 50%. Division between the EU Member States in regard to political relations with Russia was openly discussed by the Commission as early as 2004 in Communication published by the Commission.[181] In this piece, the Commission is critical of the lack of EU-wide cooperation in relations with Russia. The problem that Commission is facing is that if EU energy policy is to be successful, it should be seen as advantageous by all Member States.[182]

Building a direct gas pipeline to Germany, building a pipeline that made *Nabucco* unnecessary, making bilateral deals with EU States and promising to each one of them that they will become energy hubs for the Russian gas, is leading to the conclusion that Russia is making an effort to undermine the EU's attempts to form a common energy policy. Added to the list of efforts to undermine the EU's energy policy attempts are Russia's threats to cut back on gas supplies to EU and start exporting to Asian countries – mostly China.

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[178] Marquina, "The Southeast-Southwest European Energy Corridor," 64-66.
[179] Aalto, "European Perspectives," 176.
[180] Zorana Z. Mihajlović Milanović, *Energy Security in South-East Europe in Light of Russian Energy Policy* (Belgrade: ISAC, 2009), 2, http://www.isac-fund.org/download/06e-Dr.%20Zorana%20Mihajlovic%20-%20Energy%20security%20in%20SEE%20in%20Light%20of%20Russian%20Energy%20Policy.pdf.
[181] EC, *Communication from the Commission to the Council and the European Parliament: On relations with Russia*, COM (2004) 106 final (Brussels: EC, 2004), http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2004:0106:FIN:EN:PDF, quoted in Youngs, "Russia," 82.
[182] Mirtchev, "The New EU External Energy Policy."

Besides putting European countries to compete against each other, Putin seems to be attempting to have Europe and Asia as rivals for Russian energy.[183] Over the years Vladimir Putin has perfected the practice of playing EU Member States against each other – otherwise known as "divide and rule" tactic.[184] On this accusation, Putin responded that it was not him pursuing "divide and rule" tactic, but rather that EU Member States were lining up to sign bilateral deals with Gazprom.[185]

Just as the Commission announced the *Nabucco* pipeline as a priority, Hungary made a bilateral deal with Gazprom in March 2007 to support the *Blue Stream* extension project which rivals that of *Nabucco*, in order to secure its national energy supply for the future. Reacting to criticism from other EU States, Hungary responded that other countries do not show solidarity, that there is slow progress on common energy policy and that Hungary has to look after itself. Several days later, Greece and Bulgaria reached similar bilateral deals with Russia to secure their supplies for the future through *Trans-Balkan* pipeline,[186] although since then, Bulgaria has withdrawn its support for this project. In the same week, Putin visited Italy where new bilateral agreements were signed including agreement that deepened partnership between Italian energy giant *ENI* and Gazprom. Gazprom was allowed downstream access to Italian energy market, in return, Gazprom promised secure energy supplies to Italy until 2035.

Good relations between Italy and Russia are promoted by their energy giants *ENI*, *Enel* and Gazprom. *ENI* and *Enel* helped Gazprom acquire several *Yukos* assets, in return, Gazprom allowed them to participate in development of gas fields in Russia.[187] Other national giants in the EU signed similar deals like Italian energy companies. Signing bilateral deals with Russia comes with a promise of secure energy supplies for the future and for the biggest EU economies – an access to participate in new energy field developments in Russia. Russia, on the other hand, gets access to downstream markets and keeps EU States from speaking with one voice on energy matters. With energy becoming politicized and securitized issue, for Russia, keeping Europe apart seems to have become a top priority. The Commission was against such bilateral

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[183] Ariel Cohen, "Europe's Strategic Dependence on Russian Energy," *Backgrounder*, no. 2083 (Washington, DC: The Heritage Foundation, 2007), http://www.heritage.org/research/reports/2007/11/europes-strategic-dependence-on-russian-energy; Andrew E. Kramer, "Gazprom Reaps the Benefit of Friends in the Kremlin," *The New York Times*, 23 September 2006, www.nytimes.com/2006/09/23/business/worldbusiness/23sakhalin.html, quoted in Perovic, "Introduction," 9.

[184] Youngs, "Russia," 82.

[185] Ibid., 96.

[186] Vladimir Socor, "Agreement Signed on Trans-Balkan Oil Pipeline, Rival to Trans-Caspian Project," *Eurasia Daily Monitor* 4, no. 53, 16 March 2007, http://www.jamestown.org/programs/edm/single/?tx_ttnews%5Btt_news%5D=32596&tx_ttnews%5BbackPid%5D=171&no_cache=1#.VH9UAdKsVic, quoted in Youngs, "Russia," 86.

[187] "A Bear at the Throat," *The Economist*, 12 April 2007, http://www.economist.com/node/9009041.

deals but there was nothing it could do other than criticize. Russian officials responded that Russia was being unfairly criticized since long-term bilateral deals were signed with other countries such as Qatar and Norway and this was not met with complaints. Moreover, Russian officials stressed that in those bilateral contracts they agreed to sell below market rates and that Energy Dialogue between the EU and Russia allows for such long-term bilateral contracts anyway.[188]

Examination of EU-Russia energy dynamic leads to the conclusion that rhetoric and actions of EU officials are often contradictory. In May 2007, EU-Russia summit took place. General conclusion was that the summit did not go well and that atmosphere was not friendly. European energy giants *BP* and *Shell* were forced out of participating in lucrative field development projects in Russia and EU did not manage to take assurance from Russian officials that this will not happen again to future European investments. Issues on energy and market access were not resolved. There was no formal declaration by the end of the summit which meant that nothing had been agreed on. Many commented that Europeans took harder stance against Russia and that they stood united against Russia like never before.[189] However, this was followed by Spanish Premier visiting Russia with aim of securing new LNG contract and avoiding EU difficulties. Shortly after being very critical of Putin, Sarkozy went to Moscow on a friendly visit which resulted in Russia and France signing new cooperation agreement.[190] The Dutch government was pushing for the Netherlands to become new gas hub for Europe. *Gasunie* – Dutch gas company, took 9% stake in the *Nord Stream*[191], in return, Gazprom acquired option to buy stake in the Netherland's pipeline into UK.[192] Shortly after, Gazprom and *ENI* signed new deal, which was brought about by Putin and the then Italian Prime Minister Romano Prodi, to develop *South Stream* pipeline going from Russia to Europe under the Black Sea. In several months' time Bulgaria, Hungary, Serbia and Greece were on board to cooperate. Such bilateral deals have been identified as major culprits for the lack of solidarity within EU on energy issues.[193] However, national energy monopolies of the big European economies are too big for their governments to neglect their interests and turn to pan-European energy policy that would operate under best-for-all principle. Big European energy companies operate under the rule of profit maximization which means that they are in direct competition with each other for profits

[188] Youngs, "Russia," 87.
[189] Ibid.
[190] Ibid., 88.
[191] Susann Handke and Jacques J. de Jong, *Energy as a Bond: Relations with Russia in the European and Dutch Context*, Clingendael Energy Paper (The Hague: CIEP, Netherlands Institute of International Relations, 2007), 62, http://www.clingendael.info/publications/2007/20070900_ciep_energy_handke.pdf, quoted in Youngs, "Russia," 88.
[192] *Financial Times*, 7 November 2007, quoted in Youngs, "Russia," 88.
[193] Youngs, "Russia," 88-89.

from Russian energy projects. They compete for billions of dollars in profits and Gazprom decides how these profits will be distributed. Gazprom has agreements with *ENI* (Italy), *Gaz de France* (France), *E.On Ruhrgas* (Germany), *Gasunie* (The Netherlands), *BASF* (Germany), to name a few.[194]

Besides EU politicians, also contradictory in the EU are the wishes of most Central and Eastern European countries and European energy giants. EU Member States without big energy companies and with high dependence on Russian energy imports are the loudest supporters of unified EU approach towards Russia. Energy companies, on the other hand, are happy with things as they are – market considerations before politics. European companies are eager to work with Russia and to develop joint projects. They need to look for foreign opportunities and new energy fields to keep up their sales volumes since North Sea supply is drying out. Any new energy source opportunity is welcome, and in Russia there are many gas and oil fields waiting to be invested in and developed. Companies are looking to expand business with Russia even if it appears that Russia is sometimes bullying them. *Shell* and *BP* were forced to accept considerably diminished role in Russian energy projects. *BP* was forced to sell its 62.9% stake in Kovytka gas field to Gazprom in 2007 with option to buy back 25%. Other companies as well calmly accepted their diminished roles such as providing technical expertise and holding minority stakes. They had to agree to such terms in order to have at least some access to massive energy reserves in Russia. *Royal Dutch Shell* which is developing Sakhalin-2 oil field had to agree to pay $1 billion a year dividends to Russian government. Even big critics of Russia – Latvia and Lithuania, would probably be happy to see their Ventspils port and Mazeikiai refinery supplied with Russian oil again. However, pipelines to those facilities remain dry.[195]

Poland and Baltic States are the most active supporters of the unified EU approach on energy matters. They have also frequently experienced political problems with Russia in the past and there is certain animosity in their relations with Russia. Those states are eager to diversify away from Russia; however, they do not have the means to bring about large infrastructure projects which are needed for energy supply diversification.[196] They championed the proposed *Nabucco* gas pipeline which was supposed to bring non-Russian gas to Europe, however, Russia stepped in and began construction on the rival pipeline – *South Stream*, which effectively undermined the *Nabucco* project. This was followed by Russia and Germany moving forward with the *Nord Stream* pipeline which angered Poland and Baltic States even more. They had plans for an oil

[194] Mihajlović Milanović, *Energy Security in South-East Europe*, 2.
[195] Aalto, "European Perspectives," 167.
[196] Ibid., 175-176.

pipeline which would bring Azeri oil, but the involvement of Kazakhstan was needed for this pipeline to be feasible. Russia came in the way again because Kazakhstan energy resources are greatly controlled by Russia. Overall, Russia controls Central Asian pipeline systems which effectively limit European diversification prospects from this region. Besides rich European economies which are in minority, the rest of the EU Member States are in no position to decide on their energy security future. Antonio Marquina maintains that the EU-promoted approach to energy security as a matter of markets is not sustainable.[197]

When Russia is in question, energy dominates the EU's foreign policy considerations. EU institutions attempt to push energy matters into the sphere of high politics because Russia converts its energy wealth into considerable power and influence.[198] Standing in the way are major Member States who are anxious not to politicize their energy relations with Russia. Besides having an impact on the EU's energy policy, Russia also has an impact on the EU's enlargement policy, neighborhood policy, Central Asia and Black Sea policy, to name a few.[199] Importance of Russia in European affairs is substantial. Richard Youngs observed that Russian communism pulled Europe together after World War II, and in the new millennium, Russian energy is pushing it apart.[200] EU and Russia have not been successful in institutionalizing their relations. ECT and EU-Russia Energy Dialogue are failed attempts. Russia practices managed democracy; the EU adheres to market rules and regulations. Institutionalization of their energy relations is therefore difficult because both powers are pushing for their own mode of operation to prevail which creates friction in overall relations between the EU and Russia.

The European Council represents governments, the European Parliament represents citizens, but the European Commission represents the EU as a whole.[201] Political body of the Commission is composed of 28 Commissioners – one from each Member State. They are expected to work in the interest of the Union – not their home country. They hold the Union's executive power, managing day-to day implementation of EU policies, EU treaties, and management and allocation of EU budget. They are also the only EU institution with legislative initiative and they represent the EU internationally.[202] Creating common EU energy policy would mean giving another role to the Commission which would change the paradigm of energy geopolitics. This possibility faces resistance from the big EU economies which are already enjoying

[197] Marquina, "The Southeast-Southwest European Energy Corridor," 66.
[198] Youngs, "Russia," 97-98.
[199] Barysch, *Russia, Realism and EU Unity,* 8.
[200] Youngs, "Russia," 82.
[201] "European Commission," *Wikipedia,* last modified 23 November 2014, http://en.wikipedia.org/wiki/European_Commission.
[202] "European Commission," European Union, http://europa.eu/about-eu/institutions-bodies/european-commission/index_en.htm.

advantageous position[203] by promoting business interests at the expense of political ones.[204] Big EU Member States such as Germany, France, the UK and Italy are not ready to give up their advantages gained by favorable bilateral energy deals and they are not ready to transfer some of their sovereign rights to the Commission. Geopolitical advantages gained are impossible to give up voluntarily. It is unclear how new potential EU energy policy would affect existing bilateral deals such as France's and UK's involvement in Libya or how affected would be Germany-Russia close energy relations that have greatly benefited both Germany and Russia. The choice to form common energy policy has been compared to a choice in classic Prisoner's Dilemma.[205] If all member states sign cooperative agreement they would all be better off. However, there is strong incentive to make the first move and gain advantage over the others. In result, everybody acts for themselves to gain advantage. In this case, everyone is worse-off.

3.3. DIVERSIFICATION OF ENERGY SUPPLY SOURCES

Oil represents 60% of EU's energy imports, gas 26% and solid fuels 13%.[206] Table 2 below shows suppliers of crude oil and gas imports to the EU for the year 2010.

[203] Mirtchev, "The New EU External Energy Policy."
[204] Westphal, "Germany and the EU-Russia Energy Dialogue," 93.
[205] Mirtchev, "The New EU External Energy Policy."
[206] "EU Energy Policy," European Council press release, 2.

Table 2: Share of EU's crude oil and gas imports by destination, 2010[207]

	% of EU's crude oil imports	% of EU's gas imports
Russia	34%	35%
Norway	14%	27%
Libya	10%	3%
Saudi Arabia	6%	
Kazakhstan	6%	
Iran	6%	
Nigeria	4%	3%
Azerbaijan	4%	
Algeria		14%
Qatar		8%
Other	16%	10%

Source: Eurostat, April 2012

It should be noted that Russia's share in EU's gas supply has been decreasing over the last 15 to 20 years due to diversification. Biggest energy consumers are transport sector which consumes 33% of energy, households and services 39%, and industry 28%.[208] Currently EU imports approximately half of its energy needs; by 2030 that figure is projected to be 70%.[209]

In broad agreement in the EU, supply security is promoted by open and competitive markets.[210] Such markets would provide exchange of information, availability of investment and resources which would lead to diversified supply. Supply security does not mean that prices will be low. They may be high and volatile but that is considered as part of the cycle. Supply security is enhanced by diversification of energy sources, energy suppliers and transit routes, and in market economies such as EU, those choices are mostly left to business enterprises. Member States and the Union have the responsibility to put in place set of rules and regulations that companies must adhere to.

[207] EC, *EU Energy in Figures – Statistical Pocketbook 2012* (Brussels: EC, 2012), 22, http://ec.europa.eu/energy/publications/doc/2012_energy_figures.pdf.
[208] "EU Energy Policy," European Council press release, 2.
[209] Aalto, "European Perspectives," 158.
[210] Christian von Hirschhausen et al., "Supply Security and Natural Gas," in *Security of Energy Supply in Europe: Natural Gas, Nuclear and Hydrogen*, ed. François Lévêque et al., Loyola de Palacio Series on European Energy Policy (Northampton: Edward Elgar, 2010), 6-8.

The EU is facing increasing import dependence. Union is the largest importer of energy in the world and volumes imported are only set to increase. The EU spends approximately 2.5% of its GDP on energy imports (in 1999 it was 1.2% of its GDP). Around $372 billion is spent on oil and $55 billion on gas imports in a year.[211] In the new millennium, security of supply became an important issue on the agenda given the fact that discovery of new energy reserves is lagging behind increases in global demand. It was estimated that in 2035 global energy consumption will double from the consumption volumes of 2005.[212] China and India are at the forefront of global increase in energy demand due to their fast-developing economies. It is projected that by 2020 Asian energy consumption will account for more than one third of the world energy consumption.[213]

The EU is experiencing declining gas production and the lack of new field discoveries. Change in circumstances is best demonstrated in the case of the UK who went from gas self-sufficiency to being 40% dependent on gas imports in 2010s. By 2020, this dependence is projected to reach 80%.[214] The Netherlands is fighting to prolong the lifespan of its declining domestic reserves by putting a cap on domestic gas production for the period between 2006 and 2015.[215] It was projected that by 2030, the EU will be importing 80% of its gas demand.[216] Supply security of gas is an important issue on the EU agenda, but it is given special attention in Central, Eastern and South-Eastern Europe. These countries are under most pressure to diversify away from Russia which is attempting to take ownership of their national energy infrastructure. They fear that this would put them under Russia's control politically.

Increasing energy prices, wars and unrests in major energy exporting regions and Russian assertiveness made energy security top priority for the EU. One of the ways to improve energy security is to diversify sources of energy supply. The EU is in good geographical position to import gas from regions and countries not too far away such as Norway, Russia, North Africa,

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[211] Brian Wang, "Europe Plans to Spend One Trillion Euros by 2020 for Energy Grid Upgrades and Nuclear Included as a Core Part of the Plan," *Next Big Future Blog*, 4 February 2011, http://nextbigfuture.com/2011/02/europe-plans-to-spend-one-trillion.html.
[212] Youngs, "Introduction," 2.
[213] EIA, *International Energy Outlook 2006* (Washington, DC: DOE, EIA, 2006), http://www.eia.gov/forecasts/archive/ieo06/pdf/0484(2006).pdf.
[214] DTI, *Secretary of State's first report to parliament on security of gas and electricity supply in Great Britain* (London: DTI, 2005), quoted in Jonathan Stern, "The New Security Environment for European Gas: Worsening Geopolitics and Increasing Global Competition for LNG," in *Security of Energy Supply in Europe*, ed. Lévêque et al., 58.
[215] Machiel Mulder and Gijsbert Zwart, *Government Involvement in Liberalised Gas Markets: A welfare-economic analysis of the Dutch-depletion policy*, CPB Document 110 (The Hague: CPB Netherlands Bureau for Economic Policy Analysis, 2006), http://www.cpb.nl/en/publication/government-involvement-liberalised-gas-markets-welfare-economic-analysis-dutch-gas-deple, quoted in Stern, "The New Security Environment," 58.
[216] EC, *Green Paper,* 2006, quoted in Stern, "The New Security Environment," 58.

West Africa, Middle East, Caspian region and Central Asia.[217] Moreover, LNG trade is increasing which gives EU one more option to improve its supply security. The problem arises when it is considered that some of these regions are economically and politically unstable and building infrastructure that connects it to Europe may be too risky for companies that operate under market principles and profit considerations, therefore, seeking security for their investments.

3.3.1. North Africa

Expansion of North African energy deliveries is especially attractive for the EU's gas diversification prospects since it is a region with substantial gas reserves and export potential. There is room for new pipelines to be built and to expand the existing ones. Moreover, countries in the region are interested to increase gas volumes exported to Europe. *Enrico Mattei* (*Trans-Mediterranean*), *Pedro Duran Farrell* (*GME*) and *Green Stream* pipelines all have the potential for further expansion. There is also potential to build new pipelines such as *Medgaz* pipeline to Spain from Algeria which became operational in 2011, and proposed *Galsi* pipeline to Sardinia and Italy from Algeria.[218] Algeria from the region is an important source of relief for EU's dependence on Russian energy, with potential to further increase energy imports from this country. Oil and gas make up 97% of Algeria's exports. They account for 30% of national GDP and fund 65% of the state budget. Energy business is essential to Algeria and EU is an important partner. 62.7% of Algerian exports go to EU and 58% of Algeria's imports come from EU.[219]

3.3.2. West Africa

West Africa became important for global energy trade in 2000s when it became major LNG exporting region.[220] Nigeria was the first country in the region to develop LNG export business, followed by the LNG expansion in Angora and Equatorial Guinea. Although West Africa comes behind Middle East and North Africa when export potential is considered, there is a possibility of new reserves being discovered. West Africa is rich in energy resources and the EU could potentially increase energy imports from this region and increase investments to this region if not for the fact that most of energy exporting countries in the region are experiencing political

[217] Stern, "The New Security Environment," 58.
[218] Ibid., 71.
[219] "Geopolitics of EU Energy Supply," *Euractiv.com.*
[220] Stern, "The New Security Environment," 67.

unrests.[221] Nigeria is very important exporter of LNG and could be an important supplier to the EU. However, petroleum-related problems began in mid-2000s when people started rising against the government on accusation that they did not enjoy enough benefits from Nigerian booming energy business and they complained that energy companies were destroying their environment. Angola only recently emerged from 27-year old civil war and it remains to be seen how it will manage its energy exporting potential. Equatorial Guinea started LNG export in 2007; however, there are many complaints on human rights violations and transparency issues.

3.3.3. Middle East

Russia has the world's largest gas reserves, followed by Iran and Qatar in the Middle East. Saudi Arabia has substantial gas reserves as well; however, it chose to use gas for domestic consumption and to export only oil of the two.[222] In a short time Qatar will become the world's second largest gas exporter (first being Russia) and it will become the largest LNG exporter in the world. Qatar has already committed to building large LNG facilities on its territory.[223] In 2012, 30% of Qatar's LNG exports went to Europe.[224] With decaying infrastructure and underinvestment in new field development, Iran is not living up to its energy potential. In 2005, Iran exported less gas than prior to 1979 Iranian Revolution. It even became a net importer of gas in 2006-2007 when gas imports from Turkmenistan increased to levels that offset gas exports to Turkey.[225] With Iraq in political turmoil, besides Qatar, Middle East is not considered a good option for building gas pipelines to Europe.

3.3.4. Caspian Region and Central Asia

The EU has been active for years in attempting to have new pipelines built which would bring gas from Caspian and Central Asian countries such as Azerbaijan, Turkmenistan and Kazakhstan directly to Europe. Right now, gas from these countries ending up in Europe is mostly bought by Russia which makes it Russian gas when it reaches Europe through pipelines controlled by Russia. The main reason Russia refuses to ratify the ECT is precisely because it

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[221] Ibid., 71.
[222] "Economic Diversification Boosts Gas Pressure in Middle Eastern Markets," *Gas Matters*, March 2006, 13, quoted in Stern, "The New Security Environment," 66-67.
[223] "Gazprom: Ukraine's Plans to Import Gas from EU "Smack of Fraudulent Schemes"," *Kyiv Post*, 30 March 2013, http://www.kyivpost.com/content/business/gazprom-ukraines-plans-to-import-gas-from-eu-smack-of-fraudulent-schemes-322505.html?flavour=mobile.
[224] EIA, *Country Brief: Qatar* (Washington, DC: DOE, EIA, 2014), http://www.eia.gov/countries/analysisbriefs/Qatar/qatar.pdf.
[225] Stern, "The New Security Environment," 69-70.

holds a monopoly on pipelines and if it ratified that treaty it would be easier for the EU to buy gas directly from Kazakhstan or Turkmenistan for example.[226] By controlling Central Asian gas distribution, Russia controls East-West energy corridor. In 2007, Russia, Kazakhstan, and Turkmenistan signed an agreement by which Russia secured Kazakh and Turkmen gas for exclusive Russia distribution.[227] To Europeans this was a confirmation that Russia is not able to meet European demand by its own supplies. This fact has not stopped Russia to actively undermine the Union's diversification plans and for the most part, it has been successful, but it also experienced a few failures. Starting from 2018, Europe has managed to secure deliveries of Azeri gas from Shah Deniz 2 field in the Caspian Sea and other fields in Azerbaijan without using pipelines controlled by Russia.[228] The Trans Anatolian Natural Gas Pipeline (TANAP) and Trans Adriatic Pipeline (TAP) are expected to become operational in 2018, with construction to begin in 2015 and 2016 respectively.[229] TANAP pipeline will begin from Georgia-Turkey border, running through Turkey to Greek-Turkish border where it will connect with TAP pipeline. TAP will cross through Northern Greece, Albania, and Adriatic Sea to Southern Italy, where it will connect with Italian natural gas network. Another setback for Russian endeavors was the construction of the *BTC* oil pipeline, opened on 25 May 2005, running from Azerbaijan's capital Baku, passing through Georgia and on to Turkey's Mediterranean port Ceyhan. This project has been realized in great part thanks to the support of the United States and not the EU. The United States has been a major supporter of the Commission's efforts to diversify energy resources away from Russia due to its increasing frustration with Russia's political ambitions in Central Asia and Europe. *BTC* pipeline has been considered as a successful beginning of Western endeavor to bring energy from East to West without Russian involvement. Russia, on the other hand, claimed major victories with *Nord Stream* and *South Stream* gas pipelines. *Nord Stream* resulted in Ukraine, Belarus and Poland losing leverage as transit countries of Russian gas. *South Stream* made Commission-favored the *Nabucco* pipeline obsolete because there won't be enough demand for two gas pipelines in the part of Europe where *Nabucco* was supposed to deliver gas from Caspian region. Nevertheless, in December 2014, Putin announced that the *South Stream* pipeline project will not be

[226] Barysch, *Russia, Realism and EU Unity*, 6.
[227] Hui, *Energy Security Strategy in the European Union*, 20.
[228] Jan Hromadko, "EU Energy Chief: Need to Open Up More Gas Supplies from Caspian Region," *AutomatedTrader.net*, 28 November 2012, http://www.automatedtrader.net/real-time-dow-jones/119673/eu-energy-chief-need-to-open-up-more-gas-supplies-from-caspian-region.
[229] "What is TANAP," Trans Anatolian Natural Gas Pipeline, http://www.tanap.com/en/what-is-tanap; "TAP at a glance," Trans Adriatic Pipeline, http://www.tap-ag.com/the-pipeline.

realized.[230] With TANAP and TAP pipelines still expected to become operational in 2018, the EU can claim victory over Russia regarding development of the Southern energy corridor.

As far as oil production in the Caspian region is concerned, there are several difficulties and uncertainties. First, the amount of energy reserves is not certain with estimates for proven oil reserves ranging from 17.2 billion to 49.7 billion barrels.[231] Energy Information Administration (EIA) has estimated that by 2015, Caspian oil production will be approximately 4.2 million barrels per day. This will account for approximately 4.5% of world production.[232] Second complication is high cost of oil extraction, mostly in offshore fields.[233] Added to high costs is underdeveloped infrastructure and remoteness of the region.

3.3.5. Russia

Unlike most other major gas exporters, Russia is also a major gas consumer with domestic demand steadily increasing, giving Russia strong incentive to keep Central Asian gas supplies under its control. Gazprom's gas supply to domestic customers increased a little over 2% for 2001-2005 period to 307 billion cubic meters (bcm) in 2005.[234] During the same period, total gas delivered to Russian customers increased by 7%. Since 2002, an annual increase has been more that 2%.[235] In 2006 increase in gas demand was 4%. This development was a cause for concern and the probable reason why there is strong commitment to gradually increase domestic prices. Increased domestic prices would put pressure on increases in domestic demand which would allow Gazprom to either reduce production or increase exports.[236]

In the past few years Russia provided 12% of world oil trade.[237] Russia exports more than four fifths of its oil to the EU and Russia's share in the EU's oil market is around 30%. Oil products are also mostly exported to the Union. It is estimated that Russia holds between 5% and 10% of

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[230] "Russia drops South Stream gas pipeline plan," *BBC News*, 1 December 2014, http://www.bbc.com/news/world-europe-30283571.
[231] EIA, *Caspian Sea Region: Survey of Key Oil and Gas Statistics and Forecasts* (Washington, DC: DOE, EIA, 2006), quoted in Kelly and Leland, "Oil Actually," 43.
[232] EIA, *International Energy Outlook 2006*, quoted in Kelly and Leland, "Oil Actually," 43.
[233] Kelly and Leland, "Oil Actually," 43.
[234] Gazprom, *Gazprom in Figures 2001–2005* (Moscow: Gazprom, 2006), 28, http://www.gazprom.com/f/posts/73/210722/3statistika_eng_2001-2005.pdf, quoted in Stern, "The New Security Environment," 63.
[235] Gazprom, *Annual Report 2005* (Moscow: Gazprom, 2006), 41, http://www.gazprom.com/f/posts/57/005321/annual_report_eng_2005.pdf, quoted in Stern, "The New Security Environment," 63.
[236] Stern, "The New Security Environment," 63-64.
[237] Ministry of Energy, *Energy Strategy of Russia*, 21.

world's oil reserves.[238] In January 2011, Russia opened its first pipeline directly to China, supplying oil.[239] This created concerns that the EU will have to compete with China for Russian energy resources.

Although oil sector is more globalized, Russian supplies can still cause crisis as demonstrated by the events regarding Latvia's Ventspils oil port and Lithuania's Mazeikiai oil refinery in 2003 and 2006 respectively, when Russia stopped delivering oil through pipelines going to those complexes which made them non-operational. They had to turn to railroad and maritime transportation to secure oil supplies, which were less economical options.[240]

For gas, it is estimated that Russia holds one third of world reserves. By 2015, Russia's West Siberian gas fields will start drying up and decrease in production is a possibility if new fields are not developed. This created concerns within EU.[241] Also of concern for the EU is the fact that Russia may start exporting gas to Japan, South Korea and China through new pipelines because there are regular negotiations with those countries.[242] However, exploiting new fields in difficult climatic conditions in Russian north and East Siberia is considered to be too costly.[243] Another question mark is how far domestic energy demand will go and how much pressure it will put on energy exports, especially gas. It is thought that EU's dependence on Russian gas in absolute terms is unlikely to grow much further due to slow development of new gas wells in Russia.[244] Jonathan Stern of the Oxford Institute for Energy Studies argues that in the next few decades, the EU is unlikely to import much more than 185 bcm of Russian gas which was imported in 2006.[245] Europe's consumption of gas however is set to increase.[246] Additional gas could be imported from Norway, Algeria, Nigeria, Qatar, Iran, Egypt, Azerbaijan and

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[238] Aalto, "The EU-Russia Energy Dialogue," 27.
[239] "Russia-China Oil Pipeline Opens," *BBC News*, 8 January 2011, http://www.bbc.co.uk/news/world-asia-pacific-12103865, quoted in von Campe, "Energy Security in the United Kingdom," 27.
[240] Aalto, "European Perspectives," 163.
[241] Aalto, "The EU-Russia Energy Dialogue," 27.
[242] Aleksanteri Institute Eurasia Energy Group, *The Energy Dynamic on the Borders of the EU: Internal Dynamics of the Russian Energy Sector*, Memo, no.2 (Helsinki: University of Helsinki, Aleksanteri Institute Eurasia Energy Group, 2006), http://www.helsinki.fi/aleksanteri/energy/presentations/energy_dynamic_on_the_borders_of_eu.pdf, quoted in Aalto, "The EU-Russia Energy Dialogue," 27.
[243] Aalto, "The EU-Russia Energy Dialogue," 27.
[244] Aalto, "European Perspectives," 163-164.
[245] Jonathan Stern, *The New Security Environment for European Gas: Worsening Geopolitics and Increasing Global Competition for LNG*, NG 15 (Oxford: Oxford Institute for Energy Studies, 2006), http://www.oxfordenergy.org/wpcms/wp-content/uploads/2010/11/NG15-TheNewSecuirtyEnvironmentForEuropeanGasWorseningGeopoliticsandIncreasingGlobalCompetitionforLNG-JonathanStern-2006.pdf, quoted in Aalto, "European Perspectives," 164.
[246] Andrew Monaghan, *Russia and the Security of Europe's Energy Supplies: Security in Diversity?,* Special Series 07/02 (Swindon: Conflict Studies Research Centre, 2007), http://www.da.mod.uk/, quoted in Aalto, "European Perspectives," 164.

Turkmenistan.[247] Russia will always be important to Europe due to its proximity and its gas reserves, but with real commitment, other suppliers can be pursued to lessen Russia's weight in the European energy affairs.[248]

Within the EU, five countries depend 100% on Russian gas supplies in total gas consumption – Bulgaria, Estonia, Latvia, Lithuania, and Finland; six countries depend more than 50% on gas coming from Russia – Czech Republic (80%), Slovakia (63%), Slovenia (57%), Greece (54%), Poland (54%), and Austria (52%). Hungary uses 49% of Russian gas in total gas consumption, Belgium 43%, Germany 40%, Luxembourg 27%, Romania 24%, Italy 19%, France 17%, the UK 15%, and the Netherlands 6%.[249] However, it is noted that in primary energy consumption Russian gas does not go higher than 30% in any individual country, meaning that Member States would face difficulties if Russia cuts gas supplies but they would be able to manage it eventually. Overall, this would indicate that Russia's weigh in European gas supply is modest at best and not as alarming as frequently represented. However, the problem arises when considering countries that are completely or mostly dependent on Russian energy since they are landlocked, or they have no resources to start importing LNG, or they simply have no resources at their disposal to start any diversification projects. For those countries there are no alternative pipelines to bring energy from alternative sources. In 2012, 36% of total gas imports to the EU came from Russia. Norway is the second largest supplier of gas to the EU, covering 29% of EU's gas imports. However, most of those supplies go to Germany, France, the Netherlands, and the UK which is one of the reasons that those countries don't feel particularly energy insecure. 14% of EU gas imports come from Algeria with potential for the Southern Europe (being nearest) to further develop relations with energy-rich North African countries.[250]

3.3.6. LNG Prospects

Increased popularity of LNG trade will contribute to further diversification of EU energy supplies, though at higher prices than pipeline gas.[251] In 2012, LNG accounted for 26% of EU

[247] Gawdat Bahgat, "Europe's Energy Security: Challenges and Opportunities," *International Affairs* 82, no. 5 (2006): 961-964, quoted in Aalto, "European Perspectives," 164.
[248] Jan Kjärstad and Filip Johnsson, "Prospects of the European Gas Market," *Energy Policy* 35, no. 2 (2007): 869-888, quoted in Aalto, "European Perspectives," 164-165.
[249] "Gazprom's Grip: Russia's Leverage over Europe," *tableausoftware.com*, http://public.tableausoftware.com/views/GazpromsGripFinal/GG-final?:showVizHome=no.
[250] IGU, *Energy Dialogue: Russia-EU Gas Aspects* (Oslo: IGU, 2013), 1, http://www.gasnaturally.eu/uploads/Modules/Publications/rgs-eurogas_conference_30_may_2013_session_2_ferrier_01.pdf.
[251] von Hirschhausen et al., "Supply Security," 17.

gas imports.[252] This type of gas supply is particularly important for some Western EU States. 65% of Spain's gas imports come in the form of LNG.[253] Poland has plans to build LNG terminal on the Baltic Sea in order to diversify its energy supplies. Russia also plans to develop LNG export business with intention to sell it in Asia and even to the U.S.[254] At the beginning of 1990s, share of LNG in the global gas trade was 4%. By 2020, LNG share is expected to be 14%-17%.[255] Improved shipping techniques and new producers entering the market could somewhat reduce importance of piped gas and decrease Russia's leverage on Europe. Also of importance for European LNG import prospects is shale gas revolution in the U.S. which is removing the need for the U.S. to import LNG from other countries. This is freeing LNG from Qatar and other producers to go to Asia and Europe and it is putting downward pressure on pipeline gas prices in Europe. The U.S. is expected to start exporting LNG in 2016 and it remains to be seen whether significant amount will reach Europe or if majority will go to Asia where prices are higher.[256]

Coal continues to be an important energy source given the fact that it is used in 30% of the EU's electricity production.[257] The EU's dependence on imported coal is steadily increasing as well, from around one third now, to projected 51% by 2020.[258] Nuclear energy is losing in popularity after Japanese tsunami in 2011, and generally, the Commission leaves decisions to member states without much interference and interest.[259] Renewable energy continues to be on a small scale, accounting for less than one tenth of consumption.[260]

David G. Victor is of the opinion that diversification of energy supply sources guarantees protection to importing countries from the rent-seeking behavior of energy exporting and transiting countries.[261] Ukraine has done more for diversification of energy supply sources in

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[252] IGU, *Energy Dialogue*, 1.
[253] Paul Belkin, *The European Union's Energy Security Challenges,* CRS Report for Congress, order code RL33636 (Washington, DC: CRS, 2008), http://fas.org/sgp/crs/row/RL33636.pdf., quoted in Steven Woehrel, *Russian Energy Policy Toward Neighboring Countries*, CRS Report for Congress, order code RL34261 (Washington, DC: CRS, 2009), 19, http://www.fas.org/sgp/crs/row/RL34261.pdf.
[254] Woehrel, *Russian Energy Policy*, 19.
[255] Palonkorpi, "Energy Security," 8-9.
[256] Ed Crooks, "US shale gas exports to hit Gazprom revenue," *Financial Times*, 21 September 2014, http://www.ft.com/intl/cms/s/0/34c90b6c-419f-11e4-b98f-00144feabdc0.html#axzz3NEd9ECJT.
[257] Aalto, "The EU-Russia Energy Dialogue," 26.
[258] IEA, *Reducing Greenhouse Gas Emissions: The Potential of Coal* (Paris: OECD/IEA, 2005), 11, 23-24, https://www.iea.org/ciab/papers/ciab.pdf, quoted in Aalto, "The EU-Russia Energy Dialogue," 26.
[259] EC, *Communication*, 2007, 17-18, quoted in Aalto, "The EU-Russia Energy Dialogue," 26-27.
[260] Presentation of Christian Cleutinx, European Commission coordinator for EU-Russian energy dialogue, Luxembourg, 25 October 2005, quoted in Aalto, "The EU-Russia Energy Dialogue," 27.
[261] David G. Victor, Amy M. Jaffe and Mark H. Hayes, eds., *Natural Gas and Geopolitics: From 1970 to 2040* (Cambridge: Cambridge University Press, 2006), quoted in David G. Victor, "Natural Gas and Geopolitics," in *Security of Energy Supply in Europe*, ed. Lévêque et al., 101-102.

Europe than any other country in and out of Europe, company or organization, when it began to interrupt gas supplies from Russia to Europe starting from as early as 1995.

Plans for pipelines from Caspian region and the Middle East have been around for several decades but they stayed in planning stages because the possibility of a conflict between countries along the transit route cannot be excluded.[262] There is no guarantee that new pipelines would contribute to an improvement of European energy security over energy security provided by the Russian pipelines to Europe. Russians showed that they care to be perceived as a reliable supplier to Europe when they quickly resolved problems with Ukraine after gas deliveries to Europe were compromised.

Russia will stay an important supplier of energy to the EU for a long time to come. The EU has announced plans to exploit renewable energy and increase efficiency, however those projects take a lot of time and money. Given the current economic downturn, commitment to renewables and efficiency is questionable. It is also questionable how far they can replace oil and gas. Europe's potential to exploit other sources other than oil and gas, like coal, hydropower and nuclear power is limited given either nature's limits or environmental concerns. It should be questioned as well just how much it is in the interest of Europe to diversify away from Russia and import energy from unstable regions such as the Middle East and West Africa. Also, there is the problem of Asian countries looking to import energy from Russia and the EU might be looking at serious competition for Russian energy resources.

Conclusion

The main aim of this chapter was to examine how dependent EU is on Russian energy and to examine if Russian energy constraints the EU's ability to have common energy policy. As understood from this analysis, the overall EU's high dependence on Russian energy resources stems from several facts. First is that there is existing infrastructure in place connecting Russia and EU countries dating back to Soviet era. Building new pipelines to connect the EU with regions that are unstable politically or economically is deemed too risky and too expensive. When compared to other regions, Russia appears to be stable both economically and politically. Second is that Russia has world's largest natural gas reserves. Third is that Russia has been successfully undermining EU's diversification projects by applying pressure and buying up energy resources of potential new suppliers to the EU. This directly relates to the other part of the analysis that showed how Russia uses its energy wealth to prevent EU institutions to make

[262] Stern, "The New Security Environment," 71.

any real progress on the issue of common energy policy. As shown by several examples of natural gas and other energy crises, the EU is not able to guarantee energy security for its Member States as long as there is no common EU energy policy. By striking lucrative bilateral energy deals with individual EU Member States and building new pipelines that favor some Members and undermine national security of other Members, Russia prevents EU institutions to make any real progress on the issue of common energy policy.

CHAPTER 4: THE ROLE OF ENERGY IN RUSSIAN FOREIGN POLICY

This chapter will discuss Russia's domestic and foreign energy policies. First, this chapter will examine the importance of energy wealth for the Russian economy, social stability, and global standing and image. Linkage between energy sector and politics will be established by analyzing the tightening of state control over energy sector in the new millennium. This will be followed by the look at Russian energy giants and examine their role as instruments of not only Russian foreign energy policy but overall Russian foreign policy as well. Attempts by the Russian energy companies to increase their activities in EU markets and EU institutions' attempts to limit those activities will be examined. Finally, the second part of the chapter will look at the challenges facing Russian energy sector.

4.1. ENERGY SECTOR AND POLITICS

It is stated in the Energy Strategy of Russia that energy policy's objectives are to promote effective use of natural energy resources and maximize potential of the energy sector to contribute to economic growth, improve quality of life of country's population and improve foreign economic activities of Russia, leading to better standing of the country in world economic system.[263] The Importance of Russia's foreign energy policy is predetermined by the global nature of energy problems and their politicization and securitization, and by important role Russia plays in world energy sector. Strategic objective of foreign energy policy is full integration into world energy markets by efficiently using Russia's energy potential. From there, the intention is to enhance Russia's position and gain highest possible profits.[264]

Five problems facing Russia's foreign energy policy that need to be overcome were identified. The first is reduced prices and demand for Russian energy supplies due to world economic crisis. The second is insufficient diversification of sales markets for Russian energy. The third is Russia's dependence on transit countries. The fourth is low visibility of Russian energy companies in foreign markets. And the fifth is politicization of energy relations between Russia and other countries.[265]

The importance of energy sector for country's development is highlighted throughout the Strategy; such as Far East and Eastern Siberia regions which will be further developed socio-

[263] Ministry of Energy, *Energy Strategy of Russia*, 10, 15.
[264] Ibid., 55.
[265] Ibid., 57.

economically by the construction of new energy infrastructure in those regions.[266] Energy exports are expected to stay a major development factor for the Russian economy for the period up to 2030. However, it is predicted that the impact of energy export on the Russian economy will decrease as other industries begin to develop. Growth rates of energy exports will gradually slow down and by 2030, export volumes will stabilize. It is Russia's acknowledged long-term economic policy to diversify economic structure and decrease the country's dependence on oil and gas exports.[267]

The Strategy underlines that Russia is the single largest holder of natural gas reserves in the world with 23% of world reserves and leader in annual production of natural gas. Russia is also responsible for 25% of world natural gas trade and is a dominant gas supplier to European and CIS markets whose importance for Russia's energy export business is acknowledged. Russia also plays an important role in Central Asian countries' energy sectors by transporting their gas through Russian pipelines to EU and CIS markets. Plans were mentioned for new measures to be taken to reduce transit risks, such as further development and upgrade of export infrastructure so that Russia would continue to be a reliable supplier of energy given that 30% of European gas consumption is supplied by Russia (including Turkey but excluding CIS countries). However, plans are also made to downsize the importance of EU markets in the total volume of Russia's energy exports as it plans to diversify energy exports to Asian markets such as China, Japan, Republic of Korea and other countries of the Asia-Pacific region. Exports of oil and oil products to the region in total Russian oil export should grow from current 6% to 22-25%, for natural gas number should grow from 0 to 19-20%. Diversifying away from Europe is planned in order to have Russian energy sector less vulnerable due to high dependence on exports to European markets. Diversification to the East is meant to cement Russia's position as the leading energy exporter in the world by expanding its international business and making its companies more visible, efficient and profitable.[268] Strategy emphasizes the importance that Russia's energy policy gives to keeping stable relations with existing consumers of Russian exports and forming good relations with new consumers of Russian energy as well. This course of action is seen as important for global energy security as long as it does not conflict with Russia's national interests.[269]

The energy document lists several large scale completed projects that have enhanced security of transit and supply of Russian energy resources to Europe. The first is the *Blue Stream* gas

[266] Ibid., 19.
[267] Ibid., 22.
[268] Ibid., 21-23.
[269] Ibid., 55.

pipeline transporting Russian gas directly to Turkey under the Black Sea. The second is the first phase of the *Baltic Pipeline System* for oil which will see Russia delivering oil directly to its western customers by maritime transport from Baltic Sea and North Sea, undermining *Druzhba* pipelines passing through Ukraine and Belarus. The third is *Yamal-Europe* gas pipeline connecting Russia and Germany through Belarus and Poland. And the fourth is the first phase of the *Sever* oil product pipeline running along *Baltic Pipeline System*.[270]

Infrastructure projects whose implementation started with the aim of diversification of export markets are *Nord Stream* gas pipeline to Germany and the *Eastern Siberia-Pacific Ocean* oil pipeline to China. Agreements were made on the *South Stream* gas pipeline which was supposed to go under the Black Sea to Bulgaria, Serbia, Hungary, Slovenia, and Italy, with branches to Bosnia & Herzegovina and Croatia; the *pre-Caspian* gas pipeline from Turkmenistan to Kazakhstan and on to Russia; and the *Burgas-Alexandrupolis* oil pipeline from Bulgarian port of Burgas to Greek port of Alexandrupolis which will transport Russian oil (Bulgaria has however withdrawn its support for this project). The decision was also made to construct the second phase of the *Baltic Pipeline System* and to expand the *Caspian Pipeline Consortium* which delivers oil from Kazakhstan to Russia.[271]

Development and diversification of energy infrastructure was identified as an imperative for energy sector and it is imperative for Russia because energy sector is a major factor for the present and future long-term social and economic development of the country. The most important strategic infrastructure projects (implementation has already begun or it will soon begin) that will contribute to social and economic development of the country are: construction of oil pipeline *Eastern Siberia-Pacific Ocean*; construction of oil-product pipeline systems *Sever* and *Yug*; construction of gas pipelines *Nord Stream* and *South Stream*; construction of multiple gas-transport systems from the Yamal Peninsula; development of sea ports and transport infrastructure for liquid hydrocarbons transportation (oil, condensate, liquefied natural gas, and wide fraction of light hydrocarbons).[272]

Besides endeavors to connect Russia with as many international energy markets as possible, Russian energy companies are also encouraged to actively participate in the development of gas deposits in countries such as Algeria, Iran and Central Asian republics, as well as to participate in the construction of new interregional gas pipelines with the emphasis on South Asia. Russian

[270] Ibid., 56.
[271] Ibid., 56.
[272] Ibid., 61

gas producing companies are also expected to coordinate their export policy with those countries.[273]

As for the oil sector, since the collapse of the Soviet Union, Moscow has become increasingly dependent on the revenue from oil exports.[274] Oil exports generate more than four times the revenue of gas exports given that Russia exports three-quarters of its oil output and consumes two-thirds of its gas output which is sold below market price domestically.[275] Oil industry income supports political and economic system. Oil and gas account for approximately 30 % of Russian GDP, and since 2000, they have driven about half of Russia's GDP growth. Nowadays, oil provides almost 40 % of the government's tax revenues. Therefore, the health of Russian economy and state are linked to oil profits. Tax profits are transferred to the rest of the economy through investment programs, welfare, pensions, and subsidies. Oil revenue has helped keep Putin in power by enabling him to secure the support of various interest groups.[276]

Recovering from the economic downturn of the 1990s, in the new millennium, Russia became a key energy player in European and Eurasian markets. Leaving behind the neoliberal project of the 1990s (imposed by the West), in 2000s, Russia espoused the concept of managed democracy in which former intelligence officers from the Committee for State Security (KGB) and the Federal Security Service (FSB), such as Vladimir Putin, have key administrative roles in the government as well as state controlled oil and gas companies. Under managed democracy, Russian government seized control over energy sector either through ownership or through its substantial powers of influence. In the West this state of affairs is usually referred to as authoritarian political system.[277]

A good example of the close linkage between energy and foreign policy in Russia can be seen through the International Institute of Energy Policy and Diplomacy established at the Moscow State Institute of International Relations at the University of the Russian Ministry of Foreign Affairs. Many among the political and business elite are educated in this institution.[278] Close relationship between energy companies and Russian government can be seen by tracing

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[273] Ibid., 80.
[274] Thane Gustafson, "Putin's Petroleum Problem: How Oil is Holding Russia Back–and How It Could Save It," *Foreign Affairs*, November/December 2012, http://www.foreignaffairs.com/articles/138363/thane-gustafson/putins-petroleum-problem.
[275] Thane Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia* (Cambridge, MA: Harvard University Press, 2012), 3.
[276] Gustafson, "Putin's Petroleum Problem."
[277] Woehrel, *Russian Energy Policy*, 1-2.
[278] http://www.miep-mgimo.ru; Mark A. Smith, *Russia's Energy Diplomacy*, F75 (Swindon: Conflict Studies Research Centre, 2002), 1, http://www.da.mod.uk/, quoted in Morales, "Russia as an Energy Great Power," 26.

individuals who were involved in both administration and held a seat on boards of some of the biggest energy companies. Dmitry Medvedev has connections with Gazprom, Igor Sechin with *Rosneft*, Vladislav Surkov with *Transnefteprodukt*, Arkadi Dvorkovich with *Transneft*. Those are some of the high-ranking officials in Putin's administration who held top-level positions in stated companies[279] and they are expected to hold them again after they leave politics. Putin himself is expected to become Chairman of Gazprom after he decides to quit politics.

According to the World Bank data, during Putin's first term in the office as President (2000-2004), share of oil and gas sectors in country's GDP increased from 8 to 19%. Hydrocarbons were responsible for more than 50% of total exports. Oil alone accounted for more than 40%. During Putin's first term, oil exports increased by 80%.[280] It was fortunate for Russia that after 9/11, oil prices increased substantially, turning oil sector into very profitable business. From figures such as these regarding energy exports, it can be concluded that Moscow realized which path it should take to regain its Great Power status. Nuclear power status and the seat on the UN Security Council could not compare to energy weapon and its geopolitical efficiency in the post-Cold War world. Russia is considered to not be hesitating to use energy as a foreign policy instrument, leading to Russia frequently being accused of aspiring to become energy superpower.[281]

Strategy of using energy as a foreign policy tool was drafted under Putin's supervision as early as 2000. The 2000 Foreign Policy Concept states that "Russia must be prepared to utilize all its available economic levers and resources for upholding its national interests."[282] Under Putin's leadership, Russia capitalized on the fact that it ranks first in the world regarding natural gas reserves, second in coal and eighth in oil, to become energy great power. Russia became the world's biggest exporter of natural gas and second largest oil exporter.[283] As far as energy goes, Russia has comparative advantage over other world powers.

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[279] Julian Cooper, "The Economy," in Edwin Bacon, Bettina Renz and Julian Cooper, *Securitising Russia: The Domestic Politics of Putin* (Manchester: Manchester University Press, 2006), 167-168; Michael Fredholm, *The Russian Energy Strategy and Energy Policy: Pipeline Diplomacy or Mutual Dependence*, Russian Series 05/41 (Swindon: Conflict Studies Research Centre, 2005), 10, http://www.da.mod.uk/, quoted in Morales, "Russia as an Energy Great Power," 29.

[280] Rudiger Ahrend, "Towards a Post-Putin Russia: Economic Prospects," in *Towards a Post-Putin Russia*, ed. Helge Blakkisrud (Oslo: Norwegian Institute of International Affairs, 2006), 41-42, 46, quoted in Morales, "Russia as an Energy Great Power," 26.

[281] Fiona Hill, *Energy Empire: Oil, Gas and Russia's Revival* (London: Foreign Policy Centre, 2004), 1, http://fpc.org.uk/fsblob/307.pdf, quoted in Morales, "Russia as an Energy Great Power," 26.

[282] "The Foreign Policy Concept of the Russian Federation," Federation of American Scientists, http://fas.org/nuke/guide/russia/doctrine/econcept.htm, quoted in Morales, "Russia as an Energy Great Power," 26.

[283] EIA, *Country Brief: Russia* (Washington, DC: DOE, EIA, 2007), 1, http://www.eia.doe.gov, quoted in Morales, "Russia as an Energy Great Power," 26.

Moscow created and embraced its own Russian brand of managed democracy called "sovereign democracy". Democracy part in Russian understanding means only a system of political competition to choose the best leaders who will lead Russia on its way to becoming integrated into world economy. This will give Russia an access to investments and technology. Sovereignty means (besides traditional understanding of responsibility over territory and people) freedom from external influence in order to control strategic sectors and resources, such as energy sector and energy resources.[284]

Energy policy of Russia under Putin has been described as state capitalism. Ownership of energy companies is not truly public nor is it private. It is rather that state has control over them[285] as demonstrated by the case of *Yukos* – an energy company which attempted to behave as a private company and ignored strategic guidelines set by the state. It quickly went bankrupt and was taken over by the state-controlled entities. Mikhail Khodorkovsky's crimes were that he funded political opposition, he planned construction of new pipelines that would work as alternatives to state-controlled pipelines, and he was prepared to sell a portion of *Yukos* to U.S. companies *Chevron Taxaco* and *ExxonMobil*. Foreign investment is allowed in state capitalism but it has to be a minority stake so that state will retain control and remain a true owner.[286] Putin's vision was formed before he came to power. It was sharpened in his doctoral dissertation at St. Petersburg Mining Institute where he defended the right of the state to retain control over energy companies. He states that it is in country's national interest to limit rights of private owners:

> Regardless of whose property the natural resources and in particular the mineral resources might be, the state has the right to regulate the process of the development and use, acting in the interests of society as a whole and of individual property owners, whose interests come into conflict with each other, and who need the help of state organs of power to reach compromises when their interests conflict.[287]

In this view, oil and gas are strategically important resources, vital for the country's economic security, therefore, not to be left to market mechanisms. Private companies can be granted guardianship over energy resources but the true owner must remain to be the state.[288] Bringing

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[284] Mark A. Smith, *Sovereign Democracy: The Ideology of Yedinaya Rossiya*, Russian Series 06/37 (Swindon: Conflict Studies Research Centre, 2006), http://www.da.mod.uk/, quoted in Morales, "Russia as an Energy Great Power," 27.
[285] Anders Åslund, "Russia's Energy Policy: A Framing Comment," *Eurasian Geography and Economics* 47, no. 3 (2006): 324, http://www.tandfonline.com/doi/abs/10.2747/1538-7216.47.3.321?queryID=%24%7BresultBean.queryID%7D#.VINAM9KsVic; Michael Fredholm, *Gazprom in Crisis*, Russian Series 06/48 (Swindon: Conflict Studies Research Centre, 2006), 2, http://www.da.mod.uk, quoted in Morales, "Russia as an Energy Great Power," 28.
[286] Morales, "Russia as an Energy Great Power," 28.
[287] Fredholm, *Gazprom in Crisis*, 2, quoted in Morales, "Russia as an Energy Great Power," 28.
[288] Morales, "Russia as an Energy Great Power," 28.

his doctoral thesis from theory to practice, in December 2006, new law was introduced that requires at least 50% Russian ownership of gas pipelines and 75% ownership of oil pipelines.[289] This effectively restricted foreign ownership rights.

Putin's vision for Russia has been described as Great Eurasian Power with two-fold understanding. First, Putin seems to be aware that the age of competing with the United States is over. Still, Russia is one of the world's major powers. Second, the best way to consolidate this power status is in the post-Soviet space. Russia still sees this space as its sphere of influence and it supports multipolar system where powers like China and Russia would have more influence. This system would work as an alternative to U.S. hegemony. Therefore, Russia is working to maintain influence over countries in its near abroad[290] or to at least thwart their designs of getting closer to the West, and the major instrument at Russia's disposal to maintain influence in its near abroad is energy.

Russia's national security doctrine states that energy geopolitics is tool of Moscow's foreign policy.[291] Russia's National Security Strategy to 2020, released in May 2009 says that "Russia's resource potential…broadened the possibilities for the Russian Federation to reinforce its influence on the world stage."[292] In Russia, national economic and military-strategic interests are decided at the state level. Both Gazprom and Russian Navy can therefore be seen as extended arms of the Russian government.[293]

Russian energy companies are on a mission to purchase controlling stakes in pipelines, ports, refineries, storage facilities and other key energy assets in Central and Eastern European countries. Those markets are important because they are transit countries to lucrative markets in the West. Russian control over assets in those countries is a matter of security of demand and therefore, a matter of national security. When Eastern European countries sold assets that Russian companies were looking to buy to other companies, they frequently experienced energy supply cut-offs. Most of them were temporary but in some countries pipelines remained dry for

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[289] Kristina Kausch, *Europe and Russia, Beyond Energy*, FRIDE Working Paper 33 (Madrid: FRIDE, 2007), 5, http://fride.org/download/WP33.ING.pdf, quoted in Youngs, "Russia," 92.
[290] Morales, "Russia as an Energy Great Power," 25.
[291] Alexandros Petersen, "European Energy Security is not up to Europe," *EU Observer,* 19 March 2013, http://euobserver.com/economic/119420.
[292] Russian Government, *Russia's National Security Strategy to 2020*, approved by decree no. 537 of the President of the Russian Federation dated 12 May 2009, trans. Rustrans, last modified 17 September 2012, http://rustrans.wikidot.com/russia-s-national-security-strategy-to-2020.
[293] Kristian Atland, "Russia's Northern Fleet and the Oil Industry–Rivals or Partners?: Petroleum, Security, and Civil-Military Relations in the Post-Cold War European Arctic," *Armed Forces & Society* 35, no. 2 (2008): 364, http://afs.sagepub.com/content/35/2/362.

good.[294] Russia is fighting disobedience of some Eastern European countries by building pipelines on alternative routes. This resulted in those countries losing significance they once had as transit countries, losing fees, as well as losing their leverage over Russia. Russia prefers to supply energy through infrastructure it controls, hence, the recent activity of building new Russia-controlled pipelines to Europe. By building those new pipelines, Russia is also suspected of attempting to reduce the attractiveness of proposed pipelines from Azerbaijan and Central Asia to Europe. Many question Russia's ability to fill all those new and newly proposed pipelines with oil and gas. It is suspected that Russian energy companies will be filling pipelines that are passing through favored transit countries.[295] That would leave countries such as Ukraine, Poland and Belarus, for example, with half-empty pipelines and half-empty accounts from transit fees. Baltic States are also dealing with empty pipelines due to their unwillingness to sell some major energy assets to Russian energy companies. Russian oil companies have decreased or completely halted oil deliveries to Butinge oil terminal in Lithuania and Ventspils port in Latvia. Instead, Russia has increased use of *Baltic Pipeline System* and its oil terminal at the port of Primorsk.[296]

Russia has also been active in rising prices to former Soviet republics to market levels and eliminating subsidies they once enjoyed.[297] In those countries that are accumulating debt due to new market prices, Russia has been willing to take ownership of their key energy infrastructure assets in exchange for debt write-off. Even Russian allies such as Belarus and Armenia have faced price hikes.[298] Gazprom has been quick to substantially raise gas prices to those Eastern European countries that elected pro-Western governments to power. It is able to do this without consequences because those countries are mostly dependent on Russia for their gas supply and they are too poor to be able to initiate diversification projects. Gazprom increased energy prices to Ukraine and Georgia after elections that saw pro-Western leaders come to power, following Orange and Rose Revolutions in those countries.[299]

Georgia depends 100% on Russia for their natural gas consumption. Several times Georgia has experienced gas supply cuts and disruptions which, according to their former president Saakashvili, have been politically motivated:

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[294] Woehrel, *Russian Energy Policy*, 4.
[295] Vladimir Socor, "South Stream: Gazprom's New Mega-Project," *Eurasia Daily Monitor* 4, no. 123, 25 June 2007, http://www.jamestown.org/programs/edm/single/?tx_ttnews%5Btt_news%5D=32826&tx_ttnews%5BbackPid%5D=171&no_cache=1#.VIOdYtKsVic, quoted in Woehrel, *Russian Energy Policy*, 5.
[296] Woehrel, *Russian Energy Policy*, 4-5.
[297] Smith, "Russian Energy Pressure," quoted in Woehrel, *Russian Energy Policy*, 5.
[298] Woehrel, *Russian Energy Policy*, 5.
[299] Ibid., 6.

> …Manipulation of energy prices and supplies is a critical tool of those in Russia who believe that hydrocarbons are the best means of political influence…Russia's arbitrary cut-off sent a clear message to the European Union: There can be no energy security when an undependable neighbor is willing and able to use its energy resources as a weapon in political influence.[300]

By announcing the *Nord Stream* gas pipeline that bypasses Poland and transports Russian gas directly to Germany under the Baltic Sea, Polish president Lech Kaczynski in 2007 accused Moscow of using energy as a political weapon. For Poland, the *Nord Stream* pipeline meant that second trunk line to *Yamal* pipeline will not be constructed as previously planned.[301] The former Czech Deputy Prime Minister Alexandr Vondra complained as well:

> Unjust manipulation or interruption of energy supplies is as much a security threat as is military action… Post-Soviet countries have been experiencing that on a daily basis, as Russia's appetite for using energy as a political weapon is growing.[302]

4.1.1. Energy Companies: Tools of Russian Foreign Policy

Five companies account for more than 80% of oil and gas production in Russia.[303] Out of these, two are state-owned. The first is Gazprom which is a natural gas monopoly. In 2005, it became a major oil producer as well by acquiring 73% of *Sibneft*. The second is oil company *Rosneft* which is 75% owned by the state. In 2004 it acquired major *Yukos* assets. Other three companies are *Lukoil*, *Surgutneftegaz*, and *TNK-BP*. They are private companies. However, *Surgutneftegaz* is believed to be very close to Kremlin, and Russian shareholders in *TNK-BP* are expected to fall under pressure and sell their stake to government-controlled entity. Dmitri Abzalov, an analyst at the Centre for Contemporary Russia Politics, believes that recent police pressure on *TNK-BP* was a clear message by the government that this venture needs to come to an end because it became too profitable for foreign investors. Consequently, in 2013, *TNK-BP* was acquired by *Rosneft*.

In Russia, economic power is politicized. Catherine Locatelli, a Russian energy researcher at the French government's Centre National de la Recherche Scientifique (National Center of Scientific Research), points out that Kremlin's power in energy sector comes from regulating

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[300] Mikheil Saakashvili, "The Path to Energy Security," *The Washington Post*, 9 January 2006, http://www.washingtonpost.com/wp-dyn/content/article/2006/01/08/AR2006010801167.html, quoted in Palonkorpi, "Energy Security," 7.
[301] Aalto, "European Perspectives," 166.
[302] Alexandr Vondra quoted in: "East Europeans Slam Russia's Political Use of Energy," *RFE/RL Newsline*, 12 October 2007, quoted in Aalto, "European Perspectives," 166.
[303] Jean Foglizzo, "Russia's new energy strategy seems a lot like its old one," *The New York Times,* 30 March 2008, http://www.nytimes.com/2008/03/30/business/worldbusiness/30iht-rnrgruss.1.11526942.html?_r=1&.

rights through tax and licensing system as well as issuing permits for exploration and production. Kremlin also holds control over foreign direct investment. In 2006, *Royal Dutch Shell* was forced by the Russian government to give up its controlling stake in Sakhalin-2, an LNG project, at a low cost to Gazprom after several delays in production and accusations of environmental mismanagement.[304]

That energy companies report to the state and are under state influence was best demonstrated by the case of former oil giant *Yukos*. Its head Mikhail Khodorovsky became critical of Putin and planned projects that were contrary to government-approved strategy. He wanted to sell some major parts of the *Yukos*' business to the U.S. company *Exxon Mobil*, which state-controlled companies were looking to buy. In the short period of time company went bankrupt due to government claims of unpaid taxes, its leader was arrested, and *Yukos* was acquired cheaply on auction in 2004 by the state-owned oil company *Rosneft*.[305]

4.1.1.1. Oil Companies

During 1990s Russian government did not have a large stake in Russian oil companies. Oil companies were run by businessmen who were politically well-connected, called oligarchs.[306] Before Putin came to power, Russia's four major private oil companies were *Lukoil*, *Yukos*, *TNK*, and *Sibneft*.[307] Only *Lukoil* has remained. Change of policy was demonstrated on the oil giant *Yukos* in 2003. Observers believe that Khodorovsky was arrested because he showed alarming level of political independence from politicians in Kremlin, which was unacceptable to Putin administration.[308] In 2005 Gazprom bought (at a cut-rate price) another major oil company – *Sibneft*, from oligarch Roman Abramovich. He was not jailed. This company is now called *Gazprom Neft*. With those acquisitions, Russian government came to directly control over 30% of oil production in Russia.[309] In 2006 Putin was on record saying that state would not be taking control of any additional oil companies. However, state increased its control over oil sector by other means, such as forcing foreign oil companies to sell their stakes in lucrative oil fields on Russian territory to Russian state companies. Private oil companies such as *Lukoil* are careful to keep close relations with Kremlin and not to antagonize Putin administration because the

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[304] Ibid.
[305] Youngs, "Russia," 91.
[306] Woehrel, *Russian Energy Policy*, 3.
[307] Atland, "Russia's Northern Fleet," 372.
[308] Woehrel, *Russian Energy Policy*, 3.
[309] Peter Finn, "Russian Giant Expands Control of Oil," *The Washington Post*, 29 September 2005, http://www.washingtonpost.com/wp-dyn/content/article/2005/09/28/AR2005092801195.html, quoted in Woehrel, *Russian Energy Policy*, 3.

administration controls all oil companies directly or indirectly. Russian oil companies are still working with foreign companies but foreigners need to be satisfied with minority stakes. Besides increasing control over oil production, the state also controls oil and refined products pipelines through state-controlled company *Transneft*. This oil pipeline monopoly gives government leverage against private Russian firms, foreign investors and foreign countries as well.[310]

4.1.1.2. Gazprom

Most of natural gas supply and export structure in Russia was inherited from the former Soviet Union. Gazprom was created in 1989. In 1993 it became a joint-stock company with the government's share in ownership being 36%. Russian legislation of 1992 recognized Gazprom as a natural monopoly and allowed only 10% of foreign participation in its ownership. In 2005 reform was undertaken that opened up company for foreign participation of up to 49% in exchange for the state controlling 51%.[311] Gazprom controls almost 90% of Russian gas production and more than quarter of global natural gas reserves. "It also controls banks, industrial holdings, farms, and media outlets." With such massive operations, Gazprom is the single largest contributor to government's budget. Company also increased its operations in the oil sector by purchasing oil company *Sibneft*. Gazprom's intent was to make up for losses in domestic gas sector with profits from the oil sector. Domestic losses are more than recouped in the EU where Gazprom earns two thirds of its revenue.[312]

Putin originally promised to break up Gazprom but this never came through because he came to rely more and more on Gazprom for projecting Russia's influence abroad.[313] This also led to empowerment of Gazprom beyond energy business and profits. It was Gazprom's chief executive officer who felt comfortable enough to send a warning and a threat to European ambassadors in Moscow in April 2006, saying that "attempts to limit Gazprom's activity in European market will lead to no good results."[314] Under Putin's leadership, Gazprom became more active internationally; such as in Algeria, one of Europe's main gas suppliers and major alternative to Russian gas for Europe. This move was interpreted as an attempt to control

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[310] Woehrel, *Russian Energy Policy*, 3.
[311] Andrei V. Belyi and Caroline Kuzemko, "Conflicting Values in Gas Markets: A View on the UK-Russia Relations," in *Energy Security*, ed. Belyi.
[312] Woehrel, *Russian Energy Policy*, 2-3.
[313] Youngs, "Russia," 91.
[314] Vladimir Milov, "The Use of Energy as a Political Tool," *The EU-Russia Review* 1 (Brussels: EU-Russia Centre, 2006), 18, http://www.isn.ethz.ch/Digital-Library/Publications/Detail/?ots591=0c54e3b3-1e9c-be1e-2c24-a6a8c7060233&lng=en&id=48824, quoted in Youngs, "Russia," 91.

European supply diversification efforts and if necessary, to attempt to thwart it. Linkage between energy companies and government is best demonstrated by the fact that it is highly expected that Putin will take over as head of Gazprom once he decides to leave office.[315]

4.1.1.3. Russian Energy Companies in the EU

Russian energy companies are present in European energy networks despite the Commission's protests. According to a survey done by *Business Week, Lukoil* controls Petroleum refinery in Romania, the Neftokhim refinery in Bulgaria, and Ukraine's Odessa refinery (which was recently sold to Austria's *AMIC Energy Management GmbH,* including sale of *Lukoil-Ukraine CFI* which owns 240 filling stations and 6 tank farms[316]). Despite some quarters protesting, Western companies are eager to cooperate with their Russian counterparts. Germany's chemical giant *BASF* sold part of its distribution subsidiary to Gazprom. In return, it got access to the Yuzhko-Russkoye field. *E.ON* energy group is willing to sell its Hungarian operations to Gazprom in return for gas exploration rights in Russia. Concluding a deal with *Conoco-Phillips* which was approved by the Commission, *Lukoil* was allowed to buy more than 300 gas stations. According to *Business Week* article, this would "increase *Lukoil's* share of the retail markets to 6% in Poland, 10% in Bulgaria, 11% in Cyprus, 22% in Romania, and 29% in Finland."[317]

The Commission has proposed the EU policy that would prohibit energy-producing companies to own EU distribution networks. The Commission is feeling uneasy at the prospect of Russian energy companies acquiring whatever they can in the EU's downstream energy markets. The policy would also restrict the participation of foreign companies in the EU distribution markets unless distribution markets in their own home countries were opened up as well. Moscow was strongly critical of such proposals. The EU demands from Russia that it open up its pipelines to foreign investment and to provide stronger protection to foreign investments in its energy sector. Those are the ECT principles that Russia has been rejecting for two decades.[318]

The Commission can invoke the Competition Law and restrict Gazprom's activities in the EU due to the fact that Gazprom is monopoly in its own country and this goes against the EU's reciprocity principle. This principle is integrated in the EU Internal Market Directives and can

[315] Youngs, "Russia," 91.
[316] Stephen Bierman and Ilya Arkhipov, "Lukoil Sells Ukraine Filling Stations as Fighting Saps Sales," *Bloomberg Businesweek*, 31 July 2014, http://www.businessweek.com/news/2014-07-31/lukoil-sells-ukraine-filling-stations-as-fighting-saps-sales.
[317] Martin Walker, "Russia v. Europe: The Energy Wars," *World Policy Journal* 24, no. 1 (2007): 4, http://wpj.sagepub.com/content/24/1/1.citation.
[318] Woehrel, *Russian Energy Policy*, 4.

be used by Member States to restrict access to their markets to those companies coming from countries without liberalized markets. Gazprom is critical of this state of affairs and maintains that this was a deliberate move to restrict its participation in EU markets. Gazprom is looking to increase control in the whole chain of gas market, from gas production to gas distribution, which is making EU institutions uneasy. Russia considers liberalization of EU markets as a major danger for the security of demand, hence Gazprom's wish to enter distribution business in the EU.[319] By gaining control of distribution markets in Europe and building new export pipelines, supplemented by long-term contracts which have take-or-pay clause requiring importer to pay for gas regardless of the actual demand, Gazprom is looking to increase security of demand. This guarantees that investments in new gas production capacity will be profitable. Gazprom is looking to first secure sale of its gas before it has gas available to fill pipelines.[320] In words of Gazprom CEO: "Gas will not be produced until it is sold."[321]

The EU and Russia have different views on the meaning of reciprocity and it has been a point of contention between them. Gazprom is of the opinion that the EU proposal to introduce legislation limiting access to foreign companies in EU's downstream markets is directed against Gazprom. The EU wants Russia to ratify the ECT and to open up its oil and gas supply market which is monopolized by state-controlled monopolies *Transneft* for oil and *Gazprom* for gas. The EU's stance is that if Russia is to be allowed full access to EU market then EU companies should be allowed full access to Russian market as well. In the view of EU, ECT ratification would increase transparency and bring about reform in Russia's energy sector.[322] On the other hand, Russian Energy Minister Viktor Khristenko says that EU companies invest more in Russia than Russian companies invest in EU. He maintains that Russia does not have more limitations on foreign investment than the EU.[323]

Russia has given EU institutions a reason to feel uneasy. There were attempts from Russia to coordinate export policy with other European suppliers such as Algeria. Russia has also hinted that majority of future energy exports could be going to Asia and the U.S. instead of Europe. This could be achieved once new pipelines and LNG facilities are finished. Common response from the EU to such threats seems unlikely. Central and Eastern European countries are calling

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[319] Belyi and Kuzemko, "Conflicting Values."
[320] Perovic, "Introduction," 9-10.
[321] Aleksei Miller, "Gazprom–Strategy for the Energy Sector Leadership," Speech at the Annual Shareholders Meeting, Moscow, 30 June 2006, http://www.gazprom.com/about/management/shareholders/2006/report/, quoted in Perovic, "Introduction," 10.
[322] Perovic, "Introduction," 10.
[323] Anthea Pitt, "Russia and EU Ignore Access Row," *Upstreamonline.com*, 16 October 2007, www.upstreamonline.com/live/article142431.ece, quoted in Perovic, "Introduction," 10.

for stronger EU stance against Russian energy threats.[324] However, the EU's most influential Member States such as Germany and Italy and their energy giants have formed close ties with Moscow which promised them secure energy supplies and provided them with opportunities to invest in lucrative energy projects in Russia. They maintain that mutual dependence exists between Russia and consuming countries. They back this claim up by pointing out that the current system of gas pipelines and long-term supply contracts leaves little choice for Russia but to continue supplying its gas to Europe.[325] As for oil deliveries from Russia, many EU countries are less dependent on Russian oil than they are on gas, and oil source would be easier to change than gas as oil market is more flexible.[326]

There is no concrete evidence that Russian energy companies are primarily pursuing foreign policy goals of its government. Cutting subsidies to former Soviet republics is considered a sound business decision; however, timing of it was a little suspect. Building new pipelines is also a sound business decision to diversify export routes. However, many countries heavily dependent on Russian energy are very concerned that Russia will use their dependent position to pursue political goals by interfering in their domestic politics and force them to make foreign policy concessions to Russia. Many states are also afraid that if Russian energy companies are given control of energy infrastructure in their countries, Russia would be able to interfere into domestic political affairs by favoring selected ruling elite and supporting their political agendas.[327]

4.2. ENERGY SECTOR CHALLENGES

During Putin's two terms in the office as President, oil refinery output increased from 173 million tons in 2000 to 237 million tons in 2008. Export of oil products grew from 57 million tons in 2000 to 112 million tons in 2008.[328] Increased involvement of Russian energy companies from oil production to refining and distribution is identified as strategically important for the development of oil industry.[329] This expansion of oil business was fueled by the fact that in 2000, world oil price was $27 per barrel; in 2008, the price was $94 per barrel.[330] However, warnings were issued in the Energy Strategy of Russia that from initial oil reserves, more than

[324] Woehrel, *Russian Energy Policy*, 4.
[325] Belkin, *The European Union's Energy Security Challenges,* quoted in Woehrel, *Russian Energy Policy*, 4.
[326] Woehrel, *Russian Energy Policy*, 4.
[327] Ibid., 5-6.
[328] Ministry of Energy, *Energy Strategy of Russia*, 67.
[329] Ibid., 72.
[330] Ibid., 13.

50% has been depleted and that 77% of current oil production comes from large deposits with provision estimated only for the next 8 to 10 years. Soon companies will be operating more and more on hard-to-recover deposits. Gas deposits in main gas producing region – West Siberia, in main gas deposits, have been depleted by 65-75% and decline in production has begun.[331]

Jeronim Perovic has identified two challenges for the Russian energy sector.[332] The first challenge is whether Russia will be able to keep energy production at sufficient levels to keep its foreign and domestic energy supply commitments. Many are questioning Russia's ability to keep exporting present levels of oil, increase gas supply to Europe, satisfy increased domestic gas demand and overall substantial energy consumption, and export oil and gas to Asian markets. Reasons for concern are due to the fact that majority of present energy production comes from large but declining oil and gas fields and the fact that there isn't enough investment in exploration and development of new wells.[333] The IEA estimated that investments of around $328 billion would be needed for the 2001-2030 period in the Russian energy sector in order to maintain current production levels.[334] Steven Woehrel states that in the long-run, Russia may moderate its authoritative approach to energy policy because many experts believe that in the future Russia will depend on huge Western investments and expertise to develop new oil and gas fields in remote and difficult-to-reach areas. This may create an opportunity for the West to persuade Russia to open up its energy sector to Western ownership. On the other hand, current system has provided state and its officials with massive wealth and has cemented Russia's status as global power. Changes in such system are bound to be resisted and difficult. So far Russia's control over Central Asian energy flow has delayed development of new wells in remote areas such as Far East, Eastern Siberia and Arctic. Russia is engaging with energy-rich Central Asian countries, both economically and politically, in order to maintain its position as the only channel for Eurasian energy on its way to Europe.[335] Russia is the most significant buyer of gas from Turkmenistan, Uzbekistan and Kazakhstan. However, countries in Central Asia and Caspian region are looking to free themselves from dependence on Russian pipelines. Those countries are working to diversify export routes and their resources are not under exclusive Russian control anymore. There is now oil pipeline from Azerbaijan to Georgia and Turkey pumping

[331] Ibid., 62-63
[332] Perovic, "Introduction," 7.
[333] Alan Riley and Frank Umbach, "Out of Gas: Looming Russian Gas Deficits Demand Readjustment of European Energy Policy," *Internationale Politik–Global Edition* 8 (2007): 83-90, http://www.ssoar.info/ssoar/handle/document/13094; Vladimir Milov, Leonard Coburn and Igor Danchenko, "Russia's Energy Policy 1992–2005," *Eurasian Geography and Economics* 47, no. 3 (2006): 285-313, http://www.tandfonline.com/doi/abs/10.2747/1538-7216.47.3.285#.VIN0L9KsVic, quoted in Perovic, "Introduction," 7.
[334] Foglizzo, "Russia's new energy strategy."
[335] Woehrel, *Russian Energy Policy*, 19-20.

Azeri oil without Russian involvement. Some of Turkmen gas is flowing to Iran. There is an oil pipeline from Kazakhstan to China with further shipments from Central Asia to China only set to increase.[336]

The second challenge identified is the negative effect of high oil rents on domestic developments and increased distortion of domestic economy in favor of raw material sector.[337] According to the Bank of Finland 2008 report, oil and gas industries account for 50% of central government budget revenue as well as 65% of export earnings.[338] According to the World Bank report, in 2006, oil and gas sector accounted for 20% of Russia's GDP, 30% of foreign direct investment, and 60% of export earnings.[339] Besides Russian government claiming to work towards developing other sectors of the economy, numbers are saying otherwise. Raw material sector has been growing steadily in the post-Cold War period. According to data obtained from Russia's Federal State Statistics Services, in 1995, mineral products accounted for 42.5% of Russia's total exports. In 2005 that number was 64.8%. In 2012 it increased to 71.4% of total exports. Including metals and timber, in 2012 raw material sector's share in total exports was 84.4%.[340] Government has supported other sectors such as IT and aviation industry, however, progress has been slow.[341]

Perovic also points out that 2% of working population in Russia is employed in oil and gas sectors but many more profit from it directly or indirectly.[342] State profits substantially from energy sector by collecting taxes, duties and fees. In 2004 oil stabilization fund was set up. By January 2008, fund held $156.81 billion.[343] By the end of 2007, state accumulated foreign exchange reserves in excess of $474 billion. This puts Russia as the third largest holder of foreign exchange reserves with only China and Japan holding more.[344] However, only part of state-collected revenues from oil and gas go to those funds. Another part is redistributed to

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[336] Perovic, "Introduction," 5.
[337] Ibid., 7.
[338] Foglizzo, "Russia's new energy strategy."
[339] World Bank, *Russian Economic Report*, no. 13 (Washington, DC: World Bank, 2006), quoted in Perovic, "Introduction," 7.
[340] "Commodity Structure of Exports of the Russian Federation," Russian Federation Federal State Statistics Service, http://www.gks.ru/bgd/regl/b11_12/IssWWW.exe/stg/d02/26-08.htm, http://www.gks.ru/bgd/regl/b13_12/IssWWW.exe/stg/d02/26-08.htm.
[341] Perovic, "Introduction," 8.
[342] Ibid., 7.
[343] "Russia Oil Fund Rises to $156.8 bln on Jan 1," *Reuters*, 9 January 2008, http://uk.reuters.com/article/oilRpt/idUKL0971670520080109, quoted in Perovic, "Introduction," 8.
[344] "Russia's Gold, Foreign Exchange Reserves Grew by $7.8bn," *Kommersant*, 10 January 2008, quoted in Perovic, "Introduction," 8.

many different funds, projects, companies and officials.[345] Energy prosperity under authoritarian government has led to political stability which is bought by redistribution of rents to conflicting interest groups in order to make them content. Energy has provided government with means to carry out social development projects and keep electorate happy but it has also increased corruption. With government concentrated on keeping power, little has been done for the long-term prosperity of the country, such as developing other sectors of the economy as well. High rents allowed government to keep opposition and society in check and to exercise control over them. Economic growth is brought about mostly by the development of raw material sector. Social, economic, and political stability are in the hands of a well-functioning energy sector, with expected continuation of high energy prices on international energy markets.[346]

Over-reliance on energy can also become a point of vulnerability because its economic growth depends on world energy prices, availability of customers, transport routes and reserves.[347] There are limitations to using energy as a foreign policy tool because energy export entails interdependence between suppliers and consumers. Supplier needs consumer just as much as consumer needs supplier. Security is found in diversification of both suppliers and consumers, which is a policy that Russia has been pursuing. The danger for Russia lies in underinvestment in new field development, production facilities, infrastructure, and general modernization of energy technology. Danger also lies in increased domestic demand for natural gas which would put strain on Russia to fulfill its export commitments. Therefore, as stated in their Energy Strategy in 2010, rising domestic gas prices and suppressing increases in domestic gas demand will increase energy security of the country.[348]

Conclusion

The aim of this chapter was to examine why Russia sees energy as a tool and to explore ways in which Russia uses energy as a tool. As shown in this chapter's analysis, international energy sales (mostly to the EU) are responsible for filling up Russia's national budget and for accumulating substantial foreign exchange reserves. Energy has become the most important source of Kremlin's domestic and international power. This power is harnessed through tight control over its big energy companies. Being a nuclear power and holding a seat on the UN

[345] The Brookings Institution, *The Russian Federation–Executive Summary*, The Brookings Foreign Policy Studies Energy Security Series (Washington, DC: The Brookings Institution, 2006), 8, http://www.brookings.edu/~/media/Research/Files/Reports/2006/10/russia/2006russia.pdf, quoted in Perovic, "Introduction," 8.
[346] Perovic, "Introduction," 8.
[347] Morales, "Russia as an Energy Great Power," 26.
[348] Ministry of Energy, *Energy Strategy of Russia*, 76-77.

Security Council only supplements Russia's energy power. When threatening EU countries and other countries in its near abroad, Russia does not threaten with nuclear strike or UN sanctions – it threatens with dry pipelines. Russia can do this because the rest of Europe is energy poor and energy hungry. As much as there has been talk about supply diversification, for the foreseeable future Russia will continue to be the most important energy supplier to Europe.

CHAPTER 5: ENERGY POLICIES IN CONFLICT

This chapter will look at the nature of the conflict between the EU and Russia due to their diverging energy security policies. For the EU, energy security means pushing for liberalized energy markets in its neighborhood and in Russia. For Russia, energy security means firm state-control over energy sector and long-term bilateral energy contracts with both CIS and EU countries. The EU and Russia share neighborhood where their strategic, economic, security and energy interests are at stake. Often those interests become intertwined and hard to distinguish, preventing any significant EU-Russia cooperation. However, the EU is major buyer of Russian energy and Russia is major energy supplier to the EU. Economic interests and energy link between the two are forcing them into mutual dependence and cooperation. First, this chapter will examine how energy contributes to the conflict of great power aspirations by the EU and Russia. This will be followed by the discussion on politics of gas pipelines and how pipelines affect the overall EU-Russia relations. Then it will analyze whether there is indeed a political conflict between the EU and Russia or if it is a narrative constructed by some commentators and media that was endorsed as true. Finally, this will be followed by the evaluation, connecting theory with the EU-Russia rivalry.

5.1. THE HISTORY OF EU-RUSSIAN ENERGY RELATIONS

Energy relations between Europe and Russia began in late 1950s when oil and gas pipelines were built to Eastern Europe. Soviet oil and gas were reaching Poland, East Germany, Czechoslovakia, Hungary, Romania, and Bulgaria. Western Europe began receiving Soviet gas in late 1960s as Western European countries were looking to diversify away from oil to natural gas. Negotiations were held between Soviet Union and Austria, France, Italy, West Germany, Sweden, Finland, and Japan on the topic of Soviet gas deliveries. In 1968, Austria was the first non-communist state to receive Soviet gas which entered through Czechoslovakia, based on 20-year contract.[349] Starting in 1970, several multi-decade contracts were signed between Soviet Union and *Ruhrgas* for the delivery of Soviet gas to West Germany and France. Energy trade with Europe provided USSR with over 60% of its hard currency earnings. This was incentive enough for Soviets to suggest higher volume of gas deliveries to Europe, following the Iranian revolution in 1979. They began negotiations in 1980 with Western European gas companies,

[349] Robert E. Ebel, *Communist Trade in Oil and Gas: An Evaluation of the Future Export Capability of the Soviet Bloc* (New York: Praeger Publications, 1970), quoted in Closson, "Russia's Key Customer," 91.

banks and equipment manufacturers for the construction of East-West gas pipeline. Despite U.S. protests, Western Europeans provided the equipment in 1982 for the construction of the East-West gas pipeline. Europeans saw this project as an opportunity for domestic employment and diversification away from oil, and Americans were worried that Soviets would use earnings from this gas pipeline to finance their military arsenal.[350] The United States was also concerned about the possibility that Soviets would use France and Germany's dependence on Soviet gas to improve their bargaining position against the West.[351] The project went ahead, proving that the United States was right. Soviets tried to bargain and in the process lost diplomatic leverage that project afforded them by threatening to impose penalties on Western European companies if they sided with the United States.[352] Soviet threats backfired because after this, Europeans and Americans agreed to limit Soviet gas imports to 30%, and instead develop Norway's Troll field in the North Sea.[353] Despite those plans, by the end of the Cold War, energy imports form the Soviet Union did rise more than 30%. By 1982, France, West Germany and Italy were importing between 15 and 30% of their gas supplies from the Soviet Union. By 1990, those figures were between 30 and 36%.[354]

The next stage in Europe-Russia energy relations began with the disintegration of the Soviet Union in 1991. Russia's entire economy (including energy sector) was in chaos following transition to market economy. This led to fall in energy production. Russia reached 1990 energy production level again only in 2005. The country experienced economic meltdown in 1998, following Asian financial crisis of 1997. Even with low energy prices which resulted in the disappearance of its foreign currency reserves, Russia continued to meet its supply commitments to European customers. It continued to export energy to 14 European countries, with increased volumes to nine of those countries. Greece was added as a client in 1996. Crude oil exports to eleven European countries increased as well, including new customers Czech Republic, Finland, Germany, Lithuania, Hungary, and Italy.[355] Increase in export volumes was possible due to decreased domestic consumption resulting from the collapse of industrial

[350] Daniel Yergin, *The Prize: The Epic Quest for Oil, Money and Power* (London: Simon & Schuster, 1991), 742, quoted in Closson, "Russia's Key Customer," 91-92.
[351] Thane Gustafson, "Energy and the Soviet Bloc," *International Security* 6, no. 3 (1981-1982): 65-89, quoted in Closson, "Russia's Key Customer," 92.
[352] Thane Gustafson, *Crisis Amid Plenty: The Politics of Soviet Energy Under Brezhnev and Gorbachev* (Princeton, NJ: Princeton University Press, 1989), quoted in Closson "Russia's Key Customer" 92.
[353] Yergin, *The Prize,* quoted in Closson, "Russia's Key Customer," 92.
[354] John Van Oudenaren, *The Urengoi Pipeline: Prospects for Soviet Leverage* (Santa Monica, CA: Rand, 1984), 21, quoted in Closson, "Russia's Key Customer," 92.
[355] IEA 2007 database, requested from: www.iea.org/Textbase/stats/index.asp (sent by e-mail, 12 March 2008), quoted in Closson, "Russia's Key Customer," 92.

complex in the former Soviet space. Contributing to increased exports were also Western investments in upstream development and pipeline construction in Russia and Central Asia.[356]

The EU and Russia started to officially formalize their energy relations in the mid-1990s through international treaties. In 1994, the EU and Russia signed Partnership and Cooperation Agreement which was based on liberal economic principles. It came into force in 1997.[357] In 2000, the EU and Russia started Energy Dialogue within the framework of PCA. On the EU's side, this dialogue was initiated under the assumption that Russia will liberalize its energy market which would lead to more transparent, secure and predictable energy relations.[358] Both the EU and Russia published energy strategy documents looking 20 to 30 years ahead and both documents recognized mutual dependence and need for increased energy cooperation in the coming decades.[359] Senior officials were chosen to lead the dialogue and working groups were created to properly address issues such as investments, infrastructure and related energy issues. In 2001, in the Joint Statement by the EU and Russia, it was stated that besides energy partnership, the goal was to have Russia participate in the development of the EU's internal market.[360] To further the success of this dialogue, the EU opened Technological Center for Information and Technology Exchange in 2002 and the Permanent Council for Mutual Cooperation in 2005. Improvements in integration of EU's and Russia's energy markets were observed, including interconnection of electricity grids, agreement on regulation principles for internal markets and long-term supply contracts, and cooperation in nuclear energy and advanced energy technologies. However, in the most important part of the dialogue concerning hydrocarbons, any progress was difficult to achieve. The reason for this was that both sides had different expectations from this dialogue. Russia was looking to secure long-term contracts for its gas deliveries, to get access to technology and investments, and to have limits on Russia's energy product exports to the EU removed. The EU agenda, on the other hand, was to have Russia opening up its energy sector for foreign investments and foreign ownership. The

[356] Closson, "Russia's Key Customer," 92-93.
[357] *The Partnership and Cooperation Agreement* (PCA, 1997) and the *Protocol to the PCA* of 27 April 2004 available at: www.delrus.ec.europa.eu/en/p_243.htm, quoted in Closson, "Russia's Key Customer," 93.
[358] Barysch, *Russia, Realism and EU Unity*, 5.
[359] EC, *Green Paper*, 2000; EC, *European Energy and Transport Trends to 2030* (Brussels: EC, 2003), http://ec.europa.eu/dgs/energy_transport/figures/trends_2030/1_pref_en.pdf; Ministry of Industry and Energy (Minpromenergo), *Energeticheskaia strategiia Rossii na period do 2020 goda*, approved as decree no. 1234-r by the Russian government on 28 August 2003, quoted in Closson, "Russia's Key Customer," 93-94.
[360] Joint Statement by the EU and Russia, 3 October 2001, http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/er/12423.en1.doc.html, quoted in Closson, "Russia's Key Customer," 94.

dialogue was made even more difficult by EU Member States having diverging interests, depending on their level of dependence on Russian energy imports.[361]

Besides Energy Dialogue making slow progress, Russia also never ratified the ECT that it signed in 1994. The reason for this was that it includes provision for free transit across the territory of states that have signed the Treaty, as well as provision for dispute settlement by international mediation. Russian side complained that it would require Russia to make too many changes with little advantage to their energy companies. Russians object to anyone taking stake in Russian pipelines and to economic organizations interfering in what they consider strictly their own business.[362]

5.2. CONFLICT OF POWER ASPIRATIONS

European and U.S. reactions to the 2006 Russia-Ukraine gas dispute led to worsening of political relations between Russia and the West. The United States and the EU became disillusioned with Russia's poor commitment to democracy and economic reform. This disillusionment was further confirmed by the confidence and assertiveness of the Russian government and its energy companies in projecting their energy interests internationally. Moscow, on the other hand, pointed out that the West was applying double standards when it comes to Russia and other energy producing states and their record of economic reforms and democracy. Popular opinion in Moscow became that the West was worried about Russia's economic and political rise after Russia's weakness during the 1990s.[363] A narrative was constructed in Russia where privatization of oil and gas companies during the 1990s and Western support for liberal oligarchs at the time was part of a larger plot to weaken the Russian state and strip it of its great power status and influence, regionally and internationally. Re-nationalization of energy companies was thus justified as a necessary step to strengthen Russian state, free it from hostile Western nations and their energy companies who wanted to exploit Russia's energy resources for their own benefit[364], and regain its international power status.[365] The concept of sovereign democracy became popular among the ruling elite as an ideological

[361] Handke and de Jong, *Energy as a Bond*, 45, quoted in Closson, "Russia's Key Customer," 94.
[362] Tatyana Romanova, "Energy Partnership – A Dialog in Different Language," *Russia in Global Affairs*, no. 1 (January-March 2007), http://eng.globalaffairs.ru/numbers/10/1085.htm; Valery Yazev, "I am Against the Ratification of the Energy Treaty," *Kommersant*, 15 November 2006, quoted in Closson, "Russia's Key Customer," 94.
[363] Stern, "The New Security Environment," 68-69.
[364] Leonid Bershidsky, "Big Oil Deal Helps Putin more than Russia," *Bloomberg View*, 24 October 2012, http://www.bloombergview.com/articles/2012-10-24/big-oil-deal-helps-putin-more-than-russia.
[365] Dannreuther, *International Relations Theories*, 10-11.

challenge to the Western concept of liberal democracy. Centralization of power at home coincided with Russia's assertiveness abroad.[366]

Popular opinion in the West regarding Russia is that no foreign government can take Russia as seriously as it insists on being taken, even if its power is diminished due to the nature of its political and economic system. Russia is seen as being obsessed with great power, international standing and rank. Western opinion is that even if Russian demands were carried out, it would lead to further demands that would never cease due to Russia's insistence on being taken seriously as a great power. Some analysts go as far as to say that Russia is not making decisions based on strategic thinking of costs and benefits considerations, but it is rather making decision that in Kremlin's view would lead to preservation of its power status. Its power status is to be cemented in its sphere of influence where countries meant to uphold Russia's power appetite are experiencing erosion of their sovereignty, mainly due to Russia using energy as a foreign policy tool. Russia has been described as still trying to undo the status quo of 1989-1991.[367]

Russia's new foreign policy doctrine, as of 2008, gives Russian policy new orientation towards the EU and towards countries in its neighborhood.[368] Under this new foreign policy doctrine, Russia is not looking to institutionalize its relations with the EU. In the words of Foreign Minister Sergey Lavrov, Russia is "a self-sufficient country." As a self-sufficient country, unique alliances with countries in its vicinity are also to be left in the past. As a great power looking for a comeback, Russia is pursuing foreign policy that will create new world order which will be dominated by national interests under the framework of collective leadership.[369]

Russian foreign policy has been effective in creating fear of Russia in its near abroad. Rainer Lindner argues that Russian policies in the new millennium signaled an end to the post-Soviet space as a region of common political culture.[370] Importance that Russia gives to the post-Soviet space and to plans to spread influence in its near abroad can be seen by the creation of foreign

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[366] Youngs, "Russia," 90.
[367] Stephen J. Blank, "Resetting the Reset Button: Realism about Russia," *SSI Newsletter* (Carlisle, PA: U.S. Army War College, SSI, 2009), 3-4, http://www.strategicstudiesinstitute.army.mil/pdffiles/PUB956.pdf.
[368] "Konceptsiya Yneshney Politiki Rossiyskoy Federatsii (Conception of the Foreign Policy of the Russian Federation)," Kremlin, 15 July 2008, http://kremlin.ru/acts/785, quoted in Rainer Lindner, "New Realism: The Making of Russia's Foreign Policy in the Post-Soviet World," *The EU-Russia Review* 8 (Brussels: EU-Russia Centre, 2008), 28, http://www.isn.ethz.ch/Digital-Library/Publications/Detail/?ots591=0c54e3b3-1e9c-be1e-2c24-a6a8c7060233&lng=en&id=99772.
[369] "Vystuplenie na soveshchanii s poslami i postoyannymi prestavitelyami Rossijskoj Federacii pri mezhdunarodnykh organizatsiyakh (Speech at a meeting with ambassadors and charge d'affaires of the Russian Federation with international organisations)," Kremlin, 15 July 2008, quoted in Lindner, "New Realism," 28.
[370] Lindner, "New Realism," 29.

policy organization called The Federal Agency for CIS Affairs in 2008, which is modeled on the United States Agency for International Development (USAID). Agency's responsibility is to assist Russia and Russian citizens living in the post-Soviet space. It is attached to foreign ministry but it answers directly to the president. The agency deals with soft security and it is responsible for strategic planning and implementation of Russian policy in the post-Soviet space.[371] If not being a global power, Russia shows signs of wanting to cement its position as a regional power.

Russia's new foreign policy has been described as being based on commercialization, securitization of regional and international relations and on displays of power. This has been described as post-ideological approach. Several events have been identified which led to this new approach to Russian foreign policy. First is the perception of political and economic competition between the EU, the United States, China and Russia. Second is growing opposition to Russian designs to increase its influence in the post-Soviet space by national governments in its vicinity, by foreign actors and institutions. Third is Russia's diminished role as a dominant partner for investments and foreign trade. And the fourth is Russia's lack of vision for integration of its near abroad that would be attractive to its neighbors and that could compete with the EU.[372]

Russian government has put an emphasis on national interests where economic and energy goals remain embedded in geostrategic thinking. Russia has undergone a change from empire to energy power. The EU is seen as a threat to Russia because Russia's interior weakness becomes apparent when compared to the EU which is a successful federation of states with common internal market. It is an attractive concept to non-member states. For Russia, the EU is seen as less of a partner and more of a rival for influence in the post-Soviet space.[373] According to Realist Theory, this rivalry is unavoidable because they are engaged in a zero-sum competition. More power for one means less for the other. This power struggle in a zero-sum competition was demonstrated during 2014 Ukraine breakdown which happened because (following the 2006 and 2009 gas crises which generated much discussion and controversy) Ukraine was finally forced to choose its alignment with either the EU or Russia. Given that approximately 50% of Russian gas export to the EU is passing through Ukraine, its importance to both is significant. Rainer Lindner describes EU-Russia relations as economically close but politically

[371] Vladimir Solovjev, "SNG Popadet pod Ylivanie Rossii," *Kommersant,* no. 133, 31 July 2008, http://kommersant.ru/doc.aspx?DocsID=917672, quoted in Lindner, "New Realism," 30.
[372] Andrey I. Suzdaltsev, "Postsovetskoe Prostranstvo: Edinstvo i Mnogoobrazie" (The Post-Soviet Space: Unity and Diversity)," in Sergey Karaganov, *Rossia i mir. Novaya Epoha. 12 let, kotorye mogut vse izmenit* (Moscow: 2008), 384-410, quoted in Lindner, "New Realism," 30.
[373] Lindner, "New Realism," 30-31.

distant.[374] Energy potential is used as a weapon to accomplish wider Russian interests. Among other things, it is primacy in the EU's neighborhood. Good neighborliness policy has been dropped in favor of policy based solely on national interests. This circumstance has the potential to strongly affect its future relations with the EU. Yet, Russia depends on the EU because the EU is its main partner in modernization.

Russian foreign policy in the new millennium has resulted in Moscow having no close allies in the region. Even Belarus is no longer considered a close ally. In the Strategy Paper of the Council for Defense and Security Policy titled "The World Around Russia 2017", only Kazakhstan is perceived as the last reliable partner in the neighborhood. In 2007, Belarus and Russia were engaged in a conflict over energy transit and prices. Russia halted economic privileges it bestowed on Belarus, and chose to pursue economic self-interest. It abandoned the approach based on ideology and historical myths towards post-Soviet republics, and embraced more pragmatic approach based on national interests shaped by economic considerations.[375] This new approach received encouragement in its origin by the fact that Russia's problems with CIS countries started when pro-Western governments came to power in Moldova, Georgia and Ukraine, with aspirations to distance themselves from Moscow's influence. They wanted to align their countries with NATO and the EU.[376] Russia's conflict with the countries of the former Soviet Union showed that Russia sees itself as an influential power at the same level with the EU and the United States, and sees countries in its near abroad as non-existent actors at the regional stage at all.[377]

European security architecture became a frequent point of discussion since Russia was able to reassert its power internationally. Russia disliked its diminished role in European security matters and it always opposed to NATO and EU enlargement towards what it considered its sphere of influence. However, first serious moves to reassert its international power status and protect its influence in the post-Soviet space came in 2008, when Russia undertook military action in Georgia to reassert its political, military and security interests in its near abroad.[378] Russia's attack on Georgia in South Ossetia was significant because it was Russia's first military operation outside of Russia in more than ten years. It showed that Russian foreign policy has become militarized as well, besides other changes in foreign policy brought about by

[374] Ibid., 31.
[375] Ibid., 31-32.
[376] Stern, "The New Security Environment," 69.
[377] Lindner, "New Realism," 29.
[378] Sandra Fernandes, "The Idea of European Security: The Renewed Russian Dilemma," *E-International Relations*, 25 October 2012, http://www.e-ir.info/2012/10/25/the-idea-of-european-security-the-renewed-russian-dilemma/.

accumulated wealth from energy. Russia also fiercely opposed the prospect of Ukraine and Georgia joining NATO and the EU. Ukraine and Georgia are regarded by Russia as falling under its sphere of influence, important for its energy flows, and therefore, national security. NATO made a commitment to the expansion to Ukraine and Georgia in Bucharest in April 2008. Russia responded by issuing threats to the West because to Russia, this was a clear sign of provocation by the West.[379] On the prospect of Ukraine joining NATO, and NATO setting up a missile defense system, some Russian officials such as Sergei Karaganov responded by speculating about confrontation with possible military components.[380] Subsequently, the accession of Ukraine and Georgia to the EU and NATO was put on hold at the time.

The importance that Russia gives to having the absolute influence in its near abroad can be seen in the case of Moscow demanding all U.S. military bases out of their sphere of influence. The United States has a base in Kyrgyzstan and refueling and over-flight rights in Kazakhstan and Tajikistan. There is also a small NATO base in Tajikistan. This makes Russia and China uneasy. They attempted to have NATO and U.S. bases closed in the region by putting pressure on those countries allowing Western military to be present on their soil. In July 2005, Shanghai Cooperation Organization with Russia and China at the forefront released a declaration calling for a date to be set for withdrawal of U.S. troops from the region. The United States responded that it maintains bases in Central Asia only as a support for its operations in Afghanistan and existence of those bases is of great importance for the success of Afghan operations. Calls for U.S. troops to leave Central Asia are thought to be energy related. Russia and China seem concerned that the United States will use its presence as a platform to support its geopolitical and energy policy objectives and take control over energy pipelines in Central Asia and Caspian. This would clash with Russian and Chinese geopolitical plans for the region.[381]

Although the United States is not dependent on Russian energy and energy trade volumes between the two are small, Russian energy policy is important to Washington for larger strategic considerations. The United States is concerned about Europe's dependence on Russian energy and has often called for diversification away from Russia. It is also concerned about Russian domestic developments and Russia's increasing international assertiveness and its willingness to use energy as a foreign policy tool.[382] The United States has been engaged on the issue of Eurasian energy supplies and even forwarded some energy projects in the Caspian region,

[379] Lindner, "New Realism," 32-33.
[380] *Rossiyskaya Gazeta*, 26 March 2008, http://www.rg.ru/, quoted in Lindner, "New Realism," 33.
[381] Kelly and Leland, "Oil Actually," 81.
[382] Peter Rutland, "US Energy Policy and the former Soviet Union: Parallel Tracks," in *Russian Energy Power and Foreign Relations,* ed. Perovic, Orttung and Wenger, quoted in Perovic, "Introduction," 16.

however, critics point out that U.S. interests are not at stake because this issue concerns European energy security and therefore, Europeans should take front and center in handling Eurasian energy supply issues, with the United States playing secondary role.[383] However, Martin Walker points out that the old Europe of NATO founding member states proved to be accommodating to Russian pretensions to reassert its role as a great power by using oil and gas as geopolitical assets. The new Europe of new NATO and EU members and former members of the Warsaw Pact remained highly suspicious of Russia's intentions and are wary of Russia using energy as a foreign policy instrument. They are also highly suspicious of EU institutions and their ability and willingness to protect smaller countries' interests.[384]

Central Asia has become a more dynamic region with new tensions and geopolitical opportunities rising due to growing number of investors from the EU, the United States and China. However, Russia still has an upper hand in Central Asia due to energy export networks being mostly turned towards Russia. Kazakhstan and Turkmenistan depend on Russia's pipeline network for access to lucrative European markets. Azerbaijan has been the most successful Caspian country in breaking away from Russian control. The most successful infrastructure project in the region, supported by the West, is the *BTC* oil pipeline transporting Azeri oil. Russia sees possible diversion of Central Asian energy away from pipelines passing through Russia as a big challenge to its hegemony in the region. The EU and the United States, with varying degrees of commitment, have been pursuing projects that would divert Caspian energy away from Russia. In Central Asia and Caspian region, U.S. policy has been to undermine Russia's importance as energy export hub and create new export corridor via Turkey, by supporting and forwarding several pipeline projects which are outlined in Chapter 3 and Chapter 5. Russia, on the other hand, has been engaging in energy diplomacy, courting leaders and national energy companies in Central Asia in order to keep its position as a transit country and buyer of Central Asian energy resources.[385]

Russia also gives great importance to its good relations with Iran. By supporting internationally unpopular Iranian regime, Russia is keeping Iranian energy resources away from Europe. Flow of Iranian energy to Europe would undermine Russian interests in Europe and Central Asia. If Iran was to start exporting oil and gas to Europe, importance of Russia for European energy security would greatly be diminished. This would limit Russia's foreign policy options. It would

[383] Woehrel, *Russian Energy Policy*, 15.
[384] Walker, "Russia v. Europe," 1.
[385] Julia Nanay, "Russia's Role in the Eurasian Energy Market: Seeking Control in the Face of Growing Challenges," in *Russian Energy Power and Foreign Relations*, ed. Perovic, Orttung and Wenger, quoted in Perovic, "Introduction," 14-15.

also mean that Russia would not be as important for the flow of Eurasian energy. Therefore, it is in the interest of Russia for tensions between Iran and the West to continue, and to have Iran in a position of limited energy flow so that there would be fewer options to divert Central Asian supplies away from Russian control. Eurasian energy flow has been described as Russia's last real weapon.[386]

Perovic argues that Russia's political elite considers energy to be an engine of economic growth and restoration of Russia's great power status. Russia is using energy to punish, fight and limit pro-Western orientation in what it considers its sphere of influence, in countries that are mostly or completely dependent on Russian oil and gas supplies. Many have claimed, but Russia is not an energy superpower. When compared to Western economies, Russia is still relatively weak power given that its GDP per capita is only quarter of that of the U.S. in real terms. However, Russia is still Eurasia's leading energy power.[387] Combined with its seat on the UN Security Council and its nuclear arsenal, Russia becomes key regional player with global ambitions. Russia is using its energy potential to enter international markets while certain world powers are watching Russia's expansion and ambitions with concern. Russia's ambitions are mostly felt by its neighbors in the form of cut-offs or threats of cut-off of gas deliveries, in order to have them agree to higher prices or to punish them for their geopolitical orientation. Supply cut to Ukraine in 2006 reminded many countries just how dependent they are on Russian energy. This episode damaged Russia's reputation as a reliable supplier of energy to Europe and loud calls were made for Europe to unite and diversify away from Russia. Russia's role as reliable supplier was questioned further when Kremlin started to re-nationalize oil sector and take control of all major oil and gas fields. During Putin's second term as President, large number of production sharing agreements and joint ventures with foreign companies were called-off, licenses to private Russian companies were withdrawn and even cases of obvious expropriations were seen.[388]

While Russia is projecting its power internationally by using its status as a major energy supplier and attempting to consolidate its great power status regionally, the EU is often plagued by its ambiguous status given the fact that it is not a state in the conventional Realist sense nor is it a successful federation. Nevertheless, the permanent members of the UN Security Council – the U.S., Russia, and China have established bilateral relations with the EU and the EU engages with those powers in various crisis negotiations of their mutual concern.[389] Two members of the

[386] Blank, "Resetting the Reset Button," 2.
[387] Perovic, "Introduction," 9.
[388] Ibid., 8-9.
[389] David M. McCourt and Andrew Glencross, *The Power Politics of European Integration: The EU as a Great Power Manager*, 24, http://www.sisp.it/files/papers/2013/andrew-glencross-and-david-mccourt-1748.pdf.

EU are remaining permanent members of the UN Security Council – the UK and France. Including Germany, those European countries are the driving force behind the Union. The EU has moved into the sphere of great power politics with Common Foreign and Security Policy (CFSP) and its integral part Common Security and Defense Policy (CSDP) which clearly demonstrated that the EU wants to do what great powers do, which is to have a say in the management of international affairs. With CSDP, which moved the Union into the foreign, security and defense sphere,[390] the EU showed readiness to act as a great power even if it is not yet fully equipped institutionally given the frequent conflict of interest between its Member States and EU institutions. Nevertheless, EU Members have committed their countries to the CFSP. The aim of CSDP specifically, is "to strengthen the EU's external ability to act through the development of civilian and military capabilities in conflict prevention and crisis management."[391] Attraction of liberal democracy has provided the EU with significant foreign policy tool.[392] Besides spreading its influence by engaging in conflict prevention, peace building, mediation, and crisis management regionally and internationally, the EU is also able to exercise coercion in the form of designed diplomatic and economic sanctions, punishing those countries disrespecting the rule of law, human rights, and general democratic principles.[393] The most important instrument at the EU's disposal to spread its influence regionally is enlargement. New members or prospective new members need to agree on extensive list of conditions to join the Union, constraining their sovereignty, and effectively taking them outside of Russia's sphere of influence. With 28 members and many other countries in the east and south of Europe wishing to join the Union, EU membership card is EU's important foreign policy instrument in projecting its power regionally.[394] It is also driving the conflict of power aspirations between the EU and Russia. If not being a state and a great power in a traditional sense, the EU has been exercising regional primacy in many respects,[395] leading Moscow to feel that it must protect itself from EU's influence, which has taken a form of foreign policy assertiveness.

5.3. POLITICS OF GAS PIPELINES

Energy is a lucrative business for those who sell it, where having dependable energy supplier is

[390] Ibid., 10.
[391] "Common Foreign and Security Policy (CFSP) of the European Union," European External Action Service, http://eeas.europa.eu/cfsp/index_en.htm.
[392] Jan Techau, "How Ukraine Destroyed the Myth of Russia's Great Power," *carnegieeurope.eu*, 25 February 2014, http://carnegieeurope.eu/strategiceurope/?fa=54639.
[393] Ibid.
[394] McCourt and Glencross, *The Power Politics of European Integration*, 23.
[395] Ibid., 24.

a matter of national security. Natural gas is quickly gaining geopolitical importance. It is a fuel that travels a great distance in pipelines to be used in many economic sectors. It is preferred to some other fossil fuels due to lower environmental impact, and it has been increasingly used for electrical power generation. Over the next three decades, world gas consumption is projected to at least double.[396] About three quarters of the global proven gas reserves are located in the areas of the former Soviet Union and the Middle East.[397] Gas pipelines and electricity networks contribute to the formation of a unique kind of international relations because they physically connect producers and consumers.[398] Energy has been described as ambiguous good because it can be considered as tradable commercial good, as a service (for transportation), and as a strategic good that can be used as foreign policy tool as demonstrated by oil crises in 1970s[399] and more recently by Russia in the form of *Nord Stream* gas pipeline project. This pipeline had a dual purpose: to sell directly more gas to its high-valued and high-paying customer – Germany; and to punish those transit states that were having disputes with Russia.

Nord Stream pipeline is a joint venture between Russian, German and Dutch companies. 51% is in Gazprom's ownership, Germany's companies *Wintershall* and *E.ON* own 20% each, and Dutch *Gasunie* has 9% stake.[400] The pipeline runs for 1200 kilometers along the Baltic seafloor and connects Northwest Russia with North Germany.[401] When *Nord Stream* project was announced in 2005, it was criticized by Poland, Ukraine and the Baltic States most loudly since they would be bypassed and they would lose their leverage over Russia due to an alternative pipeline. Neighboring countries were uneasy because they felt that their national security interests were compromised. Overland pipeline with similar capacity would have cost much less.[402] Germany and Russia were prepared to pay as much as it cost in order to avoid any transit country. They showed their distrust on reliability of transit states even before 2006 gas crisis when Ukraine consumed gas which was meant for European markets. President Vladimir Putin

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[396] Victor, "Natural Gas and Geopolitics," 91.
[397] USGS, *USGS World Petroleum Assessment 2000* (Washington, DC: U.S. Department of the Interior, USGS, 2000), http://pubs.usgs.gov/fs/fs-062-03/FS-062-03.pdf; BP, *BP Statistical Review of World Energy 2007* (London: BP, 2007), http://www.bp.com/content/dam/bp-country/en_ru/documents/publications_PDF_eng/Statistical_review_2007.pdf, quoted in Victor, "Natural Gas and Geopolitics," 91.
[398] Bouzarovski, "Post-Socialist Energy Reforms," 176.
[399] Kirsten Westphal, "Energy Policy between Multilateral Governance and Geopolitics: Whither Europe?," *International Politics and Society* 4 (2006): 58, http://www.fes.de/ipg/arc_06_set/set_04_06e.htm, quoted in Bouzarovski, "Post-Socialist Energy Reforms," 176.
[400] "Nord Stream Troubles," *Emerging Europe Oil and Gas Insight*, July 2007, quoted in Bouzarovski, "Post-Socialist Energy Reforms," 176.
[401] "Jockeying for Position and Power in 2007," *Platts Energy in East Europe*, 5 January 2007, quoted in Bouzarovski, "Post-Socialist Energy Reforms," 176.
[402] Bouzarovski, "Post-Socialist Energy Reforms," 176.

stated that: "Russia should reduce its dependence on transit countries, such as neighboring Belarus and Ukraine, to help guarantee security of energy supplies to Europe."[403] George W. Bush Administration officials criticized both *Nord Stream* and *South Stream* projects saying that it only increased Europe's dependence on Russia.[404]

Nord Stream increased natural gas supply security of Western Europe and undermined supply security of Eastern and Central parts of Europe through which most pipelines from Russia pass through. Germany's support for *Nord Stream* was even more pronounced after Russia's energy crises with Ukraine in 2006 and Belarus in 2007 which led to disruptions of gas flow to Europe. *Nord Stream* would provide Germany and West Europe with dependable gas supply directly from Russia without Eastern European transit states involved. That politics and energy projects go hand in hand was demonstrated by the former German chancellor Gerhard Schröder who after leaving office became the chairman of the *Nord Stream* consortium. He and Vladimir Putin are also said to have become very good friends. Warsaw's thoughts on *Nord Stream* project were expressed by Poland's then defense minister Radek Sikorski who called it a modern version of the Molotov-Ribbentrop pact of 1939 when Nazi Germany and Soviet Union agreed to divide Poland between them.[405]

In 2003, German politicians pushed for merger of *E.ON* and *Ruhrgas*, against anti-cartel agency's wishes, in order to have company which would be powerful enough to deal with Gazprom's increasing strength. Germany and Russia have been building good relations over several decades. There was Cold War era détente, Kohl-Gorbachev deal over reunification of Germany, and most recently, Schröder-Putin deal to construct the *Nord Stream* pipeline. The *Nord Stream* project exposed geopolitical nature of Germany-Russia relations. It would have been cheaper to upgrade *Brotherhood* gas pipeline which passes through Ukraine and reaches Germany as well, or even to build new overland gas pipeline. Brotherhood pipeline's maximum capacity is 175 bcm but it transports only 115 bcm of gas per year. Talks between Russia, Ukraine and Germany to expand this pipeline failed in 2002 and Russia-Ukraine gas crisis in 2006 made expansion even less probable.[406] Russia has however revisited plans to construct *Yamal–Europe-2* pipeline that would pass through Belarus, Poland, Slovakia, and Hungary. This plan was dropped after energy disputes with Belarus, Ukraine and the Baltic States, but

[403] Neil Buckley and George Parker, "Rusia to Cut Use of Energy Transit Countires," *Financial Times*, 21 January 2007, http://www.ft.com/intl/cms/s/0/5808145a-a987-11db-9185-0000779e2340.html#axzz3LG8t5AXa, quoted in Bouzarovski, "Post-Socialist Energy Reforms," 176.
[404] Woehrel, *Russian Energy Policy*, 16-17.
[405] Walker, "Russia v. Europe," 3.
[406] Westphal, "Germany and the EU-Russia Energy Dialogue," 93-100, 107-111, quoted in Aalto, "European Perspectives," 170.

was proposed again in April 2013 by Vladimir Putin.[407]

Nord Stream was considered priority project for Germany because it provided direct link to Russian gas without possibility of some transit state disrupting gas flows.[408] Gazprom and *E.ON Ruhrgas* signed memorandum of understanding in 2004 and 2005. They also agreed to swap assets. *E.ON Ruhrgas* was promised 24.5% stake in Yuzhno Russkoye gas field in Western Siberia. In return, Gazprom received assets in three Hungarian companies controlled by *Ruhrgas*. Germany's *BASF*'s subsidiary *Wintershall* holds another 24.5% stake in Yuzhno Russkoye.[409] Those critical of Russia consider Germany's close energy ties with Russia to be a potential threat to Germany.[410] Nevertheless, Germany-Russia energy relations may be further improved when Russia decides to develop its huge untapped renewable energy potential, with Germany giving a helping hand as an expert. Germany holds global leadership in renewable energy technology. 6% of energy and 10% of electricity consumption is generated by renewables.[411] Worldwide, half of the windmills and third of the solar cells are produced by Germany. Germany also holds one-third of the hydropower installations market.[412]

Since the end of the Cold War, Russia had been dictating prices for gas that it was buying from Central Asian countries. This changed in April 2006 when Presidents of China and Turkmenistan signed framework agreement on oil and gas cooperation. Under this deal, they agreed on the construction of gas pipeline which will annually supply 30 bcm of Turkmen gas to China for the next 30 years, starting in 2009. This was an end of the Russia's gas pipeline monopoly in Central Asia and a setback for Russian energy policy. Over the years Gazprom managed to resist price increase from $65/tcm to $100/tcm, however, in September 2006 it had to agree to new prices. Under the deal, Russia agreed to buy 50 bcm of gas per year until 2009. Russia needed Turkmen gas in order to meet its supply commitments in Europe. New prices were agreed in a manner that allowed relations between Russia and Turkmenistan to remain solid and friendly. With Russia now paying higher prices for Turkmen gas, Turkmenistan's

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[407] "Yamal–Europe-2," Gazprom, http://www.gazprom.com/about/production/projects/pipelines/yamal-evropa-2/.
[408] Aalto, "European Perspectives," 170.
[409] Westphal, "Germany and the EU-Russia Energy Dialogue," 102-105, quoted in Aalto, "European Perspectives," 171.
[410] Robert L. Larsson, *Russia's Energy Policy: Security Dimensions and Russia's Reliability as an Energy Supplier* (Stockholm: FOI–Swedish Defence Research Agency, 2006), 192, http://storage.globalcitizen.net/data/topic/knowledge/uploads/20110731213514705.pdf, quoted in Aalto, "European Perspectives," 171.
[411] "Overview: Energy for the Future: Renewable Sources of Energy," European Commission, http://ec.europa.eu/energy/index_en.htm, quoted in Aalto, "European Perspectives," 171.
[412] "Report: German Companies World-Leaders in Renewable Energy," *Deutsche Welle*, 19 February 2007, www.dw-world.de/dw/article/0,2144,2355370,00.html, quoted in Aalto, "European Perspectives," 171.

President Saparmurat Niyazov also agreed to give Russia access to Yolotan gas fields and to quadruple capacity of the gas pipeline exporting gas to Russia. In December 2006, President Niyazov died. On 11 February 2007, new President, Gurbanguly Berdymukhammedov, was elected. He continued to follow energy policy of his predecessor. However, Turkmens were still not satisfied with prices Russia was paying for their gas. Gazprom was selling Turkmen gas to Ukraine for $100/tcm while price for the EU was $250/tcm. Western countries were hopeful that new energy deals on field explorations and gas pipelines could be reached with Turkmenistan now that new President came to power. Russians acted quickly to prevent this and on 12 May 2007, Presidents of Russia, Turkmenistan and Kazakhstan met in Turkmen Caspian port of Turkmenbashi. They agreed to construct new pipeline bordering Caspian Sea, running from Turkmenistan through Kazakhstan and connecting with Russian pipelines going to Europe. Initially pipeline was delivering 10 bcm of gas per year to Russia. Starting in 2012, 90 bcm of gas will be delivered to Russia annually. This was a major geopolitical victory for Russia. In December, Russia, Kazakhstan and Turkmenistan signed an official agreement for the construction of new gas pipeline along the Caspian Sea. Russia also agreed to pay new price of $130/tcm in the first semester of 2008, and $150 in the second semester. This increase in prices was mostly felt by Ukraine because on 4 December 2007, they had to agree to new Gazprom price of $179/tcm for gas.[413]

During 2008 Russia was actively consolidating the *South Stream* project. In January 2008, Putin reached an agreement with Bulgarian president under which Russia and Bulgaria would each have 50% stake in section of the pipeline passing through Bulgaria. Bulgaria wanted majority control; however, Russia had already monopolized Bulgaria's energy market so Bulgaria was left without leverage to back up its pretensions. Four days later, an agreement was reached with Serbia as well under which Gazprom gained control over Serbia's state company *NIS* – Serbia's oil and gas monopoly. In return, Serbia was promised investments to modernize its energy infrastructure. Gazprom also promised that Serbia will become energy hub for Russian energy.[414] Hungary followed the example set by Bulgaria and Serbia and gave its support to the *South Stream* project.[415]

By controlling gas pipelines in Central Asia, Russia has effectively undermined the U.S. and EU-backed *Nabucco* pipeline project. Russia sought to buy gas from Azerbaijan and

[413] Marquina, "The Southeast-Southwest European Energy Corridor," 61-62, 64.
[414] Ibid., 64.
[415] Judy Dempsey, "Hungary Chooses Gazprom over EU," *The New York Times*, 12 March 2007, http://www.nytimes.com/2007/03/12/world/europe/12iht-hungary.4885468.html?_r=0; "Hungary to Join South Stream Gas Pipeline Project," *RIA Novosti*, 7 December 2007, quoted in Marquina, "The Southeast-Southwest European Energy Corridor," 64.

Turkmenistan in an effort to remove the possibility of this gas filling *Nabucco* pipeline. These actions, combined with China's new Central Asian energy contracts and strong opposition from Iran and Russia to trans-Caspian pipeline, brought results and *Nabucco* pipeline project would not go forward because only Azerbaijan seems to be able to fill it with gas.[416] To undermine *Nabucco*, Russia has also come up with projects along the similar route and it engaged with individual EU countries in order to gain their support. This tactic has been successful in canceling the *Nabucco* project because Russia got full support from Bulgaria, Serbia, Hungary and Italy. Those countries' full support was needed for *Nabucco* to be realized, instead, they backed Russia's *South Stream* project.[417] *OMV*, the Austrian state-controlled energy company, agreed to sell 50% stake in Baumgarten gas storage and distribution center to Russians. This was another move to undermine *Nabucco* pipeline as Baumgarten was planned terminus of the project. Russia put itself in a position to directly block *Nabucco* project.[418] Another move by Russia that effectively undermined *Nabucco* project happened in March 2009 when Russian energy firm *Surgutnefegas* bought from Austrian firm *OMV* a large stake in Hungarian energy giant *MOL*. *MOL* was a key participant in the *Nabucco* project.[419]

EU has invested more than a decade of time, a lot of money and effort into never realized great European hope – the *Nabucco* pipeline project. It was a chance for Europe to lessen its dependence on Russian gas by linking Europe with gas-rich Caspian countries without using Russian pipelines.[420] From the start, *Nabucco* has been plagued by the lack of political will and finances. It has been left with no guaranteed gas supplies and Germany's *RWE*, the second largest investor, has withdrawn its support.[421] Meanwhile, Russia has opened *Nord Stream* for business.

For decades, the United States has been urging Europe to reduce their energy dependence on Russian energy, especially gas. It has been active in supporting pipeline projects to bring energy from Central Asia and Azerbaijan directly to Europe. The United States has supported the *BTC*

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[416] Nikolay Kozhanov, "Russian Energy Strategy Makes Partners out of Rivals," *WashingtonInstitute.org*, 16 April 2012, http://www.washingtoninstitute.org/policy-analysis/view/russian-energy-strategy-makes-partners-of-rivals.
[417] Woehrel, *Russian Energy Policy*, 18.
[418] Vladimir Socor, "Austria's OMV Deal with Gazprom Threatens Nabucco Project," *Eurasia Daily Monitor* 4, no. 215, 19 November 2007, http://www.jamestown.org/programs/edm/single/?tx_ttnews%5Btt_news%5D=33177&tx_ttnews%5BbackPid%5D=171&no_cache=1#.VHzeNtKsVic, quoted in Woehrel, *Russian Energy Policy*, 18.
[419] Woehrel, *Russian Energy policy*, 18.
[420] Peter C. Glover, "Europe's Other Power Crisis: Energy," *TheCommentator.com*, 18 May 2012, http://www.thecommentator.com/article/1223/europe_s_other_power_crisis_energy.
[421] Polina Chernitsa and Alexandra Dibizheva, "Nabucco–a pipeline to nowhere?," *The Voice of Russia*, 16 May 2012, http://sputniknews.com/voiceofrussia//2012_05_16/74920749/, quoted in Glover, "Europe's Other Power Crisis."

oil pipeline which carries 1 million barrels per day of Azeri oil to Turkish port of Ceyhan. The United States also supported South Caucasus Gas Pipeline project, filled from Azerbaijan's Shah Deniz gas field,[422] supplying gas to Georgia and Turkey, with plans to connect it to other proposed pipelines which would deliver gas to the EU.[423] Less successfully, the United States also supported *Nabucco* and Turkey-Greece-Italy gas pipelines.

Russia has a strong hold on oil-rich Kazakhstan and gas-rich Turkmenistan due to the fact that Russia has control over pipelines transporting most of their oil and gas exports. This is the reason the EU and the United States are losing geopolitical struggle for Central Asian resources. With China entering the struggle, the EU and the United States seem to have completely lost this region. Central Asian countries are also looking to diversify supply routes. However, this does not mean that energy will flow to the west, but rather, they are developing projects for energy to flow east, mostly to China. Pipeline from Turkmenistan to China opened in 2009, delivering 30 bcm of gas per year. China is involved in the development of one of Turkmenistan's biggest gas fields – South Yoloten. Turkmenistan is also looking to expand its gas pipeline capacity to Iran.[424] This may be strongly supported by Russia since Russia is also keeping close relations with Iran and helping it realize energy projects, with suspected agenda of keeping Iranian energy resources away from Europe in case that Europe lifts sanctions it put on Iran, in which case Iranian energy would be welcome to Europe. This would make Iran a direct competitor to Russia for lucrative European energy market. Because of this, Russia is considering becoming involved in construction of gas pipeline linking Iran and Pakistan. Many commentators believe that Russia will continue with this energy strategy of close cooperation with its energy rivals in order to limit European energy diversification prospects.[425]

5.3.1. Natural Gas Crises

Ukraine has small reserves of oil and gas on its own territory but it is mostly dependent on Russian energy deliveries.[426] Ukraine depends on Russian companies to deliver to it Russian gas and oil as well as to deliver supplies from Central Asia, especially gas from Turkmenistan via pipelines controlled by Russia. Gas takes up 50% of energy consumed in Ukraine. In 2006, 66%

[422] Woehrel, *Russian Energy Policy*, 15.
[423] "South Caucasus Pipeline," BP, http://www.bp.com/en_az/caspian/operationsprojects/pipelines/SCP.html.
[424] Woehrel, *Russian Energy Policy*, 18-19.
[425] Kozhanov, "Russian Energy Strategy."
[426] Woehrel, *Russian Energy Policy*, 7-10.

of gas and 78% of oil consumed in Ukraine came from Russia.[427] Most homes in Ukraine are heated by natural gas and natural gas is used in energy inefficient heavy industry which is a major export contributor. Ukraine has been leveraging its position as a transit country of Russian gas to the EU in order not to fall under Russian influence. This is the reason why Ukraine owns sections of pipelines crossing its territory and it also has large gas storage facilities. It receives transit fees from Russia which are partly paid in hard currency and partly in gas consumed. Russia has attempted rather unsuccessfully to infiltrate Ukrainian energy market given that up until recently, 80% of Russian gas on its way to the EU was passing through Ukraine. There were attempts to take ownership of Ukrainian natural gas pipelines, storage facilities and gas distribution network. In February 2007, Russian President Vladimir Putin and Ukrainian Prime Minister Viktor Yanukovych announced that Ukraine and Russia will take joint ownership of Ukraine's natural gas assets. In exchange, Ukraine would receive stake in some of Russia's gas fields. Such announcement was followed by the Ukrainian Parliament speedily outlawing such plans. Russia also tried to exploit the fact that Ukraine is facing problems of ageing energy infrastructure. In exchange for Russia's help in upgrading its pipeline networks, Russia is seeking to secure Gazprom ownership of Ukraine's pipeline system.

5.3.1.1. 2006 Russia-Ukraine Pricing Dispute

Security of natural gas supply in the EU became a topic of heated discussions after Gazprom cut-off gas supplies to Ukraine from 31 December 2005 to 2 January 2006, following the Russia-Ukraine pricing dispute. Dispute occurred over disagreements regarding transit fees and Gazprom's demands that Ukraine pay market price for Russian gas instead of price rates set during the Soviet era.[428] During the gas cut-off, Ukraine consumed gas intended for the EU markets which was only transiting through Ukraine. This dispute was a point of serious concern in Europe since at that time approximately 80% of Russian gas on its way to Europe was passing through Ukraine. Several EU Member States were affected by this since they were also faced with several days of decreased gas supply which in winter months was much needed.[429]

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[427] EIA, *Country Brief: Ukraine* (Washington, DC: DOE, EIA, 2007); *Country Brief: Russia* (Washington, DC: DOE, EIA, 2008), both from the EIA website http://www.eia.doe.gov, quoted in Woehrel, *Russian Energy Policy*, 7.
[428] Aalto, "The EU-Russia Energy Dialogue," 38.
[429] Stern, "The New Security Environment," 56, 59-60.

Hungary reported 40% reduced supply, Poland 38.5%, Croatia, Slovakia and France 30%. Germany and Italy also reported decreased supply volumes.[430]

Gas crisis of January 2006 could have been foreseen in 2005 when Viktor Yushchenko became the president of Ukraine. Russia was supporting his opponent Viktor Yanukovych. Yushchenko was a pro-Western leader who had plans for Ukraine to conduct reforms and join NATO and the EU in the future. Soon after he took office, Gazprom demanded higher price to be paid for its gas deliveries. By December 2005, Gazprom was asking Ukraine to pay market price of $230 per thousand cubic meters (tcm) instead of previous price of $50/tcm. Ukraine rejected Gazprom's proposal and on 31 December 2005, Gazprom cut-off gas supplies to Ukraine. Ukraine then started using Russian gas intended for European markets which was transiting through Ukraine. Europeans protested at this turn of events and on 2 January, Russia started delivering gas to Ukraine again. On 4 January, Russia and Ukraine reached an agreement. It was agreed that Ukraine would purchase gas through intermediary firm *RosUkrEnergy*. This firm would purchase gas from Central Asia which was priced below marked level. Added to Central Asian gas would be Russian gas purchased at market level. Ukraine would pay an average price of $95/tcm. Ukraine also managed to negotiate an agreement with Russia on higher transit fees for Russian gas, paid exclusively in cash.[431]

First few months of 2006 continued to be tense following the gas cut-off. February and March were characterized by cold weather throughout most of Europe. Lowest temperatures in more than 60 years were recorded in Moscow with temperatures staying below 30 degrees Celsius for more than a week. Central and Eastern European countries were in deep minus too. Domestic demand put strain on Russian gas and power networks; however, they continued to execute their domestic and international supply commitments. Due to low temperatures, Ukraine again diverted some of the gas for European markets for its own domestic use which meant that Gazprom did not meet very high demand by some European countries receiving gas through pipelines passing through Ukraine. Poland, Italy, Hungary and Austria reported many days in which gas deliveries were 10 to 35 percent lower than intended. In this situation Russia was again accused of exerting political pressure on Ukraine since Ukraine was eager to move away from Russian sphere of influence and turn to NATO and EU.[432] It seemed that Ukraine got a free pass from the EU for taking gas that did not belong to it. Those events in the first few

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[430] Aalto, "The EU-Russia Energy Dialogue," 38.
[431] Woehrel, *Russian Energy Policy*, 7-10.
[432] IEA, *Optimising Russian Natural Gas: Reform and Climate Policy* (Paris: OECD/IEA, 2006), 35, http://www.iea.org/publications/freepublications/publication/russiangas2006.pdf, quoted in Stern, "The New Security Environment," 60.

months of 2006 cemented a narration regarding Russia for years to come. Narration was that Russia presented a potential threat that needs to be addressed properly. The EU accused Russia of using energy as a foreign policy tool in order to exert political pressure on other countries.[433]

5.3.1.2. 2007 Russia-Belarus Pricing Dispute

Another country facing energy disputes with Russia is Belarus which is an important transit country for Russian energy deliveries to Europe. In January 2007, Russia increased gas prices to Belarus.[434] In response, Belarus put tariff in place for Russian oil passing through Belarus which Russia refused to pay. Belarus then started embezzling Russian oil on its way to Europe. In response, Russia cut-off gas supplies to Belarus. Belarus was firm in its demands for three days and then mostly gave in to Russian demands. Worth noting is that shortly before this episode, Russia acquired 50% stake in Belarus' gas pipelines, therefore, Belarus' leverage over Russia was substantially diminished. EU displayed more united stand in condemning this crisis than in the case of Ukraine, and even Angela Merkel was on the record saying that Russia's action was unacceptable.

Gas crises in Ukraine and Belarus were brought about by the general Russian policy since 2005 to increase energy prices to Commonwealth of Independent States (CIS) who for decades enjoyed consumption of cheap energy coming from their former patron – Russia. There was a wide gap between prices paid by the EU and CIS countries and eventually Russia decided to start closing that gap. Russian actions have been discussed in the EU as being politically motivated but in Russia they have been discussed as planned policy to increase gas prices to CIS countries and to increase prices domestically. Russian way of explaining its policies is in part supported by some European commentators such as Rainer Lindner from the German Institute for International and Security Affairs in Berlin, who stated the following:

> The new price-policy arrangements are an indication of Moscow's decision to construct relations to the states in the post-soviet region on non-ideological market principles. The Kremlin's and Russian energy industry's priority is to get access to the network of distribution in all countries which are transporting Russian gas in transit, as well as pure maximization of profits. That implies a deliberate turn away from the traditional, geopolitical carrot-and-stick policy, which in the eyes of Russian policy-makers does not correspond to Russia's interests.[435]

[433] Stern, "The New Security Environment," 59-60.
[434] Youngs, "Russia," 85-86.
[435] Lindner, "New Realism," 35.

5.3.1.3. 2009 Russia-Ukraine Pricing Dispute

In March 2008, Gazprom again reduced gas deliveries to Ukraine, this time by 60% due to another pricing dispute.[436] By threatening to interrupt gas supplies intended for the EU, Ukraine and Russia agreed on new price of $179.5/tcm for 2008. In 2007 Ukraine was paying $130/tcm which was still below $315/tcm paid by the EU. This was followed by another gas crisis in January 2009, in the middle of a very cold winter, after another gas pricing dispute between Gazprom and Ukraine's *Naftohaz*.[437] During this crisis, Gazprom cut-off all gas supplies to Ukraine, including gas that was only transiting to other European markets. Crisis started on 1st January 2009 when Gazprom halted gas deliveries to Ukraine, with explanation that new prices for 2009 had not been agreed to and that debts to Gazprom had not been paid.[438] Gazprom continued to send gas intended for other European markets. Like it did in 2006, Ukraine diverted some of that gas for its own use. On 6 January, Russia halted all gas deliveries to Europe which were passing through Ukraine. One part of Europe was not hit hard by the cut-off, including Ukraine, because they have large underground storage facilities. Some parts of Europe without large storage facilities, like the Balkans, were hit hard. Many Central and Eastern European states were badly affected and governments were warning consumers to cut back on gas they use.[439] For those countries alternatives were hard to find. In some countries gas supply to residential and industrial consumers and to public buildings had to be stopped. Romania and Slovakia were affected by the crisis to such a degree that they declared state of national emergency.[440] Bosnia and Bulgaria experienced rather severe difficulties as well. States in the Western Europe had means to fall back on alternative routes and supply options so they avoided being greatly affected by the crisis. Without common energy policy, the EU demonstrated rather effectively that it cannot guarantee energy supply security to its member states. Without political consensus and institutional framework these crises can happen time and time again. Europeans complained; however, general consensus within the EU institutions was that it was a commercial dispute between Russia and Ukraine and they should deal with it

[436] Ibid., 34.
[437] Bouzarovski, "Post-Socialist Energy Reforms," 167.
[438] Woehrel, *Russian Energy Policy*, 9.
[439] Bouzarovski, "Post-Socialist Energy Reforms," 167-168.
[440] "Europe Homes Freeze Amid Gas Row," *BBC News*, 9 January 2009, http://news.bbc.co.uk/1/hi/world/europe/7819429.stm; "Gas Crisis Gives Slovakia Excuse to Restart Nuclear Unit," *Euractiv.com*, 12 January 2009, http://www.euractiv.com/energy/gas-crisis-gives-slovakia-excuse-news-221021, quoted in Bouzarovski, "Post-Socialist Energy Reforms," 167-168.

bilaterally. On 18 January, Ukraine and Russia reached an agreement after several failed attempts, and on 20 January, gas deliveries to Europe resumed.[441]

In July 2009, the Commission secured an agreement on Ukraine's behalf, worth more than $1 billion, under which European Bank for Reconstruction and Development and the World Bank agreed to provide loans to Ukraine, for country to upgrade its gas pipelines and storage facilities.[442] In exchange, Commission demanded greater transparency in Ukrainian gas sector. When this deal on upgrade of Ukraine's gas sector was announced in March 2009, Russian Prime Minister Vladimir Putin immediately criticized it as being unprofessional. Russian officials' belief was that any deal concerning Ukrainian pipeline network should include Russia because it is thought that the EU involvement would create additional difficulties in Gazprom's pretensions to take control of Ukraine's gas pipelines and domestic gas distribution network. Ukraine's defiance in 2006 and 2009 resulted in Russia opening up new channels to deliver gas to the EU in order to bypass Ukrainian transport system and lessen its leverage over Russia. *Nord Stream* pipeline passes through Baltic Sea, connecting Germany directly to Russia. *South Stream* was supposed to pass through Balkans and on to Western Europe. This situation led Steven Woehrel to rightly predict that "Russia could feel it would have a freer hand to put greater pressure on Ukraine on other issues."[443]

Russia's disputes with Belarus and Ukraine were well publicized, starting with 2005-2006 gas crisis. However, price disputes first began after disintegration of the Soviet Union.[444] Belarus and Ukraine began accumulating debt since it was hard to convince their citizens to pay for energy they consumed after decades of leisurely consuming very cheap Russian gas during the Soviet era. Their economies were also built without any consideration for energy efficiency. After the break-up of the Soviet Union and infiltration of the capitalist system, Belarus and Ukraine had to pay closer to capitalist than socialist prices for energy they consumed, however, they could not afford it. This led to their debt to Russia increasing annually. Russia began to periodically cut-off gas supplies to Ukraine due to nonpayment, starting in 1992-1993 period. Under persistent Russian pressure, Belarus agreed to sell state company *Beltransgas* to

[441] Woehrel, *Russian Energy Policy*, 9.
[442] Ibid., 10.
[443] Ibid.
[444] Closson, "Russia's Key Customer," 93.

Gazprom in a deal that also included pipeline infrastructure. So far Ukraine has been successful in fending off similar pressure.[445]

Gas crises were particularly felt by Poland who joined the EU in 2004, with publicly professed expectations that the Union will partake in some of its security concerns.[446] It turned out that Poland was being left out of major energy projects connecting the EU and Russia. With *Nord Stream* and *South Stream* pipelines bypassing Poland, Ukraine and Belarus altogether, Poland was very vocal in its disapproval. Poland voluntarily gave up close bilateral ties with Russia with the hope that by joining the EU such bilateral ties would not be needed. In retaliation, Poland blocked the progress on the new EU-Russia treaty, replacing Partnership and Cooperation Agreement (PCA) of the 1990s which was supposed to be discussed during the EU-Russia summit in Helsinki in November 2006. Poland insisted that Russia must ratify the ECT which would regulate energy relations in the wider European area. In response, Russia cut meat imports from the EU, including meat from Poland which is an important component of Poland's export business.

5.3.1.4. Energy Disputes between Russia and the Baltic States

Baltic States of Lithuania, Latvia and Estonia are all EU and NATO members. Outside of those organizations, their relations with Russia are often strained.[447] Approximately 90% of their oil and 100% of their gas consumption comes from Russia. They started experiencing supply cut-offs in the early 1990s when they were trying to achieve independence from the Soviet Union. They pay world market prices for their energy supplies from Russia. Each of the three Baltic States is battling Russia as it tries to take control over their energy infrastructure. Gazprom already has a large equity stake in the Baltic States' natural gas companies.[448] Russia has developed a habit of cutting-off oil and gas supplies to Baltic States' energy facilities when their takeover efforts fail.

Good example of how Russia is punishing Baltic States for noncompliance has become Mazeikiai oil complex in Lithuania. It includes refinery, maritime terminal and pipeline. It was the largest enterprise in Lithuania, accounting for 10% of national GDP. In 1999, the U.S. firm

[445] Marcin Kaczmarski, "The Influence of Russian Federation on Energy Security in Europe," in *The Future of European Energy Security*, ed. Leszek Jesien (Krakow: Tischner European University, 2006), 155-164, quoted in Closson, "Russia's Key Customer," 93.
[446] Aalto, "The EU-Russia Energy Dialogue," 38-39.
[447] Woehrel, *Russian Energy Policy*, 12.
[448] EIA, *Baltic Sea Regional Fact Sheet* (Washington, DC: DOE, EIA, 2006), http://www.eia.doe.gov, quoted in Woehrel, *Russian Energy Policy*, 12.

Williams International bought a large stake in Mazeikiai oil complex and was granted operating rights. In response, Russian oil firm *Lukoil*, which was supplying oil to Mazeikiai, decreased its oil deliveries making the enterprise unprofitable. In 2002, *Williams* sold its stake to Russian company *Yukos* after going through financial problems. With *Yukos* onboard, Mazeikiai became profitable again. This lasted until Russian government became displeased with *Yukos* business decisions which eventually led *Yukos* to bankruptcy. *Yukos* was looking to sell its stake in Mazeikiai. Polish oil firm *PKN Orlen* bought *Yukos*' stake although Russian state-controlled oil company *Rosneft* wanted to buyout *Yukos*. In July 2006, Russian state-owned oil transport company *Transneft* announced that it is shutting down part of *Druzhba* oil pipeline, which is supplying Mazeikiai complex, for repairs due to oil leak. However, it never re-opened. The explanation given by *Transneft* was that the pipeline has become unprofitable. *Transneft* also declined to deliver oil from Kazakhstan to Lithuania through its pipelines. By all accounts, Russia was looking to have a final say in who owns what in the Baltic States' energy sectors in order to keep control over them. It became apparent that Russia will not shy to use energy supply as a weapon in order to get what it wants, which is the control over Baltic States' energy infrastructure.

Latvia experienced problems with Russia in January 2003 when they engaged in dispute over energy infrastructure.[449] Russian government-controlled oil pipeline company *Transneft* cut-off all oil shipments to Latvian oil terminal at the port of Ventspils, after gradually decreasing shipments starting in late 2002. As was the case with Lithuanian Mazeikiai complex, Ventspils operation was very important for Latvian economy. *Transneft* redirected those shipments to its own *Baltic Pipeline System* and the Russian port of Primorsk. *Transneft* explained situation by claiming that there is no demand for Ventspils operations. However, many are convinced that it was a power play on Russian side because *Transneft* was unsuccessful in its attempts to secure controlling stake in the company *Ventspils Nafta* which operates the oil terminal.[450]

Estonia also experienced problems with energy supply after it removed Soviet war memorial from center of its capital Tallinn.[451] Russia disapproved of this move and to demonstrate it, Russia's railway monopoly halted deliveries of oil products and coal to Estonia on 2 May 2007. Political dispute followed between Estonia and Russia over removal of the statue.

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[449] Woehrel, *Russian Energy Policy*, 12-13.
[450] Keith C. Smith, "Russian Energy Pressure Fails to Unite Europe," *CSIS Euro-Focus* 13, no. 1 (Washington, DC: CSIS, 2007), http://harvard-bssp.org/files/2006/publications/eurofocus_v13n01.pdf, quoted in Woehrel, *Russian Energy Policy*, 13.
[451] Woehrel, *Russian Energy Policy*, 13.

5.3.1.5. Aftermath of the Gas Crises

Gas cut-offs by Russia in 2006 and 2007 triggered a broad debate about the future of energy supply security in Europe. By being intimidating to smaller players like Ukraine and Belarus, Russia became intimidating to Europe as a whole. It can be argued that upon realizing that Europe fears them, Russian leaders took full advantage of the fact and started to act as Europeans perceived them. General perception in Europe is that Russia's energy industry's goal is to take ownership of infrastructure and distribution networks in all countries that take part in transportation and consumption of Russian gas and to control them.[452] This perception seems to be confirmed by Gazprom's attempts to enter the EU's downstream consumer market. Gazprom wants to be involved in the business of gas from beginning to an end – from extraction to bringing it to consumers in distribution markets. Russia is seen as favoring bilateral agreements because in most cases it is more powerful state of the two states that sign an agreement. For many EU States, increased gas dependence is directly correlated to increased insecurity, which is defined as the likelihood that gas exporting countries will cut-off or threaten to cut-off gas supplies for commercial or political reasons.[453]

5.4. THE EU-RUSSIA POLITICAL CONFLICT: REAL OR NOT

5.4.1. EU-Russia Energy Relations after 2006 Gas Crisis

In 2006, the then President of the European Commission, Jose Manuel Barroso, visited Moscow and tried to persuade the Russian President Vladimir Putin to ratify the ECT. It was again pointed out that Russia would enjoy benefits of stable and secure markets and it would have full access to western drilling and deposit maintenance technology. Russian energy companies would be able to expand their business in energy sales and distribution in EU markets and to freely buy and operate refineries and distribution networks. In short, it would enjoy all the benefits of becoming integrated into what the Commission calls "the European economic space." Transit protocol from the ECT would be the main benefit for the EU and a major loss for Russia. The EU States would be allowed full access to invest in Russian energy deposits and pipelines. Putin, however, had different plans which included not giving up control over Russian pipelines. After Barroso's offer was declined, technical discussions were continued between experts in Sochi, Russia, in March 2006. In Sochi, Russians repeated their displeasure

[452] Ibid., 6-7.
[453] Stern, "The New Security Environment," 56.

at their companies not getting access to buy into EU's downstream operations. The UK blocked Gazprom from buying *Centrica* – one of its leading gas distributors. Poland was opposed to Gazprom's wish to buy *PGNiG* – privatized gas distribution group. Russia mostly closed its doors to European investments but insisted in free access to buy into EU's energy distribution systems.[454]

Contrary to European wishes of liberalization of Russia's energy sector, Russia consolidated Gazprom's gas monopoly and successfully tightened control over the oil sector. By 2008, 50% of oil production was under direct state control.[455] Moscow also made it quite clear on several occasions that it has no intention of ever ratifying the ECT which would require Russia to liberalize its oil and gas sectors. The EU was then looking to have some principles from the Treaty to be put into the post-PCA agreement (new agreement meant to replace the PCA as basis for EU-Russia cooperation[456]) in return for free trade agreement with the Union. Moscow showed little interest in this proposition as well since three-quarters of their exports to the EU were raw materials which are not affected by trade rules in any case.[457]

Instead of ECT or the Energy Dialogue, Russia proposed and promoted the vision of EU-Russia energy relations based on reciprocity. For a short period of time, in Europe, there was optimism given that reciprocity implies interdependence and cooperation. However, just like different approaches to energy policy, the EU and Russia have different views on reciprocity. The EU approach to energy policy is rule-based where primacy is given to markets. The Russian approach to energy policy is state-control where primacy is given to state monopolies. For Europeans reciprocity means "mutually agreed legal framework" that promotes investments in and out of Europe. For Russia, reciprocity means swap arrangements for energy assets, meaning that they will open up their energy fields for development and extraction to foreign investors if they get certain energy assets in downstream operations in Europe. The EU would be forced to set aside the underlying principles such as open markets, fair competition and transparency, in order to engage Russia, but Russia refused to endorse those principles since it would mean taking energy sector out of state control.[458] Therefore, building energy relationship based on reciprocity seems impossible. Russian idea of reciprocity seems to be prevailing however, as Russian energy companies continue to find willing participants to buy and swap energy assets in

[454] Walker, "Russia v Europe," 3-4.
[455] Barysch, *Russia, Realism and EU Unity*, 5.
[456] "EU Relations with Russia," European External Action Service, http://eeas.europa.eu/russia/index_en.htm.
[457] Ibid.
[458] Ibid.

downstream European markets. Gazprom has investments in at least 16 EU States.[459] In Italy, Germany and France, Gazprom already has some direct access to gas consumers. Gazprom is also building power plants and storage facilities in some EU Member States.[460]

Responding to EU criticism of not liberalizing their energy market, Russian officials say that it is their sovereign right to protect their oil and gas reserves from foreign influence, just as OPEC countries have done. Termination of *Shell* and *BP* deals was explained by the fact that when those deals were made, Russia was weak, and in new circumstances for Russia, those deals were no longer fair and valid. This view is widely supported in Russia.[461] Alexander Bulygin – CEO of the aluminum giant *Rusal*, wrote in the *Financial Times* on 6 March 2007:

> There is nothing mysterious about the Kremlin's robust defense of national interests. Like any other government, it is simply protecting what it hold important for the country and for its people. It surprises me that anyone questions whether Russia should rightly, proudly, fairly protect its interests. Russian businesses, especially those championing the drive to the international capital markets, must naturally do the same.[462]

Frequent objections coming from Russia regarding EU was that Russia desired cooperation but that it was EU who wanted to dictate terms of this cooperation. Russia's complaint was that the EU was not engaging Russia in strategic partnership that treated Russia as an equal. Russia's accusations can in part be confirmed by EU actions that are sometimes contradictory. The EU was supporting Russia in its efforts to become World Trade Organization (WTO) member, but when Russia increased prices to former Soviet republics, which was one of the conditions for the WTO membership, the EU accused Russia of engaging in power politics.[463] The EU's and Russia's conflicting energy policies are part of the global politicization of energy security where state-control approach espoused by major producers (and some major consumers like China) is conflicting with market-approach imposed by the West.

5.4.2. Global Politicization of Energy Security

EU institutions are promoting an idea of import-export energy business that is market-based, involving international coordination based on international good governance standards and overseen by international institutions. Supplies should be locked into international markets and

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[459] Agata Łoskot-Strachota, *The Russian gas for Europe* (Warsaw: Centre for Eastern Studies, 2006), quoted in Barysch, *Russia, Realism and EU Unity*, 5.
[460] Barysch, *Russia, Realism and EU Unity*, 5.
[461] Walker, "Russia v. Europe," 5.
[462] Alexander Bulygin, "There is no mystery in Russia pursuing its interests," *Financial Times*, 6 March 2007, http://www.ft.com/intl/cms/s/0/bd7167a8-cbfe-11db-a661-000b5df10621.html#axzz3LG8t5AXa, quoted in Walker, "Russia v. Europe," 5.
[463] Youngs, "Russia," 98.

this state of affairs would limit foreign policy maneuverability. Political challenge would be to find the right policies to encourage competition and to protect long-term investments in infrastructure and production. The problem with this strategy is that it leaves producing states frustrated with a feeling that their energy strategy was decided by outsiders. It is thought that this would eventually lead to politicization of energy security anyway.[464]

In contrast to liberal dimension, in geopolitical dimension of energy security, greater stress would be put on alliances and military would be involved in protection of energy supplies. The West would be involved in intense rivalry for supplies and Western energy companies would take control over production capacity through mergers in producer states.[465] Analysis of energy security from the geopolitical point of view leads to suggestion that the EU has long neglected to properly incorporate energy security concerns into its foreign policy. Europeans were drawn into false sense of security by international oil markets of 1980s that were functioning to consumer countries' preferences. Gradual politicization of energy in 1990s was mostly overlooked. Oil price reaching very low levels in 1998 was identified as the direct cause for regime changes in energy producing Nigeria, Venezuela, and Indonesia, preceded by protests and political instability. This was the direct consequence of the more aggressive stance displayed by energy producer states in the new millennium and infiltration of politics into energy security issues.[466] It was argued that geopolitical component of energy security became pivotal because there was no agreement on the basic governance structure for international energy markets.[467] Paul Roberts suggested that Western states are not seriously committed to decrease dependence on external supplies and to decrease consumption of hydrocarbons. Furthermore, their understanding of energy security was still to strike alliances with energy producing states under conditions that are more favorable than other competitor consumer states in the West and in the world.[468] In doing so, they directly contribute to politicization of energy

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[464] John V. Mitchell, *Renewing Energy Security* (London: Royal Institute of International Affairs, 2002), 5, http://www.chathamhouse.org/sites/files/chathamhouse/public/Research/Energy,%20Environment%20and%20Development/renewing_energy_security_mitchell_july_2002.pdf, quoted in Youngs, "Concepts of Energy Security," 8.

[465] CIEP, *Study on Energy Supply Security and Geopolitics* (The Hague: CIEP, Netherlands Institute of International Relations, 2004), 24, 26, 91, http://reaccess.epu.ntua.gr/LinkClick.aspx?fileticket=Bgw7mGJEWls%3D, quoted in Youngs, "Concepts of Energy Security," 8.

[466] Youngs, "Concepts of Energy Security," 8.

[467] Bernard Mommer, *The Governance of International Oil: The Changing Rules of the Game*, WPM 26 (Oxford: Oxford Institute for Energy Studies, 2000), ii, http://www-personal.umich.edu/~twod/venezuela/nwaeg_mar07/mommer_governance_intl_oil_2000WPM26.pdf, quoted in Youngs, "Concepts of Energy Security," 9.

[468] Paul Roberts, *The End of Oil: The Decline of the Petroleum Economy and the Rise of a New Energy Order* (London: Bloomsbury, 2005), 94, quoted in Youngs, "Concepts of Energy Security," 9.

security and promotion of its geopolitical dimension, while EU institutions still insist on market-based international coordination.

Increasingly, Western norms of international markets and competition are dropped in favor of bilateral deals between consumer-producer national energy companies and their governments. This is what countries such as Germany and Italy have been doing with Russia, disregarding the interests of any other EU country, and what other EU Member States are starting to do following the example set by Germany and Italy. Energy is acquiring strong geopolitical component for which EU institutions are not prepared for, and they do not seem to accept it. EU Member States on the other hand have been engaging in energy projects with Russia, which strongly support geopolitical dimension of energy security promoted by Moscow. Russia has exposed deficiencies of the EU's free market approach for dealing with energy security.[469]

Not only in Europe, but also in the world, there is a global political concern over energy supply security. Markets are tight and prices are high since it is expected that global demand will grow faster than global supply.[470] Rapidly developing Chinese and Indian economies are demanding substantially more energy imports. Energy sectors of China, India, and Russia are under effective state control. They prefer to deal with energy business in a manner that does not adhere to Western liberal norms.[471] It was argued that energy policy could not be understood in any other way than as emerging quadripolar world with the United States, the EU, Middle East and Asia being separate power blocks.[472] Supporting this geopolitical picture is the fact that energy supplies are becoming increasingly concentrated in a smaller number of countries which prefer state-control approach, and this does not bode well for the free-market dynamics. Russia, Iran, Turkmenistan, and Qatar have more than half of global gas reserves.[473] By mid-2000s, experts such as Daniel Yergin and John Gault were warning that energy issues could not be properly addressed anymore by energy specific policies, but rather, energy issues should be incorporated into broader foreign policy.[474]

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[469] Antonio Marquina, "Introduction," in *Energy Security*, ed. Marquina, xvi.
[470] Perovic, "Introduction," 1.
[471] Coby Van der Linde, *Energy in a Changing World*, inaugural lecture as Professor of Geopolitics and Energy Management at the University of Groningen, Clingendael Energy Papers, no. 11 (The Hague: CIEP, Netherlands Institute of International Relations, 2005), 6, 13-14, http://www.policyinnovations.org/ideas/policy_library/data/01328/_res/id=sa_File1/, quoted in Youngs, "Concepts of Energy Security," 9.
[472] Mark Leonard, *Divided World: The Struggle for Power in 2020* (London: CER, 2006), quoted in Youngs, "Concepts of Energy Security," 9.
[473] Youngs, "Concepts of Energy Security," 9.
[474] John Gault, "EU Energy Security and the Periphery," in *European Union Foreign and Security Policy: Towards a Neighbourhood Strategy*, ed. Roland Dannreuther (London: Routledge, 2004), 170; Daniel Yergin, "Ensuring Energy Security," *Foreign Affairs* 85, no. 2 (2006): 69-82,

European sensitivity on energy issues was displayed when Russia and Algeria talked about the possibility of creating a gas cartel on the model of OPEC. Some European governments panicked and demanded EU intervention. Any mention of gas exporters coming together in cartel will result in extreme political and commercial reactions from Europe. Sometimes even perceived and not real threats will result in extreme reactions.[475] Exporting countries, on the other hand, feel that they have long been damaged by commercial rules imposed by importing countries. Such is the case with EU gas liberalization and competition policies which require exporters to conform to rules which they do not agree on.[476] This new assertiveness by exporting countries has been termed 'resource nationalism'.[477]

Resource nationalism has created significant commercial challenges to international oil and gas companies who are faced with governments in energy exporting countries taking control over energy resources and demanding higher rents. The Organization for Economic Cooperation and Development (OECD) energy giants are also faced with increased competition for exploration and development of energy fields from Chinese and Indian energy companies. Resource nationalism also saw some energy-rich countries challenging political and geopolitical status quo which they see as imposed by the United States and the EU when energy producers were weak.[478] This was the case with Russia. In the new millennium, they challenged energy deals signed with Western energy giants when Russia was experiencing economic crisis during 1990s, they renationalized energy companies, and became more assertive internationally, leading to gradual politicization of its energy relations with the EU.

5.4.3. Politicization of EU-Russian Energy Relations

When Russia cut-off gas supplies to Ukraine, leading to decreased supply to Europe, a debate was diffused throughout Europe on the role of Russia as energy supplier to the continent. The European media portrayed Russia as being responsible for the decreased supplies of gas to Europe; however, it was Ukraine that was diverting the gas destined for European markets for

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http://www.un.org/ga/61/second/daniel_yergin_energysecurity.pdf, quoted in Youngs, "Concepts of Energy Security," 10.

[475] Stern, "The New Security Environment," 84.

[476] Jonathan Stern, *Is There a Rationale for the Continuing Link to Oil Product Prices in Continental European Long-Term Gas Contracts?*, NG 19 (Oxford: Oxford Institute for Energy Studies, 2007), http://www.oxfordenergy.org/wpcms/wp-content/uploads/2010/11/NG19-IsThereARationaleFortheContinuingLinkToOilProductPricesinContinentalEuropeanLongTermGasContracts-JonathanStern-2007.pdf, quoted in Stern, "The New Security Environment," 84.

[477] Stern, "The New Security Environment," 67.

[478] Ibid., 67-68.

its own use since Gazprom halted gas deliveries for the Ukrainian market.[479] Some EU officials stated that Moscow is not a reliable supplier any more. In return, some Russian officials stated that the EU is not a reliable customer any more. Both sides also expressed a wish to diversify away from each other.

Gazprom issued several warnings that year. In May 2006, a Gazprom statement indicated that in the future there may not be enough gas for Gazprom to satisfy all of its current customers. Gazprom's vice CEO, Alexandr Rjazamov, stated that those countries not paying the market price are the most likely to find themselves without Russian gas supply. This was followed by a warning from Gazprom's CEO Alexei Miller, saying that if EU continues tried to limit Gazprom's access to European energy market, Gazprom would be obliged to search for new markets for gas exports.[480] However, many experts noted that the process of diverting supplies away from the EU would be too lengthy and too costly to be feasible.[481]

Another alarmist debate in Europe concerns predicted gas shortages in Russia that are bound to happen soon. Russians reject this claim. Western analysts supporting this claim that Russia will soon be unable to meet its supply commitments to Europe, point out that production in the fields in Western Siberia is declining, substantial investments are needed in upstream sector and ageing infrastructure, and there is uncertainty that there will be enough Central Asian gas to offset decline in Russia's gas field production.[482]

The debate on the security of European gas supply is focused on Russia. Many commentators have discovered the topic of security of Russian gas supplies on 1 January 2006. However, the topic is not new.[483] What has changed is that gas volumes delivered to Europe are much higher than in previous decades, Europe is more dependent on gas than before and general public became concerned that Europe imports most of its oil and gas needs from few countries which can use this against Europe. For the EU, Russia is the single largest gas supplier. This newfound issue of distress, following Russia-Ukraine gas crisis, was not properly addressed by the Commission's March 2006 Green Paper regarding energy security. While general public was concerned about increasing volumes of energy imports from Russia, in Green Paper it was

[479] Tatiana Romanova, "Energy Dialogue from the Strategic Partnership Level to the Regional Level of the Northern Dimension," in *The EU-Russian Energy Dialogue*, ed. Aalto, 89, quoted in Aalto, "European Perspectives," 165.
[480] Susanna Niinivaara, "Gazprom: Kaasua ei riitä kaikille," *Helsingin Sanomat*, 22 April 2006, B3, quoted in Palonkorpi, "Energy Security," 13.
[481] Youngs, "Russia," 80.
[482] Milov, Coburn and Danchenko, "Russia's Energy Policy 1992-2005,"; Alan Riley, *The Coming of the Russian Gas Deficit: Consequences and Solutions*, CEPS policy brief, no. 116 (Brussels: CEPS, 2006), http://aei.pitt.edu/11716/1/1389.pdf , quoted in Aalto, "European Perspectives," 165.
[483] Stern, "The New Security Environment," 59.

proposed to deepen energy cooperation with Russia. Commission also insisted that Russia must sign the ECT, which was in line with 1990s rhetoric and not in line with changed geopolitical circumstances of the new millennium. After the crisis, the Commission only proposed what was proposed many times before without any significant results. The Commission also failed to play any significant role during and after the crisis, either through EU-Russia Energy Dialogue or EU-Ukraine summits.[484]

Russia is important for the larger Eurasian energy flows because most of oil and gas exports from energy-rich Caspian and Central Asian countries still pass through Russian pipelines. Russian energy sector generated massive wealth which led to the accumulation of substantial financial reserves in the new millennium thanks to oil and gas prices reaching new heights. Most of this wealth came from energy sales to Europe. This new prosperity led to political stabilization and economic growth, with more people than ever feeling prosperous. Russia paid-off its debts to the Paris Club, accumulated from 1990s when energy prices were low and Russian economy was weak. With debts paid-off to the West, Russia did not feel tied-up anymore and it pursued assertive and independent foreign policy. Threats to diversify energy supplies away from Europe to Asia became common.[485]

Russia's rise as energy power has created level of controversy in the West not seen since the end of the Cold War. During the Cold War, the United States was very critical of Western Europe when it started planning to import significant volumes of Soviet gas since earnings could be used for military purposes. In the new millennium, the United States is again warning Europe to diversify away from Russia. As was the case during the Cold War, Europe is still Russia's main trade partner and energy sales to Europe are its main source of income. Russia has stated that the aim of its energy policy is to get the best possible economic results. In the West, the widespread perception is that Russia is using its position as a major energy supplier to the EU as a political tool. Some are accusing Russia of using energy to pull European partners and its neighbors into Russian orbit.[486]

Gas cut-offs to Ukraine and Belarus created some political tensions between Russia and the EU. To general public in Europe, Russia's image as secure and reliable energy supplier was tarnished.[487] Still, some EU Member States and Russia almost immediately started construction on new pipelines from Russia to the EU and signed new long-term bilateral agreements that will increase EU's dependence on Russian energy resources. Political tensions seemed to last for

[484] EC, *Green Paper*, 2006; Stern, "The New Security Environment," 60-61.
[485] Perovic, "Introduction," 1.
[486] Ibid., 1-3.
[487] Ibid., 11.

that period of time until new energy deals were signed.

Stern argues that political limit to Russian gas supplies to Europe is in sight due to gas crisis in early 2006. This view was derived from European political reaction to Russia-Ukraine gas pricing dispute. This limit would be imposed without any analytical conclusions about European dependence on Russian gas, or likely consequences of supply cuts.[488] As noted by Skinner, it is rather psychological notion of security which may be even more important than examination of likely scenarios.[489] Stern concludes by noting that by 2020, Europe (including Turkey but excluding former Soviet Union countries) should not expect more than 200 bcm of Russian gas per year or any increase in supplies after 2020.[490] In 2013, Gazprom supplied 161.5 bcm of gas to Europe.[491] When and if Gazprom becomes reluctant to renew long-term gas contracts or curtails short-term gas supplies, Europe should be concerned that Gazprom is unable to deliver demanded gas supplies to Europe. The prospect of constrained gas production in Russia has already resulted in Putin announcing a new policy in January 2007, which would put emphasis on coal.[492]

Western security discourse usually portrays Russia as an aggressor in its energy relations who is becoming increasingly successful in converting its energy exports to Europe into economic and political capital. Many Western scholars suggest that Europe is too dependent on Russian energy.[493] Some NATO members even threw in an idea of "energy NATO" or that gas cut-offs by Russia should be classified as an attack which would justify invocation of Article V on collective defense.[494] This perception is created by the manner in which Russia is pursuing its business interests in Europe, a policy described by the President Vladimir Putin as "energy

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[488] Stern, "The New Security Environment," 62.
[489] Robert Skinner, *Strategies for Greater Energy Security and Resource Security*, Background Notes (Oxford: Oxford Institute for Energy Studies, 2006), http://www.oxfordenergy.org/wpcms/wp-content/uploads/2011/02/Presentation34-StrategiesforGreaterEnergySecurityandResourceSecurity-RSkinner-2006.pdf, quoted in Stern, "The New Security Environment," 62-63.
[490] Stern, "The New Security Environment," 63.
[491] "Gas supplies to Europe," Gazprom Export, http://www.gazpromexport.ru/en/statistics/.
[492] Walker, "Russia v. Europe," 5.
[493] Janusz Bugajski, "Energy Policies and Strategies: Russia's Threat to Europe's Energy Security," *Insight Turkey* 8, no. 1 (2006): 141-148; Svante E. Cornell and Niklas Nilsson, eds., *Europe's Energy Security: Gazprom's Dominance and Caspian Supply Alternatives* (Washington, DC and Stockholm: Central Asia-Caucasus Institute and Silk Road Studies Program, 2008), http://www.isdp.eu/images/stories/isdp-main-pdf/2008_cornell-nilsson_europes-energy-security.pdf; Marshall L. Goldman, "The Dog Barks but the Caravan Moves On," *The Journal of Post-Soviet Democratization* 15, no. 4 (2007): 360-370; Frank Umbach, "Europe's Next Cold War: The European Union Needs a Plan to Secure Its Energy Security," *Internationale Politik–Global Edition* 7 (2006), 64-71, http://www.ssoar.info/ssoar/handle/document/13095, quoted in Closson, "Russia's Key Customer," 89.
[494] These suggestions have been made by the Polish and U.S. governments in 2006 and 2007, respectively, quoted in Closson, "Russia's Key Customer," 89.

supremacy."[495] Another reason for concern is that Russia is actively pursuing opportunities that would give it greater control over gas flow from East to West, as well as pursuing close ties with other gas exporters to Europe or even the potential ones. Russia is also active in sabotaging, in one way or the other, any proposed projects that may result in gas and oil from the East circumventing Russian territory. So far they have mostly been successful. Russia has engaged in pricing tactics in CIS countries, gas cut-offs to Ukraine and Belarus, pursuit of transit monopoly on gas going to Europe, refusing to ratifying the ECT, and limit on foreign investments in upstream projects in Russia. With such dubious activities from EU's point of view, Russia still demands free access to EU markets. As alarming as these signs are, there is still strong interdependence between EU and Russia that greatly benefits both.[496]

Closson states that EU-Russia interdependence will continue in the future and it will create conditions favoring cooperation over confrontation. One third of Russian GDP growth in the recent period has come from natural resources sector, while oil and gas taxation has contributed 50% to federal government fiscal revenue.[497] Besides statements to the contrary, Russia's dependence on hydrocarbon exports is most likely to grow. Other sectors of the economy are facing underinvestment. Energy sector is in need of huge investments as well, to boost productive capacity and upgrade infrastructure. The IEA is forecasting that Russian energy sector will need $800 billion worth of investments by 2030.[498] Russian strategy is to build more pipelines to Europe, buy more storage facilities and sign long-term purchase guarantees. With such developments, Russia is looking to remain a major player on the European energy market for the foreseeable future, accounting for quarter of hydrocarbons consumption and 40% of European energy imports. However, European gas demand is projected to rise by 70% by 2030 and Russia will not be able to cover this European demand growth.[499] The actual high interdependence between the EU and Russia is lost in the portrayal of Russia as an aggressor and the EU as player in a position of disadvantage. Closson states that Russia is better at understanding European business practices than Europe is in understanding anything about Russia. In the new millennium, Russia has engaged with individual European governments and their national energy companies and they participate in the business together. This resulted in

[495] President Putin's Candidate of Sciences dissertation at the St. Petersburg Mining Institute, completed in 1997, emphasizes the role of gas in projecting Russian influence, as a means of re-entering the ranks of great powers, quoted in Closson, "Russia's Key Customer," 89.
[496] Closson, "Russia's Key Customer," 89.
[497] EC, *Russian Federation: Country Strategy Paper 2007-2013* (Brussels: EC, 2007), 33, http://ec.europa.eu/external_relations/russia/docs/2007-2013_en.pdf, quoted in Closson "Russia's Key Customer," 89-90.
[498] EC, *Russian Federation: Country Strategy Paper 2007-2013*, 36, quoted in Closson, "Russia's Key Customer," 90.
[499] EC, *Green Paper,* 2006, quoted in Closson, "Russia's Key Customer," 90.

profitable business of creating joint stock companies and constructing pipelines in the EU, investing in storage facilities, refineries and terminals, and swapping Russian sales in European markets to European customers for upstream exploration rights in Russia's Far East.[500]

The problem for EU unity and its contradictory relations with Russia is that there is strong animosity between some Eastern European Member States and Russia. In the East, historical grievances are not forgotten. The EU was accused by Poles of not doing enough to help it fight Russian ban on Polish meat. In response, Poland vetoed start of negotiations on new EU-Russia treaty. Baltic States have regular problems with Russia over border treaties, Russian minority rights, and trade and transit issues. Russia has not shipped oil to Lithuania's only refinery in Mezeikiai since July 2006. Lithuania was left angry but unable to do anything by itself. Russians said technical fault was to blame. However, before the cut-off, Lithuania decided to sell its refinery to energy company from Poland and not to Russian one. Estonia experienced political problems with Russia over removal of the Soviet War Memorial from the center of Tallinn. This resulted in riots in April 2007 during which one Russian speaker died. EU criticized Estonia for insisting to move the Memorial. Estonia accused Russia of orchestrating cyber-attacks on its computer servers following the removal of the Memorial. Russians suspended rail traffic to Estonia and sent threats to Estonian diplomats in Russia.[501]

Besides Poland, Central European states have relatively good relations with Russia. Some countries such as Slovakia, Hungary, and Bulgaria are following the example of major European economies and forming closer bilateral ties with Russia. Unsurprisingly, calls for EU solidarity are the loudest from Poland and the Baltic States. Poland blocking negotiations on EU-Russia treaty only gave Russia an excuse to say that they were forced to make bilateral deals with member countries because EU institutions were paralyzed. Seeing as EU institutions are overloaded by administrative and bureaucratic rules that take too much time and that they are bound to follow, Russia seems to be right to deal with Member States individually. Some Member States that are too weak when compared to Russia are trying to use their EU membership card to sort out their problems with Russia.[502]

As world's major oil and gas producer, discussion on Russia is a mandatory component of any talk regarding EU energy security. Often the focus in these debates is solely on Russia. Russia's increasing confidence which leads to assertiveness has left some European countries quarrelling over how to respond to Russian challenge. This has caught the attention of general public and

[500] Closson, "Russia's Key Customer," 90.
[501] Barysch, *Russia, Realism and EU Unity*, 3.
[502] Ibid.

created much debate in the media. One of the popular opinions in the West is that importance given to Russia in these debates far exceeds the actual importance for many Member States' energy supply dependency.[503] Another opinion is that Russians need the EU to keep their country stable and strong. More than half of Russian trade is with EU. Most of foreign investment comes from EU as well. Russia will need EU's money and expertise to boost production capacity and to modernize its economy. Russia is also investing in EU and it is in Russia's interest to have the EU stable with well-functioning markets. It is in Russia's best interest to have good relations with the EU.[504] It is also widely thought that fear of Russia in Europe is directly contributing to Russia feeling important, powerful, proud, confident and assertive. One EU official pointed out that the more Europeans talked about this, the more Russians will be tempted to play this card.[505] Many experts also advanced an argument that Russia was not the rising power in the same sense as China for example, but that it was rather on a long-term path of decline, currently enjoying moment of greatness thanks to unusually high energy prices. Russia's trajectory is not a long-term trajectory of great power.[506] Russia on the other hand finds itself in defensive position because it is fighting against Western cultural expansion coming to its borders and repeated attempts to impose Western norms on Russian society, such as human rights and liberal democracy. In fighting-off such impositions, Russian policy becomes less predictable and more aggressive.[507]

Closson argues that Russia will likely be the more dependent actor in future EU-Russia energy relations.[508] The EU is Russia's main trade partner in both imports and exports. Two-thirds of Russia's oil exports go to EU. 15% of EU's oil consumption and 30% of oil imports come from Russia.[509] For gas, it is argued that to sustain current gas deliveries to Europe, Russia will need to either import more gas from Central Asia or to curb domestic demand. Russian oil is expected to cover only 30% of the EU's medium-term oil demand growth.[510] In the medium term, the share of Russian gas in EU markets is expected to be 23% of total demand.[511] For oil,

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[503] Youngs, "Russia," 79.
[504] Barysch, *Russia, Realism and EU Unity*, 8.
[505] Ibid., 5.
[506] Youngs, "Russia," 80.
[507] Viatcheslav Morozov, "Resisting Entropy, Discarding Human Rights: Romantic Realism and Securitization of Identity in Russia," *Cooperation and Conflict* 37, no. 4 (2002): 409, http://cac.sagepub.com/content/37/4/409.
[508] Closson, "Russia's Key Customer," 95.
[509] EIA, *Country Brief: Russia* (Washington, DC: DOE, EIA, 2008), quoted in Closson, "Russia's Key Customer," 95.
[510] Closson, "Russia's Key Customer," 95.
[511] The Institute for Energy Strategy in Moscow has released a Conception of Russian Energy Strategy to 2030, supposedly requested by factions within the government. However, its status of official approval is unknown, quoted in Closson, "Russia's Key Customer," 95.

in the long term, the EU can diversify. For gas, Russia is as dependent on the EU for money from gas sales just as the EU is dependent on Russia for gas consumption.[512]

Closson also underscores that level of dependence on Russian energy imports varies across the EU. There are highly valued high-paying European customers such as Germany and Italy whose demand is growing and who are signing new long-term bilateral contracts with Russia and investing in joint projects and upstream activities on Russian territory. There is also a group of states whose dependence on Russia is much higher such as Baltic States, Finland, and countries of Central and Eastern Europe. In the third category are states that may soon become more dependent on Russia because their domestic reserves are drying up, such as Norway, the Netherlands and the United Kingdom. Russia adjusts its attitude depending on which block of countries it is dealing with.[513]

Katinka Barysch argues that just as the EU is heavily dependent on Russia, Russia is heavily dependent on the EU as well. Russian energy sales to Europe are the biggest source of their foreign exchange. Energy sales to the EU are making Russia more stable, richer and self-confident and EU's image of them as intimidating is making Russia even more assertive. It was suggested that Europeans should not be worried about Russia not being willing to sell them gas, but they should be worried about Russia's future ability to do so. Russia's gas output has been stagnating for years while domestic demand is growing. She calls for the EU to readjust its attitude to new geopolitical realities and to drop the pretense of building strategic partnership with Russia based on common values.[514]

Tom Casier as well is of the popular opinion in the West that to Russia, EU is a link to the developed world to which Russia wants to belong and major source of hard currency earnings. The EU is also a rival great power from whose influence Russia must protect itself since it becomes a source of destabilization for the ruling regime. The EU is also Russia's most important trade partner. More than 60% of foreign direct investment to Russia comes from the EU. Moscow disagrees with the EU on the meaning of some democratic principles but they recognize that it is in their best interest to keep close economic relations with the EU.[515] Energy link between Russia and the EU is that of mutual dependence. Russia is the most important

[512] Closson, "Russia's Key Customer," 95.
[513] Ibid., 95-96.
[514] Barysch, *Russia, Realism and EU Unity*, 1, 5.
[515] Tom Casier, "Putin's Policy Towards the West: Reflections on the Nature of Russian Foreign Policy," *International Politics* 43 (2006): 389, 393, http://graduateinstitute.ch/files/live/sites/iheid/files/sites/political_science/shared/political_science/1988/CASIER_2006_PUTIN_POLICY_TOWARDS_WEST.pdf, quoted in Morales, "Russia as an Energy Great Power," 29.

energy supplier to the EU, especially gas for which demand is expected to increase more than oil, because gas is increasingly being used for electricity production. Europeans are paying high prices for Russian energy which directly contributes to Russia experiencing sustained economic growth and full budget.[516] However strained EU-Russia political relations may be, drastic moves by either are prevented by their mutual interdependence. Energy trade with Russia started in the first place because Europe was looking to improve its energy security by diversifying away from oil from unpredictable Middle East region.[517] Possible confrontations and complications in Iraq, Iran and Persian Gulf make continuation of energy cooperation with Russia desirable.[518] However, EU energy security would best be ensured by the common energy policy. Energy policies are left to Member States to decide on. Russia has used this situation to improve its position as energy supplier.[519]

Unlike the EU and the United States, East Asian countries such as China and Japan seem unconcerned about Russia's rise as energy power and possible geopolitical consequences. They see rise of Russia as an opportunity to develop new energy fields on Russian territory that will secure them new energy supplies.[520] East Asian countries and Russia seem to be interesting to each other as strictly energy consumer and energy producer. This may be because Russia seems to be projecting its power in Europe; therefore, powerful Russia is a European problem to handle.

5.5. EVALUATION

The fundamental statement of the Realist paradigm is that pursuit of power is the principal objective of states.[521] In Realism, international politics is described as a conflict between sovereign states struggling to gain more power and to survive in an anarchical world. Struggle for power is described as a zero-sum competition, therefore, more power for one state will mean

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[516] Fredholm, *The Russian Energy Strategy and Energy Policy*, 6-7; Zeyno Baran, "EU Energy Security: Time to End Russian Leverage," *The Washington Quarterly* 30, no. 4 (2007): 132, http://www.tandfonline.com/doi/abs/10.1162/wash.2007.30.4.131#.VIbgq9KsVic; Margot Light, "Russian Political Engagement with the European Union," in Roy Allison, Margot Light and Stephen White, *Putin's Russia and the Enlarged Europe*, Chatham House Papers (Oxford: Blackwell, 2006), 65, quoted in Morales, "Russia as an Energy Great Power," 29.
[517] Hill, *Energy Empire*, 29-30, quoted in Morales, "Russia as an Energy Great Power," 30.
[518] Smith, *Russia's Energy Diplomacy*, 3-4, quoted in Morales, "Russia as an Energy Great Power," 30.
[519] Baran, "EU Energy Security," 131, 135; Light, "Russian Political Engagement with the European Union," 66; "A Bear at the Throat," *The Economist*; Oleg Shchedrov, "Russia Wins Hungary for South Stream Gas Project," *Reuters*, 25 February 2008, http://uk.reuters.com/article/2008/02/25/russia-hungary-pipeline-idUKL2530997220080225, quoted in Morales, "Russia as an Energy Great Power," 30.
[520] Perovic, "Introduction," 11.
[521] Lebow, "The Long Peace," 263.

less power for another. Structural Realists further elaborate that the best policy for states to ensure security is to constantly concern themselves with relative gains of other states. In this view, the EU and Russia are rivals that seek to gain power at each other's expense by widening their sphere of influence in the post-Soviet space. For Russia, the major instrument of projecting their power internationally is energy; for energy-poor EU, the major instrument is promoting ideology of free-markets and liberal democracy. This lays the foundation for the instances of the EU-Russia political conflict which due to Russia's source of wealth is always greatly connected with the issue of energy. Russia subscribes to the Realist interpretation of energy policy in which energy is not an economic issue that should be left to market forces. In Realist theory, energy would be seen as a strategic resource which is important for national energy security; therefore, energy resources and energy production should be under government control. The EU adheres to liberal interpretation of energy policy in which supply and demand for energy resources (like other tradable goods) should be left to market forces to regulate.[522]

Besides EU's and Russia's conflicting energy policies – liberal markets versus realist state-control, the EU and Russia also have differing views on reciprocity, which was a concept proposed by Russia with aim to overcome their differing energy policies and to regulate the EU-Russia energy relations. However, in the EU's understanding, reciprocity implies putting in place legal framework to regulate investments reciprocally in open markets. In Russian understanding, reciprocity implies swap arrangements for energy assets (development and extraction rights for Russian energy fields in exchange for assets in EU's downstream operations), with the energy sector still firmly under state control. Reciprocity principle has joined the ECT and the Energy Dialogue as another failed attempt to establish a set of principles to regulate EU-Russia energy relations. The EU persistently insists on market-based solution to regulate EU-Russia energy relations which Russia persistently rejects. Unable to institutionalize their energy relations, gradual politicization of EU-Russia energy relations has been seen since 2006 gas crisis in Ukraine. This gradual politicization peaked in 2014 crisis in Ukraine when the seemingly simple economic issue of Ukrainian payment for Russian gas became a matter of high politics between the EU and Russia, with meetings taking place at the highest level. Displayed by the case of Ukraine which is an important transit country for Russian gas, the EU and Russia are engaged in geopolitical struggle to secure energy resources and pipeline routes. The EU's pursuit of energy security and Russia's pursuit of great power status has turned into a race to secure control over regions and countries that are rich primarily in oil and natural gas. Control over energy transit countries is seen as equally important as well. This race has turned

[522] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. Edwin Cannan (London: Methuen & Co., Ltd., 1904), http://www.econlib.org/library/Smith/smWN.html.

into a zero-sum contest that most recently led to armed conflict in Ukraine because Ukraine was forced to choose alignment with either the EU or Russia due to its difficult financial position.

The reason for the EU's failure to engage Russia in institutionalization of their energy relations can be found in the Realist analysis which states that powerful nation states are the central focus while international organizations and other groups are only considered as instruments to serve interests of the most powerful states in the international system. This is the view that Russia has often displayed regarding the EU by engaging the EU Member States in bilateral agreements instead of going through EU institutions. Willingness of its Member States to engage in bilateral agreements when it benefits them prevents the EU to form common energy policy and to properly respond to politicization of energy challenges originating from Russia's actions. The EU's most powerful states will not commit to common energy policy because when it benefits them, they prefer to act unilaterally, and when it suits them, they would also like to utilize full benefits of the collective EU might.

To better understand EU's dependence on Russian energy and Russia's dependence on energy sales to Europe, Keohane and Nye developed an analysis of interdependence, linking interdependence to power by using the concept of "asymmetrical interdependence" as a power source. "It is asymmetries in interdependence that are most likely to provide sources of influence for actors in their dealings with one another."[523] They concluded that asymmetrical interdependence can be used as a source of power in bilateral relationships.[524] They also analyzed the concept of "complex interdependence" which refers to a situation involving number of countries where multiple channels of contact connect those countries and their societies, and governments do not use military force towards one another.[525] Keohane and Nye highlighted that the major contribution of their book to the study of interdependence was to stress that patterns of economic interdependence have implications for power.[526] When analyzing politics of interdependence, they elaborated that just because there is interdependence, it would not automatically lead to cooperation, nor would it necessarily be benign in other respects.[527] "The key point was not that interdependence made power obsolete – far from it – but that patterns of interdependence and patterns of potential power resources in a

[523] Rober O. Keohane and Joseph S. Nye, *Power and Interdependence: World Politics in Transition* (Boston, MA: Little, Brown, 1977), 10-11, quoted in Robert O. Keohane and Joseph S. Nye, "Power and Interdependence Revisited," *International Organization* 41, no. 4 (1987): 728, http://www.jstor.org/stable/2706764.
[524] Keohane and Nye, "Power and Interdependence Revisited," 734.
[525] Keohane and Nye, *Power and Interdependence*, 24-25, quoted in Keohane and Nye, "Power and Interdependence Revisited," 731.
[526] Keohane and Nye, "Power and Interdependence Revisited," 736-737.
[527] Ibid., 730.

given issue-area are closely related – indeed, two sides of a single coin."[528] In Realist theory, military force is identified as the most important power resource at states' disposal in world politics. Due to zero-sum nature of the international system, states will struggle to maintain their relative positions in the system even if it needs to be achieved at high economic cost.[529]

Conclusion

The aim of this chapter was to examine the role of energy in the overall EU-Russian relations and to examine the extent to which energy security pursuit of the EU and great power pursuit of Russia are conflicting. As shown in the analysis, energy sales to the EU are the major source of Russia's foreign exchange earnings and Russia is the major energy supplier to energy-poor EU. This economic dependence is so great that any hint of a problem or irregularity invites public interest, media attention and political discussions that usually end up with calls for diversification of energy suppliers. Energy resources have become a major source of Russia's power and a major weakness for the EU. In the new millennium, high energy prices have enabled Putin administration to consolidate their power at home and to turn to foreign policy whose aim is to spread Russia's influence in its near abroad where EU is not a partner but rival for political influence. Besides its near abroad, Russia is also interested in engaging with potential future suppliers of energy to the EU, and many have interpreted this as Russia's attempts to undermine EU's diversification prospects. As shown in previous chapters, energy issues are creating discord among the EU Member States. Conflict resulting from energy security pursuit of the EU and great power pursuit of Russia is creating some political concerns; however, the biggest and most influential EU economies are anxious to avoid serious politicization of Russian energy in the EU. The EU-Russia energy conflict is unlikely to become militarized on the territory of EU or Russia; however, as was shown in the case of Ukraine, armed conflict in countries found in the middle is not excluded, resulting from the EU's and Russia's energy related power plays. It also seems unlikely that this conflict will become too politicized since their economic interdependence is very high and EU Member States have very different views on desirability of politicization of EU-Russian energy relations. Politicization of EU-Russian energy relations would mean that EU and its Member States would need to reconsider their Liberal interpretation of energy security based on free markets, and consider Realist interpretation of energy security where state would be more actively involved.

[528] Ibid.
[529] Ibid., 729.

CHAPTER 6: CONCLUSION

This thesis has attempted to analyze the importance of energy for the wider EU-Russian relations by using traditional realist perspective of zero-sum competition among states for power and security in an anarchical world. As has been shown throughout this thesis, energy is a major point of contention in EU-Russian relations given that energy wealth has elevated Russia's international status and made it more assertive, while energy-poor EU struggles to improve its energy security which is greatly affected by Russia's energy policy.

As was discussed in the first chapter, Realists (and Moscow) see energy resources not as economic goods that should be left to market forces to determine their prices and allocate their supply and demand (the liberal view promoted by the EU), but as strategic goods important for national security; therefore, energy exploration, production, and supply should be under government control. The introductory chapter laid the foundation for understanding how energy has become a dominant issue in the EU-Russian relations. Since the end of the Cold War (and Putin becoming the President in 2000), political conflict over ideology has been replaced by the conflict over pipeline routes, transit countries and energy prices, because Russia's power status in Europe is derived not from its nuclear arsenal, but from its energy wealth and control over energy flow from East to West. To this end, Russia has been active to spread disunity among EU Member States in order to prevent the EU from forming common energy policy which could undermine Russia's control over East-West energy corridor. Given their proximity and spheres of influence, EU's and Russia's international status is gained at each other's expense.

Chapter Two was dedicated to explaining concepts of Realism and energy security since they factor heavily in the analysis of the role of energy in EU-Russian relations. Section on the Realist theory paved the way for further analysis in which the EU and Russia are seen as two power blocks existing in an anarchical world, competing for power in a zero-sum competition. Realism also provides explanation for failures on the part of the EU to form common energy policy. Regardless of how strong the union is, the EU still consists of nation-states that are looking after their own well-being and survival. Self-help is the principle by which they are bound to operate in an anarchical system because national interests come before any other consideration in such an environment. As was shown throughout this thesis, those explanations given by Realism were exploited by Russia in order to prevent the EU from forming common energy policy, which in return prevents the Union from becoming a more powerful player on the international energy stage. Concept of energy security was introduced as becoming a major economic and political problem due to rising global energy demand, fear for future energy

supply, decline in new oil and gas field discovery, energy-rich regions being politically unstable, rising concerns about climate change and fear of future devastation. Energy security has been described as a complex mix of geopolitical and strategic concerns with added economic considerations. Due to EU's inability to form common energy policy, the EU has been unable to incorporate energy security issues into its foreign policy dimension. This is seen as imperative because the EU is energy-poor and it is world's major energy importer. Without common energy policy the EU cannot be a proper rival to Russia in their geopolitical struggle to secure energy resources and pipeline routes which leaves EU's energy security susceptible to Russia's threats and pressure.

Chapter Three dealt with analysis of many challenges preventing the EU to form a common energy policy, with Russian energy strategy underlined as creating most of those challenges. During 1990s energy prices were low, Russia was experiencing severe economic crisis and the EU was still mostly concerned with oil supply security. The European Commission was sporadically pointing out the advantages of common energy policy but there was no urgency in their reports, and therefore, their reception was lukewarm by Member States. They had no reason to make an effort for common energy policy since energy was cheap and economy was booming. Russia refused to ratify the ECT which would open up its pipeline infrastructure to foreign ownership, but Russia was also economically weak, borrowing heavily from the West. The EU also showed little interest to engage with Central Asian republics which were in disarray following disintegration of the Soviet Union. The opportunity was missed to engage energy-rich Central Asian countries on energy issues while Russia was too preoccupied with its domestic problems. Deeper engagement with those countries was not seen as necessary since Russia was considered as a reliable and trustworthy energy supplier during 1990s, with a good track record going back to Soviet era. Tables started to slowly turn against the EU's good energy and economic run when in 2000 energy prices tripled in a year and coincidently, Vladimir Putin became the President, armed not with nuclear weapons but with very specific ideas about correlation between energy resources and power. By the time EU institutions started urging EU Member States to form common energy policy following the 2006 Russia-Ukraine gas crisis, it was too late. Russia was too rich, energy was its major foreign policy instrument, EU was too dependent on Russian energy, and EU's biggest economies were pushing for opportunities to share in Russia's energy wealth by signing exclusive bilateral agreements which meant that they were not too interested in common energy policy while there were profits to be made by engaging with Russia bilaterally.

Chapter Four dealt with Russia's energy strategy in the new millennium under the direction of Vladimir Putin. Putin administration seized control over energy sector either through state ownership or through its substantial power of influence. Wealthy oligarchs were bought out and they were no longer in control of the energy sector. Former intelligence officers like Putin were given key administrative roles and they took seats on energy companies' boards. In short, whether energy company is public or private, it is under state's control and it is bound to follow Kremlin's energy strategy at home and abroad if it is to continue its operations. It was acknowledged in the Energy Strategy of Russia that domestically, energy represents lifeblood for Russia's political, economic, and social stability. Moscow relies on energy sector to drive country's development and to keep electorate happy. This was possible due to very high energy prices in the new millennium. With consolidated power at home, Moscow could turn its attention to improving its power status abroad. Energy wealth and pipeline-control became a very powerful foreign policy tool that gave Russia comparative advantage over the post-Soviet space and energy-hungry EU. It enabled Kremlin to use manipulation of prices and supply as a foreign policy tool in order to gain influence abroad and to prevent countries of the former Soviet Union to align themselves with the EU, the United States and NATO.

Chapter Five dealt with EU-Russia energy policies in conflict, a conflict which has risen above mere energy issues and economic issues, and instead transformed into political issue. Given that energy is the source of social, economic and political stability in Russia and tool of its foreign policy, on Russia's side, energy-economic-political issues are chained together and they are one and the same. As shown throughout this thesis, if Russia is experiencing problems in one component of the chain, it will inevitably find a way to become other two issues as well. So far, the EU has resisted such outright politicization of energy. One block of EU countries in Eastern and Central Europe (which are highly dependent on Russian energy and not powerful enough) is pushing for common energy policy and politicization of EU-Russia energy relations. The other block of EU countries is resisting politicization and is composed of those Member States in the West who are engaged in lucrative energy projects with Russia, spearheaded by their energy giants (some of which are national monopolies). With such conflicting interests within the Union, the EU institutions are unable to guarantee energy security for its Member States and they lack means to respond properly to Russia's energy strategy which is embedded in geostrategic thinking. In short, discord within EU has left Russia free to become more aggressive in its foreign policy in order to reassert its power status in the post-Soviet space on the back of energy wealth, and it has left EU struggling to retain its own power standing.

In conclusion, this thesis tried to show that EU-Russia relations are driven by energy considerations. EU is locked into dependence on Russian energy by pipeline infrastructure mostly inherited from the Soviet era and by the fact that other energy-rich regions are politically unstable. Given that energy resources are source of Russia's stability domestically and its power internationally, energy is seen as political, economic, and foreign policy tool. Russia is using its energy wealth and control over East-West pipelines to manipulate supply and prices in the post-Soviet space in order to support its foreign policy goals. It is also using its position as a major supplier to the EU to have its Member States competing amongst themselves for more favorable energy deals and new pipeline routes. This tactic prevents the Union from forming common energy policy. Such policy would see the Union better equipped to respond to Russia's power plays in the post-Soviet space which is overall threatening EU's energy security, and more specifically, it is threatening national security of its Central and Eastern European Member States. It is also threatening the EU's power standing in the region. Energy security pursuit by the EU and great power pursuit by Russia are obviously in conflict, however, so far, serious politicization of that conflict has been avoided even after war broke out in important gas transit country Ukraine in 2014.

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