Gazprom is a monopoly gas company controlled by the Russian state. While the company presents itself as motivated solely by commercial logic and economic interest, it has a consistent track record of acting as an arm of the Kremlin’s foreign and economic policy. This paper provides an assessment of the choices facing the European Commission in regard to both Gazprom and Russia, as well as some background for the business community. In particular, the paper provides policy recommendations for US policy makers as the European Union (EU) negotiates on Gazprom’s latest pipeline project, Nord Stream 2, a proposed new export gas pipeline that would run from Russia to Western Europe below the Baltic Sea. Nord Stream 2 is slated to have the same throughput capacity as an existing pipeline, Nord Stream 1. The conclusion is that Nord Stream 2 is a politically motivated project that presents a major challenge to European law and EU principles, and jeopardizes the security interests of the United States and its EU allies.

Brief history of Gazprom in Europe

The Russian gas industry’s relationship with Europe has always been determined by the Kremlin. After the collapse of the Soviet Union in 1991, Boris Yeltsin partially privatized the Soviet Gas Ministry and renamed it Gazprom. The state always maintained majority control, however, and though there were efforts in the early days to make Gazprom behave as a private company, in practice, it evolved into a hybrid institution that brought foreign currency into the state budget, provided a slush fund for insiders, and could be deployed as a foreign policy tool in relations with the West and the former Soviet republics.

Gazprom has a monopoly on the gas transit system in Russia as well as a monopoly on pipeline exports outside Russia. Since 2000, Gazprom has produced roughly over 75 percent of Russian gas and is a dominant seller of gas and downstream player in many regions in Russia, the former Soviet space, and Central and Eastern Europe (CEE).

In the early 1990s, when gas prices were low and Russian relations with the West were warm, Russia restricted the political use of Gazprom to its immediate neighbors in the former Soviet space. That changed in the 2000s, with the accession of Vladimir Putin to the presidency. This period coincided with the beginning of an unprecedented rise in commodity prices, including gas. Putin, who had grander ambitions than his predecessor, quickly seized the opportunity to use Gazprom to further his political goals—most importantly by having Gazprom continue to link the price of gas to that of oil through long term contracts (LTCs). LTCs crucially included “destination clauses” that prohibited buyers from selling gas purchased from Gazprom to third parties, which ensured that Gazprom continued its bilateral trade with each European country separately, and allowed it to implement rigid take-or-pay clauses for piped gas, as opposed to more flexible contracts based on spot pricing and reduced intake obligations. Many countries that were heavily dependent on Gazprom’s gas were thus given a de facto choice: compromise with Russia on sensitive political and economic issues and receive favorable LTCs, or defy the Kremlin and pay high gas prices for years to come.

In 2009, the European Union, responding to Russian and North African attempts to dominate its internal gas markets, implemented the Third Energy Package. This legislative package, which came into force in September 2009, seeks to open more broadly the gas and electricity markets in the EU, while enforcing ownership separation or unbundling. In 2010–14, after demand for gas fell in Europe, competition from Norwegian producers, liquefied natural gas (LNG) suppliers, and spot traders increased, and customers started to challenge Gazprom’s pricing system and investment plans in arbitration courts. In the same period, Gazprom reluctantly agreed to include some limited spot pricing in its contracts. In 2011, its anti-competitive practices were exposed by a large EU Commission antitrust investigation, which revealed illegal practices in eight Eastern European countries where Gazprom continues to be a dominant or major supplier.

In addition to concerns over corrupt business practices, Gazprom’s operations are particularly disconcerting as the Kremlin uses the company to exert control over the post-Soviet space while deepening European dependence on Russian gas. The proposed construction of Nord Stream 2 would specifically allow Gazprom a strategic foothold in Germany, as the project “opens the prospect for Germany to become the main center for the transit and storage of Russian gas and its onward distribution in Western Europe.”


4 Unbundling is a legal process which ensures the separation of gas companies’ generation and sale operations from their transmission networks in order to remove monopolistic capacity and create more competition.


Kremlin’s gas games: from Nord Stream 1 and Turkstream to Nord Stream 2

The case of Nord Stream 1

After many years of negotiations, the agreement to begin construction of Nord Stream 1 (then called the North European Gas Pipeline) was signed in 2005 by Gazprom, BASF, and E.ON. While Gazprom’s likely motive was to bypass Ukraine—so as to reduce the political and economic power Ukraine derives from being the main transit country—Russian negotiators insisted that Gazprom strictly applied commercial logic against transit risks and offered additional (supposedly non-political) justifications for the Nord Stream and South Stream projects, such as “meeting Europe’s soaring gas demand,” bringing new Russian gas from the Shtokman and Yamal gas fields, and facilitating Central Asian gas exports to Europe.

Nonetheless, the Kremlin’s motivation for the construction of Nord Stream 1 was always political. Russia and Ukraine have long been involved in disputes over gas transit via Ukraine’s state-owned oil and gas company Naftogaz. From Moscow’s point of view, this was a clear indication of Ukraine’s political independence from Russia and a means to assert greater control over European gas markets.


The Kremlin’s Gas Games in Europe

- Nord Stream 1
- NEL
- OPAL
- Nord Stream 2
- Eastring
- Soyuz
- Brotherhood
- Yamal-Europe
- Turkstream
- TAP
- TANAP
- Blue Stream
- Trans-Balkan
- South Stream

OPERATIONAL

PROPOSED

UNDER DEVELOPMENT

CANCELLED
view, bypassing Ukraine’s transit system would allow Gazprom to control exports to the European market without negotiating for transit fees with Ukraine. Unlike other post-Soviet countries, successive governments in Kyiv tried to dictate transit terms for Gazprom’s gas, asking for political concessions from the Kremlin, and playing Europe against Russia on sensitive issues, using gas as leverage. Gazprom had to make payments to Ukraine as the price of transit, roughly one to two billion dollars per year.15 The Kremlin, and Putin personally, objected to having to make these payments, both because it was costing Russia and because this money, in effect, helped fund the Ukrainian budget and thus supported the existence of a politically independent Ukraine.16

In order to reduce these payments, the Kremlin sought to subvert the Ukrainian elite through various forms of corruption in the gas trade, allowing insiders from both sides to extract enormous rents. Ukrainian oligarchs nevertheless understood that renunciation of national control over the gas transit system would deprive them of future revenue, killing the goose that lays the golden egg. While vested interests in each successive government in Kyiv engaged in various forms of corruption in the gas trade, none of them allowed Gazprom ownership or control of the Ukrainian gas transit system. In 2007, the Ukrainian parliament passed legislation that prohibited privatization or leasing of any element of the gas transit system—legislation that would be difficult to change.17

Officially, as noted above, Nord Stream 1 was driven chiefly by the need to create greater and more secure supplies of European gas, especially when Gazprom was still considering development of the Shtokman offshore field and the Bovanenkovo field in Yamal, which the monopoly presented as brand new sources of gas to satisfy rising EU gas consumption.

In practice, Nord Stream 1 has been lucrative for Gazprom’s partners in the project but disastrous for Russian taxpayers and the state budget. The cost of transporting gas through Nord Stream 1 proved to be identical to or higher than the cost of transit via Ukraine.18 Furthermore, estimates show that the pipeline cannot adequately meet Europe’s peak demand due to base load arrangements19 and Putin’s documented manipulation of the supply.20 The pipeline has offered no cost savings, and the gas transported through Nord Stream 1 is simply being diverted from pipelines that go through Ukraine.21

Additionally, the promise of increased transit for Central Asian gas via Ukraine after the launch of Nord Stream 1 has also not been fulfilled. In 2009, at the start of the financial crisis and after a highly controversial incident involving an explosion on an import pipeline (believed to be staged by Russia),22 Gazprom defaulted on its

16 Putin started making degrading comments about Ukraine long before annexation of Crimea. In 2005, at the G-8 summit in Scotland, he said that Russia plans to increase cooperation with Ukraine only “if it stops nicking gas”; “G-8 Summit will take place in St. Petersburg in 2006,” Newsrus.com, July 8, 2005, http://www.newsrus.com/russia/08jul2005/piter.html; in 2007, responding to a question on democracy, Putin said that in post-soviet space “Ukrainian guys were the last hope but they have fully discredited themselves, it is going full speed to tyranny. Full violation of constitution and all laws”. “Putin had a hope for ‘guys from Ukraine’, but the latter are headed towards tyranny,” UNIAN, June 4, 2007, http://www.unian.net/world/48232-u-putina-byila-nadejda-na-rebyat-s-ukrainy-no-te-idut-k-tiranii.html; At a Russia-NATO summit in 2008, Putin told U.S. President George Bush that “Ukraine, it is not even a state! What is Ukraine? Part of its territories – it is Eastern Europe, another part, and a big one, was given by us as a gift!”, Olga Allenova, Elena Geda, and Vladimir Novikov, “NATO Bloc Divided Into Blocks,” Kommersant, April 7, 2008, http://www.kommersant.ru/doc/877224.
19 From autumn 2014 to spring 2015, Gazprom was ordered by Putin to unilaterally cut supplies by up to 50 percent to countries (Poland, Slovakia, Austria, and Hungary) that displeased the Kremlin by selling gas to Ukraine through reverse gas flow mechanisms. This is the most serious act of coercion by Gazprom in Europe since the company’s 2009 transit halt: Alan Riley, “Smoke and Mirrors: Russian Disinformation Meets Pipeline Politics,” Center for European Policy Analysis, March 29, 2017, http://cepa.org/EuropesEdge/Russian_Disinformation_meets_Pipeline_Politics.
20 Gazprom claims future supplies to Europe may come from Yamal and other new sources. However, the likelihood of this occurring is difficult to verify, and in any case this will in all probability be mostly or entirely Gazprom’s gas. No Central Asian or other non-Russian gas is slated to be admitted into Nord Stream 1 or 2.
binding agreement to import 40 billion cubic meters per year (bcm/y) of gas from Turkmenistan and has since kept the intake of Central Asian gas at a low level.

Nord Stream 1 is still far from profitable; volumes are uncertain for the next ten to fifteen years. Gazprom has guaranteed to return the €12 billion investment to its European partners, even if the pipeline stops working—a promise that, if fulfilled, will hurt the Russian taxpayer even further.23 Even if Nord Stream 1 were to pay back its construction loans by the mid-2020s, this would not bring any more revenue to Gazprom or the Russian budget, because the same volume of gas is being transported to the same customers under the same contract only through more expensive export routes.24

The Case of Turkstream
In the last ten years, apart from Nord Stream 2, Russia has sought out other projects designed to bypass Ukraine’s transit pipelines. These include South Stream, cancelled in 2014, and Turkstream, proposed to run from the southern Russian Krasnodar Region across the Black Sea to Turkey. Gazprom’s argument that Turkstream would serve rising gas demand in Southeastern Europe is rather weak, however. Even under optimistic scenarios, the main commercial prizes for Turkstream in the early 2020s would be Italian and Turkish markets, and possibly (through more pipelines) Northwestern Europe, not Southeastern Europe. Once again, the political reasons for the investment are far more important. In April 2015, Gazprom’s Chief Executive Officer Aleksey Miller made a milestone announcement about Russia’s intention not to renew a transit contract with Ukraine in 2019, and thereafter to stop all gas deliveries to Europe through that country.25 Miller suggested that by 2019, European customers would be able to find ways to pick up Russian gas from Turkstream at the future gas hub on the Greek-Turkish border.26

Since then, the Russian government has issued conflicting statements, regarding their intention to stop all transit through Ukraine over the next two years. In any case, both Turkstream and Nord Stream 2 are part of the same plan to bypass Ukraine and possibly shut it out from Gazprom exports completely by 2019 or soon thereafter. An additional motive behind Turkstream is to weaken the political and commercial influence of the EU-/US-led Southern Gas Corridor that aims to bring Azerbaijani gas to Europe via Turkey as an alternative to Gazprom’s gas.

Turkstream may also serve to repair Russian-Turkish relations, which were damaged after the Turkish military brought down a Russian jet flying over its airspace. Following a new intergovernmental agreement signed in August 2016,27 Turkey approved all necessary construction and environmental permits for the development of the first 15.75 bcm/y line of the pipeline in early 2017.28

The state of play for Nord Stream 2
In its advocacy of Nord Stream 2, Gazprom has sought from the beginning to portray the project as essentially identical to Nord Stream 1. But the political and economic context is very different in these two cases. At the time of the Nord Stream 1 approval in 2005, when the pipeline received most of its EU and national permits, the EU Third Energy Package had not yet been fully enacted. More importantly, Russia had not yet invaded Eastern Ukraine or annexed Crimea, and therefore did not have to address Western economic sanctions, which have limited Gazprom’s ability to raise long-term loans and access upstream technology to develop offshore and shale deposits.

This new context gave rise to new obstacles. The first is legal: if the project goes forward, Gazprom will be the sole supplier, as well as the dominant owner and operator, of the existing Nord Stream 1 and future Nord Stream 2 pipelines. This infringes on the core tenets of the Third Energy Package and other existing EU laws that require unbundling, tariff regulation, and third party...
The Kremlin's Gas Games in Europe

access rules, and which protect the security of energy supply and commercial viability of existing projects involving EU member states.\textsuperscript{29} Gazprom is suggesting that these gas regulations are not applicable to Nord Stream 2, on the grounds that they were not applicable to Nord Stream 1. The EU, however, has subjected the Polish end of the Yamal-Europe pipeline to a full Third Energy Package certification, so it is hard to see why an exception should be made for Nord Stream 2.\textsuperscript{30} At the end of March 2017, the EU Commission, after bitter disputes with German regulators and divisions within its own legal team,\textsuperscript{31} said it will seek a mandate from EU member states to negotiate with Russia on a special legal regime for Nord Stream 2; however, whether it receives such a mandate depends on approval from two-thirds of the twenty-eight bloc members\textsuperscript{32} and could delay the project’s start beyond 2019.\textsuperscript{33}

The second complication for Nord Stream 2 is political. Along with Ukraine, the pipeline will bypass several other countries with functioning pipelines. In March 2016, eight EU governments from Central and Eastern Europe signed a letter to the European Commission objecting to the Nord Stream 2 project, arguing that the project violates the competitive principles of the EU and could have “potentially destabilizing geopolitical consequences.”\textsuperscript{34} This letter, like other statements from opponents of Nord Stream 2 within national governments and among EU commissioners, argues that the project violates the spirit and aims of the emerging Energy Union.

Recent studies show that the overall welfare effect of Nord Stream 2 would be negative for the EU. Though Gazprom’s European energy partners and Transmission System Operators (TSOs) in Germany would gain profits, their counterparts in Central and Eastern Europe, Southeastern Europe, and Ukraine would lose.\textsuperscript{35} In addition, Nord Stream 2 would create throughput congestion in existing pipelines from Germany to Eastern Europe and significantly increase the risk that the project could be used to separate German and other markets and exercise market power in Central and Eastern Europe, Southeastern Europe, and Italy, as well as cut supplies to Ukraine.\textsuperscript{36}

Such outcomes would be particularly troubling for the United States, EU, and their allies as it would enable Russia to once again exert pressure on gas pricing in Central Europe, without the old tool of destination clauses. This would allow the Kremlin to coerce Kyiv as cut supplies to Ukraine, a scenario inevitably entailing political concessions from Ukraine.


“By giving the green light to Nord Stream 2, the EU will be endorsing a schizophrenic policy, in effect helping to empower a country whose policies are designed to undermine the EU.”
There is, however, a more straightforward argument for opposing the pipeline: Gazprom is one of the Kremlin’s main cash generators and international political tools. Even if Nord Stream is bad for the Russian budget, Gazprom secures lots of money from other projects. It also exports the message of Kremlin’s political and economic domination in the energy sector to Russia’s neighbors.

Gazprom’s Pressure on the EU

German Chancellor Angela Merkel is under pressure from the German industrial lobby, which wants lucrative deals with Gazprom, guaranteed long-term gas supplies, and an exclusive role as the new mega-hub for gas trade in the heart of Europe. So far, however, Merkel has been openly suspicious of Putin’s intentions in Ukraine and Europe, and has stood ambivalent to the project and firmly by the EU sanctions against Russia, even threatening to increase them over deteriorating situations in Syria and Ukraine.

Putin’s response to Merkel’s lukewarm position on Nord Stream 2, as well as her critical views on his regime, appears to have taken political form. There is a wide range of evidence suggesting that the Kremlin has been campaigning both directly and indirectly against her government, in part by trying to create anxiety about refugees and immigration. In France, Russian intermediaries are openly funding Marine Le Pen, the leader of the National Front, who has vowed to leave both the EU and NATO, and to join forces with Russia.

Another project that would extend Nord Stream 1 to the United Kingdom (UK) has apparently been shelved by Gazprom due to low gas prices. However, Gazprom’s leadership may simply be waiting to see if the Brexit process and Donald Trump’s presidency strengthen its hand and allow the project to move forward. The UK and United States have been key advocates of sanctions against Russia and skeptics of both Gazprom and Nord Stream 2. But with Brexit and the potential of a more domestically focused US policy, Russia’s allies in Europe may have an opportunity to sway Brussels, which has so far been opposed to the pipeline project.

To that end, Gazprom has undertaken an effort to secure prominent European customers and improve its image in Europe. In the United Kingdom, for example, the National Health Service, Oxford University, and other organizations have contracts with Gazprom.


In Europe, Gazprom has worked with top public relations firms such as GPlus, Hill & Knowlton, and Brunswick. In the US, the New European Pipeline AG, the consortium behind Nord Stream 2, has also been active: “Lobbying Registration,” Legislative Resource Center, February 1, 2016, https://sopweb.senate.gov/index.cfm?event=getFilingDetails&filingID=c-61517fa-a82e-4593-8eb8-223ae83bd229&filingTypeID=1.


The Kremlin’s Gas Games in Europe

The Austrian company OMV, a key supporter of the pipeline in Europe, joined the Nord Stream 2 consortium in 2015. In the same year, the company hired a new president, Rainer Seele. In a previous role as chairman of WINGAS, Seele was “above all responsible for alerting the public to the significance of cooperation with Russia for Europe’s gas supplies.”

“Gazprom’s anti-commercial mentality has also blinded the company to the long-term potential of shale gas in Europe.”

Still, despite Gazprom’s public relations efforts, in July 2016, the Polish antitrust agency (UOKiK) issued a formal objection to Nord Stream 2, arguing that the project will negatively affect Poland’s purchasing power in Russia. As a result, Gazprom’s European partners—Uniper, Wintershall, Shell, OMV, and Engie, all of which were slated to become 10 percent shareholders in Nord Stream 2 AG—gave up on the plan to form a consortium. Nonetheless, Prime Minister Dmitry Medvedev has since claimed that Gazprom has “already found ways of this project’s implementation with the participation of [Gazprom’s] foreign partners.”

Gazprom’s anti-commercial mentality has also blinded the company to the long-term potential of shale gas in Europe. With the rise of renewables, greater energy efficiency, and the emergence of unconventional gas (such as shale gas), Gazprom’s arguments become even less rational. The company itself mocks renewables, famously putting a frozen windmill on the cover of its corporate magazine. Gazprom officials periodically sneer at Europe’s pursuit of renewables and energy efficiency as uneconomical and politicized.

Gazprom also failed to foresee the long-term impact of LNG imports into Europe, including into its own traditional markets. In 2014, completion of the first LNG terminal in Klaipeda, Lithuania effectively ended Gazprom’s monopoly hold over its market there. Norwegian Statoil is now competing with Gazprom to be the main supplier in the country, and the price level for imported gas is now much more acceptable. In the long term, Poland, which opened its own LNG terminal at Świnoujście a year ago, is on the same trajectory.

Gazprom additionally failed to predict the rise in exports—not only from traditional LNG suppliers such as Qatar and Norway—but also from the United States, where prices have dropped due to shale gas production. Gazprom’s anti-commercial mentality has also blinded the company to the long-term potential of shale gas in Europe. Instead of adapting to the circumstances, the company has sought to use political means to undermine the shale gas industry. Over the past two years, Russia has been frequently suspected of organizing protest groups and lobbying

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56 “Norway to Surpass Russia as Lithuania’s Top Gas Supplier in 2016,” Reuters, February 8, 2016, http://www.reuters.com/article/lithuania-gas-idUSL8N15N1UF.
against shale gas development in Romania, Bulgaria, and other European countries.

The real reason for Gazprom’s reluctance to accept the realities of energy efficiency, renewables, shale gas, and LNG is that the company is ultimately accountable not to a commercial board but to its political masters in the Kremlin. Indeed, Gazprom lacks the managerial capacity and flexibility to make market-oriented responses to new developments. Instead, the company prefers to rely on things that it knows best: oil-linked LTCs, bilateral negotiations in European capitals, and subversive operations.

**Fierce competition in Central and Southeastern Europe**

After Gazprom announced its plan to end transit through Ukraine by 2019, several countries in Southeastern Europe responded with proposals to connect themselves and their neighbors to the new Turkstream delivery points in Greece and elsewhere. But these proposals are being driven by governments and national companies, not private investors. The interested parties hope to receive partial or full financing from the EU or Russia, as there is very little capital in the region for infrastructure projects. Several countries are promoting themselves as candidates for gas hubs and are in competition with one another and with Turkey. These countries—mainly Bulgaria and Greece, but also Albania and Croatia—seek to achieve hub status not only through their own (future) diversified pipelines and virtual trading platforms, but also with storage facilities and LNG terminals, where sea access is available. The warming up of Russo-Turkish relations in 2016 renewed Bulgaria’s hope that Gazprom will help finance a national gas hub in the Black Sea port of Varna, an idea that was put on hold when the South Stream pipeline was cancelled in 2014.

The construction of vital pipelines and interconnectors is a priority for most Southeastern European countries, but the question of who will fund them remains unanswered. Bulgaria, Hungary, Slovakia, and Greece all have strong pro-Russia factions that have, in the past, torpedoed EU-led gas projects, some of which were aimed at reducing local vulnerability to Gazprom blackmail. Both Brussels and Washington have fought back, either through legal means or political pressure, and all four countries have withdrawn support for key Kremlin gas and political initiatives in the past three years.

In countries with tenuous political cohesion and serious economic problems, the competition between Russia and the EU and/or the United States has spilled into politics. Last year, the Center for Strategic and International Studies published a report on Russia’s subversive activities in Eastern Europe, including a detailed account of Gazprom’s meddling in Hungarian and Bulgarian politics and economy. Responses to...

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64 This is not to say that Gazprom is incapable of employing commercial logic, but that there is a hierarchy in its decision-making process. All major financial, project, and contract decisions are made by the Kremlin with an eye to achieving political objectives. Gazprom’s top management thereafter ensures its own vested interests and those of well-connected sub-contractors and other insiders. Lastly, on a residual basis, the company applies commercial rationale for the remaining decisions. The commercial rationale is applied, in other words, only when it is politically suitable. When it is not politically expedient for the Kremlin and Gazprom management, commercial logic rarely applies, giving way to corruption and/or politically driven deals.

65 By and large, Southern and Eastern European countries lack even basic infrastructure, technology, and skilled personnel required for such a goal, and they are unlikely to improve in these areas in the next five to seven years without considerable external help. Ukraine has ample storage capacity but obviously lacks security and is undermined by Russia in various ways.


68 Other problems include a large shadow economy, bureaucratic obstruction, vested interests, and anti-EU nationalism.


70 Heather Conley et al., “The Kremlin Playbook: Understanding...
Gazprom’s operations by local governments have been inconsistent. Lastly, even though Turkstream was approved for construction, it is possible that future sanctions would seriously impede Russia’s ability to finance the project.

Political bottom line of Russia’s energy strategy in Europe

All indicators suggest that Russia’s pipeline policy is dictated entirely by opportunistic concerns. The Kremlin seems keen to take a few more years to engage with Southeastern European countries to see how the political situation there develops, but without jeopardizing old alliances.

Public comments from Gazprom and its associates support the hypothesis that Putin is biding his time while looking to sow confusion and provoke anxiety.

On the one hand, a former Gazprom consultant told the company’s official magazine that all European governments are run by the CIA, and that only Italy, Austria, Hungary, and Greece have the strength to resist the Americans in the upcoming regional confrontation in Europe between Russia and the United States.71 Another group of Russian ex-officials issued a consultancy outlook with aggressive wording about a future Russian victory over an “inconsistent European regulatory system” full of “absurd controversies,” and called for a halt to transit via Ukraine by 2020.72

On the other hand, however, Gazprom’s CEO has offered only vague warnings to European customers regarding

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its intentions to cut off supply via Ukraine. The Gazprom press service diligently assures Europe that “Gazprom will always meet its gas delivery obligations,” and that the company is “in discussions with our European partners to adjust the LTCs accordingly.”

In short, Gazprom and its Russian supporters are deliberately incoherent on how the monopoly can fulfill its obligations under LTCs without transit through Ukraine. Nevertheless, Gazprom keeps its rhetoric upbeat on the 2019 deadline and the many options available to bypass Ukraine’s gas transit system. Russian media boast that Gazprom is circumventing Western sanctions by buying expensive pipe-laying vessels to build Nord Stream 2 and offshore projects under sanctions in the Far East. It seems that, on the contractual level, Gazprom will seek to honor its obligations unless the Kremlin orders otherwise. However, in its public statements (or statements from its supporters), Gazprom will continue its abrasive and defiant propaganda.

Conclusions: implications for Western policy makers

Russia will not change through the EU’s unprincipled gas cooperation with Gazprom

Cooperation with Putin’s Gazprom should not be regarded as just another “trade decision” or form of “business as usual.” Large mineral extraction corporations and infrastructure companies have argued since Soviet times that bilateral trade with corrupt and authoritarian states will reform their political character and bring them closer to liberal market economies. The reality, however, is that oil and gas revenues allow dictatorships and kleptocracies to establish a stronger grip on power by deploying improved surveillance techniques, purchasing military and police equipment, and engaging in regional wars and domestic oppression. Both in the Cold War era and today, the Europe-Russia oil and gas trade has undermined both liberal capitalism and democracy.

Gazprom is a monopoly gas company controlled by the Russian state. Therefore, it should not be treated as a regular commercial enterprise. The avoidance of politically charged projects like Nord Stream 2 and demonopolization of the gas trade between Russia and Europe should become overarching objectives of the EU in all relevant policy fields.

“Cooperation with Putin’s Gazprom should not be regarded as just another ‘trade decision’ or form of ‘business as usual’.”

Concrete policy recommendations on Nord Stream 2

US and European policy makers should debunk myths about the positive outcomes of Gazprom’s proposed plans in Europe

To that end, US policy makers, Congress, and agencies should:

• Support the dissemination of information on Gazprom’s structure, strategy, and politically motivated actions against other countries in the policy-making community by holding open hearings and briefings.

• Task the US Department of Energy (DOE) with preparing and publicizing a forecast analysis for US LNG exports to Europe, assessing LNG’s ability to uphold competitive practices and satisfy long-term gas demand in Europe, while at the same time pointing out the limitations of US LNG trade in the European market. The DOE should work with the European Commission on the outlook of global gas demand and on sharing best business practices in the energy sector, which can be useful to the evolving Energy Union.

• Task US intelligence and law enforcement bodies to prepare a briefing for their EU partners on the current status of the Kremlin’s intelligence and organized crime operations in the energy sector in Europe and worldwide.

• Urge the European Commission and Parliament to sponsor an independent inquiry, by industry experts not associated with Gazprom or the Kremlin, into the funding of Nord Stream 1, Nord Stream 2, and the accompanying infrastructure in Russia and the host countries. The US Department of State and Department of Energy should assist

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73 These are statements from the Gazprom press service in response to the author’s questions regarding Miller’s comments about the 2019 deadline and the need for Europeans to agree on a new delivery point at the Greek-Turkish border.
as facilitators and expert contributors to this assessment.

To that end, European policy makers, institutions, and agencies should:

• Task the Directorate-General on Energy (ENER), International Cooperation and Development (DEVCO), and Trade (TRADE), together with The European Political Strategy Centre (EPSC)—the European Commission’s in-house think tank—with producing a comprehensive analysis of the history of European cooperation with authoritarian hydrocarbon states and the extent to which such cooperation has made these states more democratic. This study should also include an analysis of Gazprom’s compliance with the EU Third Energy Package and other competition regulations.

• Task Europol, together with relevant agencies of the EU Commission and national security agencies of EU member states, to conduct a study analyzing Gazprom’s use of Russian security agents in Europe, and the company’s connections to organized crime figures both within and outside Russia.

• Task the EPSC, along with other relevant think tanks and EU Commission research centers, to engage more proactively in conversation about the political and economic principles of the emerging Energy Union, and how to redefine the concept of EU energy security in light of Russia’s aggression against Ukraine in 2014. The EPSC, together with other relevant agencies, should publish a paper summarizing all legal and regulatory debates concerning Gazprom’s ambitions to build and access pipelines in Europe in a way understandable to the general public and media.

• Task the Disinformation Review (published by the European External Action Service) along with the Directorate-General for Energy to run a brand-new, separate analytical section countering energy propaganda coming out of Russia, as it creates a distorted view of the EU’s policies and outlook on renewables, shale, and other conventional and unconventional energy.

The protection of Ukraine’s sovereignty and its gas supply must be non-negotiable elements of any talks between US and/or EU agencies and Russia and Gazprom

US policy makers could consider the following:

• If Gazprom persists in isolating Ukraine from reverse gas flows from Europe, breaks its delivery or transit contracts with EU members in order to force its 2019 deadline on Ukraine, or if Russia and Gazprom expand their aggression against Ukraine in any other significant way, the US Congress ought to respond by increasing sanctions against Gazprom and its Russian associates and intermediaries in Europe. To that end, Congress should pass the Stability and Democracy (STAND) for Ukraine Act. The US State Department and Intelligence services should closely monitor all Gazprom’s plans to exclude Ukraine from commercially viable gas imports and share this information with EU allies.

• The US Department of State, the US Agency for International Development, and the National Endowment for Democracy, along with US representatives in the World Bank, should further enhance existing teams in Ukraine and develop a more comprehensive plan for the reform of Ukraine’s indigenous energy production to ensure more self-reliance and diversification away from Russia. In addition, contingency plans for decreasing volumes of Russian gas transit via Ukraine after 2019 should be prepared, focusing on measures that Ukraine and its EU neighbors can take even in worst-case scenarios.

European policy makers could consider the following:

• Relevant EU agencies should continue to implement the Deep and Comprehensive Free Trade Area (DCFTA) agreement with Ukraine and uphold standards for transparency and accountability in the energy market. As the EU Energy Union

74 In 2016, the US House of Representatives adopted H.R. 5094, the Stability and Democracy (STAND) for Ukraine Act, a bipartisan bill that locks in the minimum underpinnings of the US response to Russia’s annexation of Crimea and its occupation of parts of eastern Ukraine. This bill converts some of the Obama administration’s executive actions into Public Law, makes it much harder for President Trump to overturn. STAND also tightens current sanctions, extends the Magnitsky Act to all territories under Russian occupation, and requires the State Department to counter Russian propaganda and cyber offensives.
develops its principles and regulations further, the adjustment of DCFTA standards with Ukraine should be improved accordingly and without delays.

- The Directorate-General for Competition and Energy should prepare guiding principles on negotiations with Gazprom about Nord Stream 2 that would require Gazprom to be explicit about its position on the 2019 deadline ultimatum and demand that the company uphold all of its existing delivery and transit obligations with individual EU member states.

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