Central Europe's Energy Security Schism

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Executive Summary: Russia's monopoly control over post-communist Central Europe's energy sector constrains competition and increases Russian influence over American allies. The United States has an interest in helping Central European capitals mitigate the political impact of Russia's energy grip by helping them access alternative energy supply sources and encouraging greater European unity on energy policy. Complicating matters, however, is the fact that Central Europeans themselves are divided in their policy response to the phenomenon of Russian energy dominance. Absent a serious common EU energy policy, the United States' ten allies in Central Europe have adopted a diverse set of diplomatic and technical response strategies. In general, these responses can be divided between those of "strategic players" like Poland and Romania, and "commercial opportunists" like Hungary and Bulgaria.[1] While the former group spearheads efforts to check Russia's energy power, the latter displays a willingness at times to strike calculated partnerships with Russian energy companies. This energy security schism frustrates energy supply diversification projects like the Nabucco pipeline and opens avenues for Russia to restore its political and economic clout.

Implications for U.S. Policy:

- In a worst case scenario, Russia's dominant energy position could dissuade Central European states from siding with Washington on an international issue.
- At present trajectory, the United States' ability to encourage energy supply diversification in Central Europe will run up against certain states' willingness to bandwagon with Russia. Among other things, this will reduce the ability of the United States to align the interests of regional players on Western-backed pipelines like the Nabucco project.
- The United States should clearly articulate its opposition to Russia's two newest pipeline projects in Europe, the Nord Stream and South Stream pipelines. These gas conduits could increase Central Europe's vulnerability to Russian monopoly pressure.
- The United States should make clear to members of the "commercial opportunists" group that actions which undermine Western-backed diversification projects are unacceptable.
- Washington should speak out against Germany's special relationship with Russia in the energy sphere. Bringing about a sea change in Berlin could remove a major impediment to creating a common EU energy policy.
- U.S. decision makers should recognize the long-term role that EU-Iranian gas trade could play, under the right political circumstances, in diversifying Central Europe's energy mix. The United States should be prepared to drop its opposition to EU energy deals with Iran as part of a basket of incentives to get the Islamic Republic to cooperate on the nuclear issue.

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[1] Credit for the delineation of "strategic" vs. "opportunistic" policies is owed to Vladimir Socor. See: Panel Discussion, "Russia's Energy Policy and Strategy in Europe," Center for Strategic and International Studies, April 21, 2008, Washington, DC. Summary available at <http://www.csis.org/media/csis/events/080425_vladimir_socorreport.pdf>.

Introduction

"Those who control your energy supply control you politically. This is unacceptable."[2]

-- Valdas Adamkus, President of Lithuania, Berlin, July 11, 2006.

The ten countries of post-communist Central Europe are important U.S. partners on a number of levels. When the going gets tough, these allies' support can "tip the scales" in America's favor.[3] Yet Russian influence in the region looks set to make a come-back through the westward march of Russian energy companies.

Central Europe lies at the center of a game of post-Cold War competition between the West and Russia: the battle for control of energy resources feeding the European market. The continent's dependence on Russian gas supplies is for the most part concentrated within the former communist states of Central Europe. Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia are all members of both the European Union and NATO, but most are disproportionately exposed to Russia's energy monopoly. Gazprom, Russia's state-owned gas giant, supplies almost two-thirds of Central Europe's gas, compared with only 24 percent for the European Union (EU) as a whole.[4] There is a similar situation with respect to oil. Monopoly power of this kind runs counter to American interests because it places U.S. allies in a state of reliance upon the Kremlin's goodwill.

This in turn complicates America's interest in remaining a power in Europe. Against the backdrop of Russian resurgence, U.S. influence on the European continent is declining. A more robust European Union, public disenchantment with U.S. foreign policy in the wake of the Iraq war, and other factors combine to reduce the weight of America's voice in Europe. This is even true for traditionally Atlanticist "new Europe." It is in this context that Russia's renewed geopolitical sway – via its energy dominance – is particularly worrisome. The United States needs Central Europe as a military bridge to the Greater Middle East, a hub for U.S. business in Europe and as part of a "pro-America" caucus within the EU.[5] Unless something is done to minimize the political impact of Russian monopoly power, the Kremlin may effectively neutralize American influence within Central Europe and the EU as a whole.

The United States has recognized the dependency problem facing its allies in Central Europe, and has given its blessing to new pipelines and other projects aimed at diversifying the region's gas supplies. Sadly, there is no consensus within Central Europe as to the correct policy response vis-à-vis Russia's energy dominance. Observers sometimes wrongly generalize by suggesting that Central Europe and the United States

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[2] Quoted in: "Lithuania Slams Russian 'blackmail,'" *RFE/RL Newsline*, July 12, 2006.
[3] For an overview of the importance of the U.S.-Central European relationship, see: Wess Mitchell, "Tipping the Scales: Why Central Europe Matters to the United States," Center for European Policy Analysis, May 2006. Available at <http://www.cepa.org/file_download/CEPA_Tipping_the_Scales.pdf>.
[4] Eurostat (2006).
[5] For additional discussion of these points, see footnote no.3 above.

are on one side of the debate, with Western Europe on the other.[6] In fact, from a bird's eye view of the region, Central Europe looks bifurcated by an energy security schism.

In the absence of a common EU energy policy, the ten countries of Central Europe have adopted a diverse range of diplomatic and technical responses at the state-level to cope with energy reliance on Russia. In terms of a conceptual schism, these national responses can be lumped into two broad categories: "strategic thinking" and "commercial opportunism."[7] Those in the strategic camp – Poland, Lithuania, Estonia, Romania and the Czech Republic – complement American interests by working to mitigate Russian monopoly power by diversifying their energy mix. The commercial opportunists – Hungary, Slovakia, Bulgaria and (with caveats) Latvia and Slovenia – undermine the work of the first group through their willingness to strike long-term partnerships with Russian firms. At minimum, these policies are short-sighted. At maximum, the states on the opportunistic side of the schism can unwittingly become linchpins for Russian political and economic clout in Europe.

The first section of this paper elucidates more clearly the problem of Russia's energy grip, focusing primarily on natural gas due to Russia's dominant position and the nature of international gas markets. The second section explains the mosaic of Central European energy security policy responses in greater detail. The third section sheds some light on how and why the energy security schism within Central Europe appears to have deepened in recent years and offer insights for the road ahead. The fourth section explains how commercial opportunism complicates U.S. interests. Finally, the present analysis makes recommendations for American policymakers aimed at buttressing the energy security of key U.S. allies.

Three principal assumptions underlie this report: (1) Russian energy policies in Central Europe represent a legitimate source of concern in the region; (2) the EU's current disaggregated approach to Russia in the energy sphere is not desirable; and (3) because questions of energy security are wrapped up in issues of national sovereignty, the United States has an interest in helping Central Europe acquire greater freedom of maneuver in energy supplies. This paper argues that there is still more the United States can and should be doing in the contest with Russia over Central Europe's energy lifeblood.

Russia's Resurgence and its Energy Grip on Central Europe

Before delving into Central Europe's energy schism, it is necessary to understand the challenge presented by Russia's energy position and policies. Today's Russia is politically, economically and militarily resurgent, and increasingly assertive abroad. Though Moscow's present preoccupation is with the post-Soviet space (e.g. Ukraine, Georgia), Russia cannot ignore the area now known as Central Europe. Restoring Russia's voice within the geo-strategic triangle between the Baltic, Adriatic and Black Seas is essential for

[6] See Czech diplomat quoted in: David Francis, "NATO summit highlights U.S.-Europe divide on Russia," *Christian Science Monitor*, April 4, 2008.

[7] [7] Credit for the delineation of "strategic" vs. "opportunistic" policies is owed to Vladimir Socor. See: Panel Discussion,"Russia's Energy Policy and Strategy in Europe," Center for Strategic and International Studies, April 21, 2008, Washington, DC. Summary available at <http://www.csis.org/media/csis/events/080425_vladimir_socorreport.pdf>.

Russia's aspirations to be a major power on the European continent. The Russian strategy has been to expand the nation's economic reach into the Central European region in order to counter the expansion of Western influence accompanying NATO enlargement. And Russia's status as the principal supplier of fossil fuels to Central Europe offers an almost irresistible instrument for leverage.

The Kremlin's political wish-list as regards the Central European region includes the following:

- Restoring Russian diplomatic influence in the region to counterbalance perceived U.S. and NATO encroachment.
- Minimizing European criticism of Russian internal and external policies.
- Establishing a veto – formal or informal – over Central Europe's security arrangements (e.g. missile defense, further NATO enlargement).
- Minimizing Western involvement in Ukraine, Belarus and the Caucuses.
- Bringing the "frozen conflicts" on Europe's doorstep (e.g. Transnistria, Abkhazia) to an end only on Russia's terms.
- Encouraging the development of a "pro-Russia" caucus within the EU to neutralize those voices that traditionally run counter to Russian interests (e.g. Poland, Lithuania).

Central European Dependency on Russian Natural Gas

Country	2006 Natural Gas Consumption (bcm*)	2006 Imports of Russian Gas (bcm*)	2006 Share of Imports from Russia	2006 Share of Consumption from Russia
Bulgaria	3.63	3.26	100%	89.8%
Czech Republic	9.47	7.41	74%	78.2%
Estonia	1.01	1.01	100%	100%
Hungary	14.32	9.46	79.4%	66.1%
Latvia	1.76	1.91	100%	108.5%
Lithuania	3.07	3.10	100%	101%
Poland	15.47	7.69	68.8%	49.7%
Romania	18.26	5.63	94%	30.8%
Slovakia	6.72	7.11	100%	105.8%
Slovenia	1.12	0.57	50.9%	50.9%
CE-10	74.83	47.15	83.3%	63%
EU-27	547.42	132.40	31.8%	24.2%

Source: Eurostat. Consumption figures refer to gross inland consumption. Percentages in the right-hand column greater than 100 indicate in some cases Russian gas that is transited on to other countries.
*bcm refers to billion cubic meters.

Looking at the foreign policy toolkit available to Russian leaders, energy appears a choice vehicle to advance the items on this wish-list and make inroads into the "new West." First, few other countries can boast what Russia can: 25 percent of the world's natural gas reserves (the biggest share of any country), the seventh-largest oil reserves globally and an extensive pipeline network in Central and Eastern Europe.[8] The chart above outlines Central European dependency on Russian natural gas. Second, the Russian state plays a preponderant role in energy policy (especially when it comes to natural gas, where state-owned Gazprom rules the roost and is symbiotically tied to Kremlin elites). Such a set-up allows Russian policymakers to make use of the country's hydrocarbon stature for foreign policy purposes when and where possible. Russia also dominates on the oil front, but oil is much more of a fungible global commodity, and Russian state control over this resource is not as pronounced.

Besides, Russian military influence has clear limitations. Though Russia has been willing at times to exert implied military pressure in Central Europe (such as when it says it can target missiles towards proposed missile defense sites in Poland), there are unambiguous constraints on what Russia can actually do when push comes to shove. Why would Russia brandish military threats when the prospects of losing gas contracts, energy transit revenues or lucrative deals on infrastructure projects can, under the right circumstances, move a country to cater to Russian state interests?

Russia's infamous gas cut off to Ukraine on Jan. 1, 2006, served as a wakeup call to transatlantic decision makers, but it sometimes overshadows Russia's more covert energy imperialism in Central Europe. Leaving aside Russian attempts in the early 1990s to pressure the Baltic States over politics, Russia has for the most part sought to quietly penetrate countries in the region and place them in a state of dependency, rather than openly declare war via a supply disruption as Russian leaders did with Ukraine during the 1990s and into the 2000s.[9]

Of course no one can say for sure what the norm of Russian behavior will be moving forward. Analysts at the Swedish Defense Research Agency posit in a 2007 report that "NATO and EU membership is clearly not a barrier" against more coercive Russian policy in the future of one kind or another.[10] The authors suggest that it remains to be seen whether Russian policy in Central Europe will involve more arm-twisting in years ahead, pointing to last year's cyber-attack against Estonia[11] and the Russian boycott of Polish meat as incidents that could suggest a possible "new stage in Russia's use of leverage, one where the EU is in focus."[12] If true, any coercive use of energy towards EU or NATO

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[8] Rankings and percentages derived from: *BP Statistical Review of World Energy 2008*.

[9] Russia's decision to cut rail deliveries of oil to Estonia in the midst of a diplomatic row in April-May 2007, and Russia's still ongoing blockade of oil deliveries to Lithuania's sole refinery represent exceptions rather than the rule when it comes to Central Europe. For a more thorough treatment of Russia's use of energy as a policy lever in general see: Robert L. Larsson, *Russia's Energy Policy: Security Dimensions and Russia's Reliability as an Energy Supplier*, Stockhom: Swedish Defence Research Agency, March 2006; Jakob Hedenskog and Robert L. Larsson, *Russian Leverage on the CIS and the Baltic States*, Stockholm: Swedish Defence Research Agency, June 2007.

[10] Jakob Hedenskog and Robert L. Larsson, *Russian Leverage on the CIS and the Baltic States*, Stockhom: Swedish Defence Research Agency, June 2007, p.116.

[11] The extent of the Russian government's involvement in this incident remains unclear at the time of this writing.

[12] Jakob Hedenskog and Robert L. Larsson, *Russian Leverage on the CIS and the Baltic States*, Swedish Defence Research Agency: Stockhom, June 2007, p.116.

members will likely start in Central Europe. But for the time being, as Hungarian analyst Dr. Anita Orbán explains, the risks from Russian energy policy will be more subtle:

> "The next phase of this energy crisis in Europe will not appear with a big bang, like the 2006 'cut off' in Ukraine. Rather, it will continue to persist with a long drawn-out whimper, with Central and East European members of the [NATO] Alliance being drawn further into Russia's 'Energy Empire.'"[13]

This so-called energy empire is often a subtle imperium – a point that should be stressed. Too often, pundits keen to highlight the dangers of Russia's energy monopoly for Central Europe do their cause a disservice by not choosing their words more carefully. By over-hyping the risks associated with Gazprom, for instance, Central Europe's friends in the United States can inadvertently make it easier for the company's PR hacks to pick apart their arguments and advance the case that Gazprom policies are simply smart business decisions.[14]

Talk of Russia's "energy weapon" evokes images of Russia shutting off the gas to one or more European countries lest they side against Moscow on an international issue. A supply disruption of this kind is a legitimate concern and is not impossible. Indeed, it is possible that Russia has already used its oil wealth to pressure the Czech Republic over missile defense; as this paper went to print, Russia announced that it would be forced to reduce deliveries of oil to the Czech Republic due to technical reasons. But the timing of this announcement was suspicious; it took place only days after leaders in Prague signed a missile defense-related agreement with the United States.[15]

Turning back to natural gas, it should be realized that Gazprom under Vladimir Putin (or his successor, Dmitry Medvedev) has, to date, never closed its pipes to any European gas consumer that has paid its bills on time.[16] Non-payment issues do not justify the use of heavy-handed tactics against countries with pro-Western governments in the dead of winter (like Ukraine), but they do provide a useful pretext for getting away with it. If Kremlin leaders are rational, then they should understand that crossing the threshold and treating a paying customer in the same fashion Gazprom has dealt with Ukraine would be risky from both a political and a business standpoint. At the end of the day, Russia has both its export revenues and commercial reputation to consider.

Though Russia is constrained in shutting off the gas does not mean that Russia cannot leverage its hydrocarbon wealth to gain geopolitical influence over U.S. allies. Far from it, the Russians have a number of tools at their disposal short of an actual supply interruption. Russian energy policy consists of intelligent and crafty imperialism, where

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[13] Anita Orbán, Deputy Director, International Centre for Democratic Transition, Budapest, Hungary, "NATO's Missed Opportunity," Unpublished Essay, April 2008. Dr. Orbán is the author of *Power, Energy and the New Russian Imperialism*, Praeger, 2008, forthcoming.

[14] The Kremlin and Gazprom are engaged in a major PR offensive in the West. See for example: Peter Finn, "Russia Pumps Tens of Millions Into Burnishing Image Abroad," *The Washington Post*, March 6, 2008; "Ketchum Caught 'Man of the Year,'" *O'Dwer's PR Daily*, Feb. 20, 2008. Portions of article cited online, available at <http://www.prwatch.org/node/7021>.

[15] Judy Dempsey, "Energy cuts 'not political,' Russia says; Technical woes cited on Czech deliveries," *International Herald Tribune*, July 15, 2008.

[16] Clearly, countries in Central Europe have experienced supply disruptions as a result of Russian gas disputes with Ukraine and Belarus, but in these cases the Central Europeans were not the intended targets; they were collateral damage.

energy is relied upon as a stick, a carrot and a shield all at once, but not so much an offensive weapon.

As a stick, Russia's energy influence can be operationalized through so-called "contractual re-evaluations." Russia's gas contracts are done on a bilateral basis, rather than with the European Commission. Russia prefers it this way in order to maximize its leverage and undermine attempts at EU unity. As industry analyst Paul Domjan put it, "Russia is trying to segment the European market through sweetheart deals with key countries."[17] Gazprom is able to exploit jitters about ensuring future energy supplies, creating something of a "chicken and egg" problem; European nations feel the need to strike long-term bilateral deals with Gazprom to guard against becoming left out – even if they don't see dependence on Russia as desirable. Though bilateral contracts are sacred in principle, they are often re-negotiated in practice. Every now and then, Russia makes use of aggressive negotiating tactics in the midst of contractual talks to boost its monopoly position. The following recent cases offer a telling snapshot:

- In 2006, Bulgaria was afraid that if it didn't sign a deal with Gazprom on other energy-related matters then it would lose its contracted gas supplies.[18]
- In 2007, it seemed that Slovakia was giving up on attempts to recover from Russian firms a 49 percent stake in Transpetrol – Slovakia's oil pipeline operator – in exchange for a Russian commitment to supply the country with energy through 2014.[19]
- In 2007, Russia's Ambassador to Hungary Igor Savolskiy issued what could be perceived as a threat in response to suggestions that Russian energy policies were not market-oriented. "If the Hungarian market becomes uncertain, even for domestic political reasons, Russia will look for another more secure market. Are we understood?"[20]
- In late 2007, head of the energy department at the German Institute for Economic Research Claudia Kempfert argued that Gazprom's price hike for many of its European customers for 2007-08 was in part a political tactic to pressure the EU on its energy sector reforms. "The price hike announced by Gazprom cannot be explained by higher oil prices alone, but is partly politically motivated," she claimed. "Gazprom is angry at the EU because Brussels talks about unbundling and liberalization, while trying to introduce special laws preventing Gazprom from entering the European market."[21] Even if one disagrees with Kempfert's assessment of the rise in gas prices, it is not hard to imagine a scenario where Russia puts forward a sharper price increase to leverage a political or commercial concession.

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[17] Paul Domjan, senior consultant at John Howell and Co., quoted in: "Dreams of gas hubs," *Petroleum Economist*, April 2007.
[18] "Bulgaria-Russia Gazprom deal signed," *United Press International*, Dec. 18, 2006.
[19] "Slovakia's PM discusses oil and gas issues with Russian President," *SKRIN Market & Corporate News*, May 8, 2007.According to some reports, Polish firms are also interested in buying the pipeline stake, an idea likely to ruffle some feathers in Moscow. See: Daniela Krajanova, "Fico denies Russian media reports, but only in Slovakia," Sme (Bratislava), BBC Monitoring Reports, April 11, 2008.
[20] Russian Ambassador Igor Savolskiy quoted in: "Russian envoy on Hungary joining gas pipe project, energy security, Kosovo," *Nepszabadsag*, BBC Monitoring Reports, March 3, 2008.
[21] Claudia Kempfert quoted in: "Gazprom Warns Europe of Impending Price Rise," *European Gas Markets*, Nov. 30, 2007.

Notably, such contractual disputes do not provoke the outrage that one saw during the 2006 cutoff of gas to Ukraine; this makes them more subtle forms of pressure.

In theory, Russia could use a scarcity of gas supplies as an excuse to re-open negotiations on a number of its contracts with European customers to pressure select countries on foreign policy issues and expand its energy monopoly power over these states. A key driver opening up such possibilities is Gazprom's likely gas shortfall. Rather than investing in future gas production, the Russian company has been pouring its cash into Europe's downstream (by buying pipelines, distribution networks and storage facilities).[22] One worrisome consequence of this asset acquisition is a potential increase in Russian political and economic influence, as will be discussed below. But the first point to be emphasized is that a lack of upstream investment in recent years, combined with rising gas consumption within Russia, will likely result in a serious gap between Europe's expected import volumes from Russia and Gazprom's ability to export.[23]

Despite this upcoming gas deficit, Gazprom continues ahead with plans to build additional pipelines in the Baltic and Black Seas. In the North, Russian President Vladimir Putin teamed up with then German Chancellor Gerhardt Schröder in 2005 to ink a deal for the "Nord Stream" project. Nord Stream plans two parallel pipelines with a combined annual capacity of 55 billion cubic meters (bcm) under the Baltic Sea from Russia's terminal at Vyborg to German markets – bypassing Estonia, Latvia, Lithuania and Poland. In the South, Gazprom is partnering with Italy's Eni for its project "South Stream," which, if built, would send 30 bcm per year under the Black Sea to Bulgaria, and from there to Italy and Austria through a number of Central and Southeast European transit states.

Why would the Russians be building so much more export capacity when they expect to have less gas? If it is supposed to be a joke, it is not amusing; being locked into long-term contracts for Russian gas, Gazprom's customers have less of an incentive to diversify away from Russia as a supplier or move away from gas as a fuel. Clearly, part of Russian strategy is to undercut projects promoted by the United States and its allies, like the proposed Nabucco pipeline through Turkey. Another element of Russian strategy is to bypass Ukraine (considered by Russia as an unreliable transit state) and, to a lesser extent, Belarus. But there may be more going on here than simply avoiding transit risk. For instance, it's not necessary for Nord Stream to pass under the Baltic Sea just to bypass Belarus; the pipeline could easily take an overland route to Germany through Poland and the Baltic States through the proposed "Amber Stream" pipeline.[24] But what Nord Stream's planned route can provide is an ability to circumvent these Central European states should the Kremlin desire. So it's possible that Russian leaders would like to make the best out of a paucity of gas by gaining increased control over energy flows to European customers.

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[22] Oxford Analytica, "RUSSIA: Gazprom investment," April 23, 2008. Available at <http://www.iht.com/articles/2008/04/23/news/23oxan-gazprom.php>.

[23] Some say the gap between Gazprom's supply commitments and its actual production could reach 100 bcm per year. See: Michael Fredholm, Conflict Studies Research Centre, Speech before the Vilnius Energy Security Conference, "The Impact of Russia's Emerging Natural Gas Deficit on European Energy Security," Oct. 11, 2007, Vilnius, Lithuania.

[24] See: Presentation by Dariusz Bogdan, Undersecretary of State, Polish Ministry of Economy, Conference at the Johns Hopkins University-SAIS: "Energy Geopolitics in Central Europe," Panel I: "Competing Pipelines in Central Europe," June 23, 2008, Washington, DC. Available at <http://www.cepa.org/events/Bogdan_EnergyPresentation062308.pdf>.

Right now, Russian leverage via contractual reevaluations is constrained by a limited number of pipeline routes to Europe. Russia has two main gas conduits to Europe: the "Yamal" line through Belarus and Poland and the "Druzhba" ("Friendship") system through Ukraine and Slovakia (in addition to the smaller "Progress" route via Romania). But added pipeline choice in the form of Nord Stream and South Stream – as well as any future pipelines – could give Moscow even greater command over how gas supplies and transit revenues are distributed to countries in the region. In other words, Russia could gain more wiggle room with respect to Central European customers. It is here that the lines between business and politics get blurry.

Another potential benefit Russia could derive from added export capacity amid scarcer supplies would be an improved capacity to set up a gas cartel for Europe. Pundits often shoot themselves in the foot when they use the term "gas OPEC"; gas markets cannot be influenced in the same way that OPEC nations shape the market for crude oil. However, what Russia could do is coordinate with other gas producers to divide up European and Eurasian markets and reach understandings on delivery volumes to specific locations.[25] In theory, new pipelines such as South Stream could allow Russia to control the delivery of Caspian or even Middle Eastern gas to Europe.[26] Regardless of whether a gas cartel materializes, new pipeline capacity with less gas could lay the groundwork for a resurgence of Russian pressure on Central European states via a manipulation of bilateral gas contracts.

Energy carrots are even easier to wield. Carrots in this case constitute pipelines and energy distribution hubs that not only extend the reach of Russian energy companies but also offer attractive business ventures for other countries. Putin has boasted about the seductive quality that Russian energy carrots can have for Central European capitals. "There is a tough struggle among European nations for Russia to build such transportation networks… We don't need to convince anyone; they are pleading for us for that every day, especially in the autumn and winter period."[27]

The Kremlin correctly views Central Europe not as a bloc, but as a political montage. On one hand, Russia perceives many of its former satellites, such as those in the Baltic region, as a gang of Russophobic trouble-makers that should be marginalized. Lithuania's recent willingness to block EU talks with Moscow on a new Partnership and Cooperation Agreement (PCA) reinforces this thinking.[28] At the same time, Russia gets along more cozily with other countries, in particular Slovakia, Hungary and Bulgaria. Because Central Europe is divided, not united, in its approach to Russia, Kremlin elites need ways to distinguish between friend and foe.

In years past, Russia provided carrots in the form of gas subsides to those states it considered more or less "pro-Moscow" in the Commonwealth of Independent States (CIS). Raising the price of exports to all its foreign customers, Russia has settled on a

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[25] Vladimir Socor, "Gazprom, the Prospects of a Gas Cartel, and Europe's Energy Security," in Svante E. Cornell and Niklas Nilsson (eds), *Europe's Energy Security: Gazprom's Dominance and Caspian Supply Alternatives*, Central Asia - Caucus Institute & Silk Road Studies Program, 2008, pp.74-75, 78.

[26] Vladimir Socor, "Gazprom's South Stream Project Can Be Halted in the Black Sea," *Eurasia Daily Monitor*, March 6, 2008.

[27] Putin quoted in: Vladimir Isachenkov, "Russia, Bulgaria sign Pipeline Deal, tightening Moscow's grip on European energy supplies," *Associated Press*, Jan. 18, 2008.

[28] For background on this item see: Ryan R. Miller, "Lithuania's Lonely Gambit," *Central Europe Digest*, May 15, 2008.

policy of "friends-in-transit" as a new way to hand out carrots. As part of this strategy, Russia will route its pipelines and establish gas distribution hubs in those states considered as "friendlies," disbursing transit revenues and capital investment. Such goodies are more of a privilege than a right, and in practice this approach rewards states that cooperate with Moscow while punishing those critical of Russian policy.

Withdrawing carrots as a tactic is most clearly seen with oil in the Baltic region. Once a major export hub for Russian oil destined for tankers on the Baltic Sea, Russia has been scaling back its use of Estonian and Latvian terminals in favor of a port Russia is upgrading at Primorsk.[29] Estonia was in recent years a major export hub, handling 500,000 barrels of Russian oil per day.[30] However, following the Russo-Estonian spat over a Soviet war memorial in 2007 the Russians have slashed back on exports through Estonia.[31] Despondent, Estonia's Economy Minister has stated that it is perhaps time for his country to find new things to trade.[32]

Russia has in some cases played countries in the region against each other. For instance, after momentum began to build for extending Ukraine's Odessa-Brody oil pipeline to Poland to bring non-Russian crude to the Baltic region, Moscow proposed connecting the line instead to Slovakia-bound Russian pipelines. Such a proposal would set Poland and Slovakia – who would benefit from the added transit role – in opposition to one another.[33]

There are also signs of transit preference when it comes to gas. South Stream would go through states viewed in Moscow as reliable Russian partners at the diplomatic and political level: Greece, Bulgaria, Serbia, Hungary, Slovenia and Austria. In April 2008, Russia showed signs of using Slovenia as a bargaining chip with Austria; some might say that Moscow effectively held out the possibility that South Stream could pass through the former Yugoslav republic and cut Austria out of the picture.[34] At the time, it looked possible that Gazprom was leveraging its Slovenia option to pressure Vienna into signing a deal that would expand the Russian company's presence in the Austrian energy sector.[35] Such tactics are similar to those used with respect to Serbia in January 2008, when Russia promised that South Stream's main line would pass through Serbian territory only after Belgrade had committed to selling 51 percent of its state oil company to Gazprom.[36]

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[29] "Russian Oil Exports," U.S. Energy Information Administration. Available at <http://www.eia.doe.gov/emeu/cabs/Russia/Oil_exports.html>.
[30] "Baltic Sea Regional Fact Sheet," Country Analysis Briefs, U.S. Energy Information Administration. Available at <http://www.eia.doe.gov/emeu/cabs/Baltic/Oil.html>.
[31] Laura Sheeter, "Russia's oil trade shuns Estonian ports," *BBC News*, Dec. 19, 2007. Available at <http://news.bbc.co.uk/2/hi/business/7149573.stm>.
[32] Ibid.
[33] Remarks by Anita Orbán, Conference co-sponsored by The Harvard Ukrainian Research Institute and The Davis Center for Russian and Eurasian Studies, "Session 3. From Producer to Consumer: Pricing Mechanisms, Transit, and Informal Institutions," March 8, 2008, Cambridge, Massachusetts.
[34] At the time of this writing, however, South Stream seems to have committed to both Slovenia and Austria. For background see: "Gazprom Says Gas Pipeline to Cross Slovenia," Slovene news agency STA, BBC Monitoring Reports, June 10, 2008; "Gazprom, Austria to sign deal on South Stream project," *RosBusinessConsulting*, June 9, 2008; "Austria may be excluded from South Stream project and the gas pipeline may be built to Italy via Slovenia," *The Russian Oil and Gas Report* (Russia), April 16, 2008.
[35] "Austria drops out of "South Stream," *Integrum*, April 14, 2008. Available at <http://www.integrum.com/ArticlesByCategoryPage.aspx?oid=219>.
[36] "Serbia to sell controlling stake in NIS to Gazprom Neft," *EIU ViewsWire Select*, Jan. 30, 2008.

Russian officials must take a certain cruel satisfaction in watching Central Europeans vie for transit revenues from Russian energy projects. Speaking about South Stream, Russia's Ambassador to Hungary Savolskiy put it like this: "the choice was pretty simple: Will the gas reach Austria through Hungary or by bypassing it?" He added, "I would be interested to know whether there is a country whose government would voluntarily decline that income [from transit revenues]."[37]

Notably, the South Stream pipeline avoids Romania, which has taken a more critical line against Russian foreign policy and has been a more stalwart supporter of European attempts to diversify away from Russia's energy monopoly by accessing Caspian oil and gas. In theory, Gazprom could use South Stream to obviate the need for Romania as a transit state. Currently, Romania is a transit state for Russian gas en route to the two Balkan countries through the Progress pipeline. But with South Stream in place, Russia could withdraw energy carrots that currently flow to Bucharest.

Looking ahead, it is also possible that Russia could stop transiting energy through Poland. At present, about 20 percent of Russian gas exports to Europe is pumped through Polish territory to Germany through the Yamal-Europe line. But now Gazprom intends to circumvent Poland with its Nord Stream pipeline. Gazprom in 2006 said it would not build a previously-planned second stretch of Yamal, as Nord Stream became the preferred option from Russia's perspective. Conceivably, the Russian gas giant could use the undersea pipeline to threaten a cessation of gas transit through Poland, unless perhaps Warsaw compromises on other matters – such as missile defense. The bottom line is that energy can provide Russia with a vehicle for influence over U.S. allies even without the threat of a supply interruption.

Furthermore, it should be recognized that energy can be used as a "shield," rather than a sword. In practice, dependence any energy supplier can create an incentive to shy away from criticizing its domestic or international policies. As former advisor in the British Foreign Office David Clark once said,

> "I do not believe in the Pearl Harbor scenario where Europe suddenly becomes completely dependent on Gazprom and the Kremlin shouts 'Gotcha'; it's more subtle than that… I do think there is a process of Finlandization going on under which European politicians will eventually end up realizing it is not in their interests to get on the wrong side of the Kremlin."[38]

In a sense, Russia might not have to do anything; it can sit back, conscious of the fact that its customers know they are dependent upon Russian energy, and let outcomes speak for themselves. Arguably, this has already started to happen. Gazprom's biggest customers in Europe, Germany and Italy, have been noticeably reserved in their criticism of Russia and have sided with Moscow on issues like the question of whether or not to extend Membership Action Plans (known as MAP) to Ukraine or Georgia. It is interesting that Hungary, Gazprom's most important customer in Central Europe, and a country which

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[37] Russian ambassador Igor Savolskiy quoted in: "Russian envoy on Hungary joining gas pipe project, energy security, Kosovo," *Nepszabadsag*, BBC Monitoring Reports, March 3, 2008.

[38] David Clark quoted in: Terry Mecalister, "The energy empire: Russia's power play in Europe," *The Guardian*, April 12, 2007.

depends on Russian gas for a huge chunk of its energy mix, was the sole member of "new Europe" that wavered in supporting MAP for the two NATO candidates.[39] Russia's energy shield may or may not have played a role in Budapest's reluctance, but it does raise eyebrows.

Russia boosts its energy shield strength by aggressively buying into European energy infrastructure. Since Putin was elected in 2000, Russia stepped up its pace of asset acquisition. In February 2008, EU foreign policy chief Javier Solana said, "sometimes I think Russia is investing in future leverages instead of future production."[40] In the gas sector, Gazprom – Russia's largest foreign investor[41] – has in recent years been aggressively pursuing ownership of key energy assets in EU states. Russian energy companies generally take a first step of buying a blocking minority in a local company (25 percent plus one share).[42] For instance, at the time of this writing, Gazprom looks set to invest in a new natural gas-fired power plant in Latvia, but only if the company is awarded a blocking stake.[43]

On occasion, Russia resorts to covert tactics in its efforts to secure control of the region's energy sector. Some suspect that Gazprom is keen to acquire downstream assets of MOL, the Hungarian national oil company (and manager of the country's gas distribution network), by collaborating with Austria's OMV in its hostile takeover bid for the Hungarian firm.[44] Rome-based energy analyst Federico Bordonaro notes how Russia could benefit from the takeover: "If Austria enters Gazprom's orbit, and then if the Austrian major [OMV] takes over the Hungarian major [MOL], then it is like you scored two goals with only one strike. Then, via Austria, you also control Hungary."[45] Some experts fear that, by acquiring large parts of MOL, Gazprom could leverage the political influence that comes with owning large chunks of Hungary's energy sector to increase Hungarian reliance on Russian energy[46] - thus perpetuating a state of dependence for the Central European country.

Indeed, energy dominance by Russia can lead to the establishment of business lobbies in certain cases that stick up for Russian political and economic interests. Edward Lucas of *The Economist* describes how energy trade with Russia can in some instances blunt criticism of Russian policies:

> "Typically, the first stage is characterized by an acceptance, and then a dependence, on Russian gas supplies delivered along Russian-controlled pipelines. Next the country may allow Russian energy giants to buy assets such as

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[39] "Hungarian MP Backs Ukraine, Georgia Bid to Join NATO Membership Plan," Nepszabadsag website, BBC Monitoring Reports, April 3, 2008; "Central European countries back Ukraine's, Georgia's NATO aspirations," CTK news agency, BBC Monitoring Reports, April 23, 2008.
[40] Solana quoted in: Judy Dempsey, "Russia Proposes New U.S. Dialogue," *International Herald Tribune*, Feb. 10, 2008.
[41] Agata Łoskot-Strachota, "The Russian Oil and Gas for Europe," Centre for Eastern Studies (Warsaw), Oct. 2006, p.13.
[42] Keith Smith, *Russian Energy Politics in the Baltics, Poland, and Ukraine: A New Stealth Imperialism?*, Washington, DC: Center for Strategic and International Studies, Dec. 2004, p.7; "Gazprom seeks blocking stake in Latvian gas-fired power plant," *Russia & CIS Business and Financial Newswire*, April 7, 2008.
[43] "Gazprom eyes Latvia Plant," *International Oil Daily*, April 8, 2008.
[44] "Hungary: Gazprom's Subtle Attempt to Take Over MOL," Stratfor, July 5, 2007; Vladimir Socor, "Gazprom Takeover in Hungary Looms Behind Possible OMV Takeover," *Eurasia Daily Monitor*, July 25, 2007.
[45] Quoted in: "Russia: Gazprom's Advance Into Europe Continues," *RFE/RL*, Jan. 25, 2008.
[46] Zeyno Baran, Testimony before the U.S. House of Representatives, Foreign Affairs Committee, "Central and Eastern Europe: Assessing the Democratic Transition," July 25, 2007, Washington, DC.

> refineries and distribution companies. That soon creates a powerful local lobby for good relations with Russia, and unwillingness to defend those being bullied or browbeaten elsewhere."[47]

Though Germany (and in particular former Chancellor Gerhardt Schröder) could be said to have fallen prey to Russia's energy charm, Berlin is not the only European capital that Russia courts via energy relationships. For instance, Lukoil's President, Vagit Alekperov, remarked in 2001 that he was "certain that Bulgaria, whose oil sector is almost entirely owned by Russian companies, will not conduct an anti-Russian foreign policy in the foreseeable future."[48] Some Bulgarian scholars claim that Russian companies have mastered the art of "informal personal influencing" of public officials in countries like Bulgaria.[49]

Some in Lithuania feel that Russian energy cabals use shady intermediaries to dole out funds to political allies in the country, creating a sense of corruption and state capture.[50] In neighboring Latvia, there are also warning signs of Russian energy influence. A former Latvian Foreign Minister remarked this year that "Russian money is returning, and sooner or later it will demand its place in Latvian politics."[51] Gazprom owns a hefty one-third of the Latvian gas utility,[52] helping to cement Russian influence over the country's energy sector. Vaira Paegle, Chairwoman of the Latvian Parliament's European Affairs Commission notes the presence of "Gazprom politicians" in Latvia; those inclined to "base foreign policy on the possible economic benefits that might be gained."[53]

A local business presence of Russian energy firms can also undermine attempts at supply diversification. A Czech Foreign Ministry paper leaked to the press in 2007 suggested that Gazprom could try to acquire the Czech Republic's Transgas, which is controlled by a German firm. Gazprom could then leverage this company to deny the Czech Republic gas deliveries from Norway – the country's main alternative supplier.[54]

There are different points of view on what drives Russian policy. Aside from the power considerations presented here, some argue that Gazprom policy can be explained largely by corporate logic. The argument is that Gazprom is a monopoly, and so naturally seeks to maximize its profits and market share. To do this, it follows the monopolist's playbook

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[47] Edward Lucas, *The New Cold War: Putin's Russia and the Threat to the West*, London: Palgrave MacMillan, 2008, p.15.
[48] Quoted in: Fiona Hill, "Beyond Co-Dependency: European Reliance on Russian Energy," *U.S.-Europe Analysis*, The Brookings Institution, Washington, DC, July 2005.
[49] Ognyan Minchev, director of the Sofia-based Institute for Regional and International Studies, quoted in: Matthew Brunwasser, "Nuclear ambitions fan controversy in Bulgaria," *International Herald Tribune*, Oct. 30, 2007.
[50] See the following: "How Grupa Lotos Backed Its Rival and Lost a Big Tender," *Polish News Bulletin*, Oct. 11, 2007; Audrius Baciulis, "Kirkilas's Entourage," *Veidas*, BBC Monitoring Reports, Oct. 4, 2007; Laurynas Kasciunas, "Membership in NATO and EU: Has Lithuania Become Safe?," *Veidas*, BBC Monitoring Reports, August 23, 2007; Arturas Racas, "Dujotekana Rules!!!," Lithuanian news website Alfa, BBC Monitoring Reports, Sept. 1, 2007; Gediminas Stanisauskas, "Fugitive's Hope – Gazprom," *Kauno Diena*, Sept. 20, 2007; Audricis Baciulis, "Energy Is Russia's Trojan Horse in Lithuania," *Veidas*, BBC Monitoring Reports, Nov. 29, 2007.
[51] Commentary by former Latvian Foreign Minister Artis Pabriks, "Russia Returning Faster to Our Country Than We are Returning to Europe," *Diena website*, BBC Monitoring Reports, April 14, 2008.
[52] Agata Loskot-Strachota and Kataryna Pełczyńska-Nałęcz, "Gazprom's Expansion in the EU – Co-operation or domination?," Centre for Eastern Studies (Warsaw), April 2008, p.13. Available at <http://www.osw.waw.pl/files/GP_EU_en.pdf>.
[53] "Latvian MP discusses relations with Russia, United States," *Latvijas Avise*, BBC Monitoring Reports, April 21, 2008.
[54] "Czech Republic must focus on long-term energy security, reduce Russian reliance – special envoy," *Czech Republic and Slovakia Business Weekly*, Jan. 22, 2007.

by locking in customers and derailing competition, which is nothing more than how business is done. A third viewpoint presents the personal interests of individuals tied to the Putin-Medvedev entourage as a prime consideration in Gazprom's march westward. According to this line of reasoning, national champions in the energy sector offer a way for members of the Kremlin elite to fatten their pocketbooks.

One should note that these three considerations are not mutually exclusive. But more importantly, it might not matter from a U.S. policy perspective. Regardless of whether power, profits or pocketbooks underpin Russian strategy, it does not immediately follow that the answer should drive a policy response. The domination of one's energy sector by a foreign state-owned entity represents a danger to be avoided, regardless of what considerations (political, corporate or personal) brought about such a state of affairs. Military analysts typically look at capabilities, not intentions. Should the Kremlin and Gazprom set the board in their favor, it will be up to them to decide what to do with such muscle.

In sum, a nuanced discussion of Russian energy and Central Europe highlights the risks involved in Russia's "energy grip," rather than its "weapon." This grip is essential for securing influence over Central European countries, both *directly*, through state-to-state understandings on energy deals, and *indirectly* via the creation of business lobbies. Sadly, not all countries in Central Europe are working to tackle the problem.

The Schism Sketched Out: Central European Energy Security Policies

A key premise of this analysis is that Russia's excessive energy market share in Central Europe should be reduced. This report therefore considers that an ideal national strategy for a Central European state would be to do the following: (1) aim at diversifying the region's energy supplies away from Russian-controlled sources of energy; (2) express solidarity with those committed to diversification measures; and (3) actively support a common EU energy policy vis-à-vis Russia. Those states most committed to this side of the spectrum include Poland, Lithuania, Estonia, Romania and the Czech Republic.

On the other side are those classified in this report as "commercial opportunists." Their approach consists of making little or no attempt to diversify away from Russian energy, and simultaneously offering oneself as a "strategic partner" for Russian state-owned energy companies – to reap as many economic benefits as possible. Rome-based energy analyst Federico Bordonaro once noted that small states that function as energy corridors are "especially sensitive to the influence of big powers."[55] While Bordonaro was referring to Azerbaijan and Georgia, the same could also be said of states like Hungary. In effect, certain states rely on foreign policy (in the form of cozying up to Moscow) to keep themselves off the receiving end of Russian pressure. This group includes Bulgaria, Slovakia and Hungary. Latvia and Slovenia can be thought of as "swing states"[56] that could go either way, but have been included into the opportunists' category because of

[55] Quoted in: Brian Whitmore, "Looking For Ways To Circumvent Russia," *RFE/RL*, March 23, 2007.
[56] As far as I am aware, Edward Lucas coined the phrase "swing states" to refer to those states in Central and Eastern Europe where the West and Russia are competing for influence today. See: Edward Lucas, "A gloomy upshot," *The Economist*, Jan. 24, 2008.

recent developments. As Poland has historically been a trend-setter for the Central European region, we will start by looking at energy security through Warsaw's eyes.

Poland: A Regional Leader on Energy Security

The response coming from Poland is one of supply diversification "tous azimuts" and active defiance of Russia's energy monopoly. Summing up the Polish position, President Lech Kaczyński has declared to his European partners that "it is in our common interest that [Russian companies] Lukoil and Gazprom should function but should not become dominant."[57] So from the Polish perspective, energy security means a "basic level of independence that will allow us to make choices," in the words of Prime Minister Donald Tusk.[58] To this end, Poland actively supports three specific infrastructure projects to acquire alternative source of supply: (1) The Baltic Pipe – an undersea gas pipeline designed to connect Poland to Scandinavia's gas deposits; (2) a planned liquefied natural gas (LNG) terminal on Poland's Baltic coast to import non-Russian supplies by sea; and (3) the Odessa-Brody oil pipeline via Ukraine that intends to bring Caspian oil to Baltic markets without reliance on Russian transit. Under the previous government of the President's brother, Jarosław Kaczyński, Poland aggressively pushed on these items. At the time of this writing, the current Tusk government and the relevant state-owned companies continue to support all of these projects.[59]

In a way, Poland's opposition to Russian energy ambitions is disproportionate to its actual vulnerability. Thanks to some domestic gas supplies, Poland has some flexibility in terms of supply choices. Additionally, natural gas makes up only 13 percent of Poland's Total Primary Energy Supply (TPES); Poland has tremendous coal reserves, which provide for roughly 60 percent of the country's energy.[60] Poland also has the safety blanket of being a transit state for Russian energy supplies en route to Europe (about one-fifth of Russia's gas exports to Europe flow through the Yamal-Europe line). For the time being, any supply interruption directed against Poland would risk affecting Gazprom's hard currency customers in Germany. Nevertheless, the Polish elite is wary of Russian energy influence.

A key source of concern is Russia's planned Nord Stream pipeline in the Baltic Sea. In 2006, Poland's then Defense Minister (and current Foreign Minister) Radosław Sikorski compared the Russo-German deal to the 1939 Molotov-Ribbentrop pact in which Hitler and Stalin divided up Eastern Europe.[61] Some in Poland harbor suspicions that Russia could use this new gas conduit to manipulate the country's gas deliveries while supplying Germany (Russia's most important customer) at the same time. It is also possible that

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[57] Interview with Polish President Lech Kaczynski by Gabor Stier, "Different Approach to Russia Is a Rift – President Lech Kaczynski on Prospects of Cooperation, Need to Overcome Past, Changes in Polish Foreign Policy," *Magyar Nemzet*, BBC Monitoring Reports, March 29, 2008.

[58] "Exclusive Interview with Polish Prime Minister Donald Tusk for Interfax ahead of visit to Moscow," *Poland Business Newswire*, Feb. 6, 2008.

[59] Zoe Grainge, "New PGNiG Board to Continue Diversification Projects, Regulator Grants 14.3% Tariff Rise," *Global Insight*, April 14, 2008; "Poland to speak with single voice during upcoming energy summit in Ukraine - Polish PM," *Poland Business Newswire*, May 13, 2008; "Polish gas monopolist PGNiG's Q1 2008 results support continuation of major investments," *Poland Business Newswire*, May 14, 2008.

[60] Data is from 2004. See: "Poland - Energy Mix Fact Sheet," European Commission, January 2007. Available at <http://ec.europa.eu/energy/energy_policy/doc/factsheets/mix/mix_pl_en.pdf>.

[61] "Polish DM Likens Pipeline Deal to Nazi-Soviet Pact," *RFE-RL*, April 30, 2006.

Russia simply wants to stop transiting gas through Poland to deny the Polish state any positive economic benefits from its relations with Russia. Warsaw continues to argue that an overland route to Germany through Estonia, Latvia, Lithuania and Poland would make more sense. [62]

Diplomatically, Poland has called for a greater multilateral approach to energy security. In EU circles, Sikorski characterizes Poland's position on energy as "more communautaire" than that of many other European capitals.[63] Polish Members of Parliament (MPs) proposed an energy solidarity clause for the EU's new constitution to absorb the blow of any political suspension of energy supplies.[64] Polish officials said that MPs, President Kaczyński and the government strongly lobbied that EU language regarding a common energy policy be included in the Reform Treaty.[65]

Poland has been assertive in EU circles as to its preferred European approach to Russia. In particular, the Polish state favors a more robust external dimension to the EU's energy security competence. According to Tusk, "what Poland is interested in is that the high representative for common foreign policy also takes responsibility for energy policy."[66] In recent years, Warsaw proposed that the EU write a clause into any new Partnership and Cooperation Agreement (PCA) with Russia that would make unilateral decisions on energy deliveries unacceptable.[67] In 2006-07, Poland threatened to veto talks with the Russians over a new agreement unless Russia ratified the Energy Charter Treaty (ECT) and signed the ECT's Transit Protocol – measures which would force Russia to accept greater levels of competition and transparency in its energy policies.[68] Since that time, Poland has climbed down from this position, but only dropped its opposition to talks moving forward once Polish-Russian meat disputes were resolved and Warsaw got a commitment that any EU mandate for PCA talks would include the issue of energy security.[69]

Following the 2006 Ukraine gas crisis, President Kaczyński presented EU leaders with a proposal for a European energy security treaty. The plan included a provision not unlike NATO's Article V (the alliance's collective defense clause), calling for an agreement under which signatories would support each other "in the event of a threat to their energy security from natural or political causes."[70] Such ideas never acquired broad support in Brussels.

Parallel to its efforts to "Europeanize" questions of energy security, Warsaw has worked to form ad-hoc coalitions with like-minded states within Central Europe. In particular, Warsaw has joined the Baltic States in calling for greater EU cohesion on energy

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[62] "Overland pipeline may be preferable to Nord Steam – Polish minister," *Russia & CIS Business and Financial Newswire*, Dec. 12, 2007; "Polish Foreign Minister: Moscow worried about Baltic pipeline costs," *Deutsche Presse Agentur*, Jan. 23, 2008; "Poland Seeks Cheaper Pipeline Route," *The Moscow Times,* Feb. 4, 2008.
[63] Financial Times interview with Radek Sikorski, April 28, 2008. Video accessed May 15, 2008. Available at <http://www.ft.com/cms/af1f4356-e399-11dc-8799-0000779fd2ac.html>.
[64] Vladimir Socor, "Russian Oil Pipeline Shutoff to Lithuania: Wider Ramifications," *Eurasia Daily Monitor*, June 6, 2007.
[65] "Poland hopes for discussion on energy security at EU summit," *PAP*, OSC Transcribed Text, June 20, 2007.
[66] "Poland proposes EU early warning system to boost energy security," *Central Europe Energy Weekly*, March 14, 2008.
[67] Vladimir Socor, "Russian Oil Pipeline Shutoff to Lithuania: Wider Ramifications," *Eurasia Daily Monitor*, June 6, 2007.
[68] Valentinas Mite, "Russia: Poland Holds Up EU Partnership Talks," *RFE/RL*, Nov. 14, 2006.
[69] "Poland's Sikorski calls for start to EU-Russia negotiations," *Deutsche Presse-Agentur*, April 24, 2008.
[70] Judy Dempsey, "EU urges an energy pact with Russians," *International Herald Tribune*, March 9, 2006.

security.[71] Most notably, Polish officials have worked closely with their Lithuanian counterparts, stressing that the two countries are "linked by deep historical ties." [72] The two states work closely on efforts to extend the Odessa-Brody oil pipeline to the Polish port at Gdańsk and coordinate their positions on Nord Stream and Russia's adherence to ECT principles.

Finally, Poland has pushed for greater NATO and U.S. attention to European energy security. In 2006, Poland's then Prime Minister Kazimierz Marcinkiewicz brought up energy security with NATO Secretary General Jaap de Hoop Scheffer, urging the alliance to get more involved in the issue and calling for a NATO spirit of "one for all and all for one."[73] Polish officials continue to push NATO to get more involved in energy security questions.[74] Regarding their American friends, Polish officials have expressed hope in the past that Washington or the U.S. private sector would support non-Russian oil and gas pipelines through Ukraine.

Lithuania: Working to Minimize the Hand of Russia

Among the three Baltic States, Lithuania holds a special place given its leadership in raising the problem of reliance on Russian hydrocarbons. As with Poland, Lithuania's strategy is to minimize dependence on Russian sources of energy. Lithuanian President Valdas Adamkus once summed up the Lithuanian mentality as follows: "energy independence is a guarantee for our political independence."[75] Adamkus, like his Polish counterparts, has expressed his opposition to Germany and Russia's plans for Nord Stream.[76] The Baltic State calls for the Amber stream pipeline to be built in its place.

To reduce dependence on Russian gas, Lithuania intends to make use of nuclear power and build energy bridges to Poland and Scandinavia. It also hopes to get oil from the Black Sea region (via Poland and Ukraine). Unlike Poland, however, Lithuania is smaller and more dependent on Russia for energy. Furthermore, Lithuania is not a transit state to EU markets; any disruption of Lithuania's gas supplies would not grab as many headlines in Europe. So Lithuania is truly punching above its weight.

Lithuania's bold stand on energy issues is to some extent a result of the country's experience of Russian pressure and the perceived negative influence that Russian energy interests have in the country. The principal Lithuanian gripe with Moscow on the energy front is Russia's oil blockade of Lithuania's Mažeikių Nafta refinery. In July 2006, Russia's Transneft (the state-owned oil pipeline monopoly) shut off a spur from its Druzhba

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[71] Joint Communiqué of the Meeting of the Presidents of Estonia, Latvia, Lithuania and Poland, Vilnius, Nov. 6, 2006. Available from Latvian Ministry of Foreign Affairs. Available at <http://www.mfa.gov.lv/en/security/news/4457/?pg=8403>.

[72] "Lithuanian-Polish Presidents Call for 'Special Relationship,'" *Deutsche Press-Agentur*, Sept. 5, 2006.

[73] "Poland Can Count on NATO support on energy security issues," The Chancellery of the Prime Minister of Poland, Feb. 16, 2006. Available at <http://www.kprm.gov.pl/archiwum/english/2130_7846.htm>.

[74] Speech by Radek Sikorski before the 44th Munich Conference on Security Policy, Feb. 9, 2008, Munich, Germany. Text of speech reprinted in: "NATO's Driving Spirit Must Be Solidarity," *Hampton Roads International Security Quarterly*, April 15, 2008.

[75] "The President of Poland pledges to do his utmost that Lithuania and Poland would enjoy best relations ever in the history of both countries," Press Release, Office of the President of Lithuania, March 14, 2006. Available at <http://www.president.lt/en/news.full/6463>.

[76] "Lithuania wants to sink the Nord Stream gas pipeline," *New Europe*, April 21, 2008.

pipeline to the refinery, allegedly for technical reasons. Lithuanians argue that Russia halted oil supplies in an attempt to acquire the refinery for themselves; in point of fact, Transneft halted supplies only a few months after Poland's PKN Orlen outbid Russian firms for the refinery's purchase.[77] The oil blockade continues to this day, forcing the refinery to get its supplies by sea.[78]

Beginning in 2007, Vilnius blocked talks on an EU-Russia partnership agreement, demanding that Russia restart the flow of oil supplies through the pipeline and observe the principles of the ECT.[79] Explaining the Lithuanian position last year, Adamkus said, "if somebody's pushed into a corner and there's no way to get out of it, in desperation you have to use your final chance."[80] At an EU foreign ministers' meeting on April 29, 2008, Lithuania insisted it would continue to block discussions unless four items were included in the mandate for any talks with Moscow, two of which are energy-related: (1) reactivating the Druzhba pipeline and (2) calling on Russia to stick by the principles of the Energy Charter Treaty.[81] Only after a compromise was reached with Polish, Swedish and Slovene representatives in May 2008 did Lithuania relent.[82]

Central to Lithuania's diversification strategy is the use of nuclear power as an alternative to gas. The country's existing nuclear reactor at Ignalina, scheduled to close in accordance with EU rules, currently provides around 75 percent of Lithuania's electricity and over 35 percent of the country's total energy.[83] Once the plant is shut down, according to Lithuanian officials, the country will depend on Russian gas for three-quarters of its heating and electricity.[84]

Vilnius has therefore been working with the other Baltic States and Poland on building a new, regional 3,000-3,500 megawatt (MW) nuclear power plant near Ignalina in the next decade (energy experts say 2020 is a realistic start date[85]). Lithuania plans to invest up to 8 billion litas (about $3.6 billion) in the project,[86] and create a National Investment Company combining state and privately-owned electricity assets to oversee the plant's development.[87] Since the Baltic electricity market alone is too small to justify a nuclear plant of such a large capacity, Lithuania's Economy Ministry plans to construct power bridges to Poland and Scandinavia by 2012.[88] Polish and Lithuanian officials signed an accord last February paving the way for such a connection.[89] Electricity connections of this

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[77] Valentinas Mite, "Russia: Poland Holds Up EU Partnership Talks," *RFE/RL*, Nov. 14, 2006.
[78] "Lithuania's Mazeikiu refinery back online after two-month gap," *Agence France Presse*, Nov. 16, 2007.
[79] "Lithuania Threatens to Block Negotiations of Russia and Europe," *Kommersant*, May 14, 2007; Lithuania Awaiting EU's Negotiator Over Negotiations Mandate with Russia," *Baltic News Service*, April 30, 2008.
[80] "Lithuania Says It May Block EU-Russia Treaty Over Oil," *Bloomberg*, May 12, 2007.
[81] "As Lithuania continues battle for its interests, PM receives phone call from Ljubljana," *ELTA*, April 29, 2008. Available at <http://www.euro.lt/en/news/lithuanias-membership-in-the-eu/news/3194/>.
[82] Arturas Racas, "EU ministers cut deal to end Lithuania's veto on Russia talks," *Agence France Press*, May 11, 2008.
[83] Data is from 2004. See: "Lithuania - Energy Mix Fact Sheet," European Commission, January 2007. Available at <http://ec.europa.eu/energy/energy_policy/doc/factsheets/mix/mix_lt_en.pdf>.
[84] "New nuclear power plant deal postponed: Lithuanian premier," *Agence France Presse*, Oct. 10, 2007.
[85] "Lithuanian Prime Minister calls Russia's energy plans PR campaign," *Deutsche Presse-Agentur*, April 18, 2008.
[86] Nerijus Adamaitis, "Lithuania adopts law on new nuclear power plant," *Reuters*, June 28, 2007.
[87] "Govt submits papers on setting up of Lithuania's energy holding Leo LT to parliament," *Baltic News Service*, Dec. 27, 2007.
[88] "Lithuania's Authorities Urged to Give Fresh Impetus to Building of Power Bridges to Poland, Sweden – Daily," *Baltic News Service*, Oct. 2, 2007.
[89] "Lithuania, Poland Sign Power Deal, Spurring Nuclear Plan," *Agence France Presse*, Feb. 12, 2008.

kind will enable Lithuania and other countries involved to share power reserves as needed.[90]

Disturbingly, however, Russia is thought to be covertly working to undermine Lithuania's nuclear plans. A mysterious report with unknown authors was released in 2007 that outlined steps to undermine the nuclear plant,[91] and some suspect Russian involvement. Furthermore, a top business executive accused Lithuanian conglomerate MG Baltic of having connections to Russian intelligence services and trying to undermine plans for the power station.[92] Such developments are not uncommon. Lithuanian commentator Audricis Baciulis quipped, "Lithuania's experience over the past 10 years shows that each attempt to escape the grip of the Russian energy system has always resulted in scandals."[93] Russia also recently floated the idea of setting up its own nuclear power station in the Baltic region (specifically, in Russia's Kaliningrad enclave) by 2015.[94] This could be a Kremlin stunt to cut the legs out from Lithuania's energy security strategy as existing electricity markets are too small to absorb the output from two nuclear power plants.

At the EU level, Lithuanian officials would also like greater European unity when it comes to Russian energy. At the height of the dispute surrounding the Druzba pipeline, one Lithuanian foreign ministry official commented, "we were full of rosy dreams [when we joined the Union]… We thought Europeans would speak to Russia with one voice. Now we're fighting Russia on two fronts."[95] This is an apparent reference to Russia's simultaneous military and energy pressure in the Baltic region. Speaking as the host for the October 2007 Vilnius energy security conference, Adamkus supported the Commission's energy proposals for reform of the EU's internal energy market. But he insisted that Europe develop a common approach to energy suppliers like Russia:[96] "It is a matter of concern that some European countries prefer to deal with energy security related challenges individually, instead of acting in a united manner based on core Euro-Atlantic values."[97] Adamkus urged like-minded countries to get together more often to discuss items related to energy security. He suggested meetings of this kind could take place before each Spring European Council or the EU-U.S. Summit.[98]

Estonia: Escaping Energy 'Islandization'

Estonia views energy security through a strategic lens. In April 2008, Estonian President Toomas Hendrik Ilves commented that, "energy imports from third countries rank among the main *threats* to the European Union's internal market and to energy security" (emphasis added).[99] Importantly, Estonia is more energy self-sufficient than Lithuania.

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[90] Arunas Gricius, "The Baltics Going Nuclear: Can a Regional Energy Strategy Work?," *Central Europe Digest*, Aug. 18, 2006.
[91] "Russia's Gazprom May Frown on Lithuania's New N-Plant – Daily," *Baltic News Service*, Nov. 13, 2007.
[92] "Lithuanian PM Downplays Importance of Ownership Stakes in N-Plant Co," *Baltic News Service*, Nov. 22, 2007.
[93] Audricis Baciulis, "Energy Is Russia's Trojan Horse in Lithuania," *Veidas*, BBC Monitoring Translation, Nov. 29, 2007.
[94] "Lithuanian Prime Minister calls Russia's energy plans PR campaign," *Deutsche Presse-Agentur*, April 18, 2008.
[95] Charlemagne, "A Cool Peace," *The Economist*, March 3, 2007.
[96] Speech by Valdas Adamkus, President of the Republic of Lithuania, "Proposals of Development of External EU Energy Policy," Vilnius Energy Security Conference 2007, Oct. 11, 2007, Vilnius, Lithuania.
[97] Ibid.
[98] Ibid.
[99] "Estonia, Lithuania against third countries' influence on NATO enlargement plans," *Russia & CIS Military Newswire*, April 30, 2008.

Solids – oil shale deposits – make up practically all of Estonia's electricity[100] and over half of the country's total energy, making the country one of the most energy self-sufficient countries in the EU. But solids production has been in decline since 1990,[101] posing an energy security dilemma for Estonia. To address this problem, Estonian leaders desire links with fellow EU countries as a way to reduce reliance on Russian gas through electricity and escape energy "islandization." Tallinn supports completing the new Ignalina nuclear plant in Lithuania as soon as possible[102] as nuclear power does not currently enter into Estonia's energy mix.[103]

The centerpiece of Estonia's coping strategy centers upon building an energy bridge to Scandinavia. The "Estlink" cable – capable of carrying 350 MW of electricity between Finland and Estonia – became operational at the beginning of last year.[104] Plans exist for the installation of another 650 MW sea cable by 2013, to bring the total capacity of Estonia's energy bridge to Finland to 1,000 MW.[105]

Estonia has also done what it can to protest Nord Stream's construction. In September 2007, Tallinn rejected a request by the Gazprom-led consortium to survey the seabed off the Estonian coast for a possible route for the pipeline, potentially forcing Nord Stream to rethink its route along the Baltic seabed.[106] Estonia would like to see the proposed Amber Stream pipeline – being promoted by Tallinn and other capitals in Central Europe's Baltic tier – receive consideration. Estonian Foreign Minister Urmas Paet asked, "Why didn't Nord Stream want to investigate a real alternative – the overland option?"[107] The Minister has also complained that the Baltic States and Poland were kept outside the negotiations on the pipeline for long periods of time.[108] In a move that underlines Estonia's strategy of caucusing with like-minded states, Paet indicated that his country would work with Poland and the other two Baltic States to enlist the Commission in discussing matters relating to the German-Russian pipeline.[109]

Estonian officials have voiced support for European solutions to the region's energy dilemmas. Tallinn backs a common EU policy and favors the energy package proposed by the Commission in 2007. Paet has voiced support for a more uniform EU energy policy. "A unified energy policy is part of security policy," he said in November 2007.[110] President Ilves has stated that only by speaking with one voice can Europe hope "to resist the attempts of any country to use energy supplies to increase their political profile."[111]

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[100] Data is from 2004. See: "Estonia – Energy Mix Fact Sheet," EU Commission, January 2007. Available at <http://ec.europa.eu/energy/energy_policy/doc/factsheets/mix/mix_ee_en.pdf>.
[101] Ibid.
[102] "Latvia, Estonia confirm backing for Lithuania's nuclear plant project," *Baltic News Service*, Dec. 21, 2007.
[103] See: "Estonia – Energy Mix Fact Sheet," EU Commission, January 2007. Available at <http://ec.europa.eu/energy/energy_policy/doc/factsheets/mix/mix_ee_en.pdf>.
[104] "Estlink 2 cable to be built by Estonian Energy, Fingrid," *Baltic News Service*, Oct. 9, 2007.
[105] "Eesti Energia supports second Estlink," *Baltic News Service*, Sept. 17, 2007.
[106] Anneli Reigas, "Estonia blocks key Baltic Sea gas pipeline," *Agence France Presse*, Sept. 20, 2007.
[107] "Campaign against planned Nord Stream pipeline," *New Europe*, Nov. 3, 2007.
[108] Ibid.
[109] Anneli Reigas, "Estonia blocks key Baltic Sea gas pipeline," *Agence France Presse*, Sept. 20, 2007.
[110] "Paet: The European Union Needs a Coordinated Energy Policy," Press Release of the Estonian Ministry of Foreign Affairs, Nov. 15, 2007. Available at <http://www.vm.ee/eng/kat_138/aken_prindi/9011.html>.
[111] Quoted in: "Caspian Region Provides an Alternative to Russia for Europe's Energy Supply – Estonian President," *Baltic News Service*, May 23, 2008.

Romania: Covering Central Europe's Southern Flank

Romania is the sole "strategic player" in Central Europe's southern tier, and the strongest link in the Nabucco chain. The country's relative self-sufficiency in hydrocarbons encourages Bucharest to take a tougher line than many of its neighbors, who generally fall in the "commercial opportunists" category. Romania's domestic gas deposits constitute a substantial safety blanket; 630 bcm of natural gas reserves lie beneath Romanian soil, or enough to last 50 years at present rates of production.[112] Domestic gas supplies cover a large portion of demand, and Romania in 2006 imported only 31 percent of its gas consumption from Russia (the lowest share in the Central European region).[113] For this reason, EU newcomer Romania is able to be an active player on the energy security front.

Romanian leaders favor a common EU policy regarding energy agreements with producer countries. "We want the European Union to adopt a common stance as soon as possible," Prime Minister Călin Popescu-Tăriceanu said in March 2008. Doing so, he explained, "would help [Europe] better negotiate all agreements concerning energy supply."[114]

With a common EU approach nowhere on the horizon, Romania focuses on finding new sources of supply, both for itself and for Europe. Romania was among the countries that met following the Ukraine gas crisis in January 2006, to draw up a plan to reduce dependence on Russian gas. Plans discussed embraced LNG facilities and accelerating the Nabucco gas pipeline project.[115] Romania's Foreign Minister visited Washington in March of that year, underscoring to U.S. journalists that "we [in Romania] have been talking about [energy security] for a long time, but for some in Europe, this [Russo-Ukrainian gas spat] was a political watershed."[116]

Romanian President Traian Basescu has shown himself to be bold in criticizing Gazprom and Russia. He has characterized Russia's energy power as "more efficient than the Red Army used to be,"[117] and has called for "diminishing the political impact" of Europe's reliance on Gazprom through alternative sources of energy.[118]

Basescu is a staunch supporter of diversification measures. Two years ago, he became the first European head of state to unambiguously call for an EU Caspian-Black Sea energy supply strategy.[119] In an interview with a Russian news outlet, he expressed dismay that Russia undercuts Europe's aspirations for supply diversification.[120] At a time when countries like Bulgaria or Hungary appear to simultaneously nod in favor of Nabucco and South Stream, the Romanian President has underlined his support for the former. "The

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[112] *BP Statistical Review of World Energy 2008*, p.22.
[113] Data is from Eurostat.
[114] Quoted in: "Romania wants common EU energy policy – PM Tariceanu," *Hungary Business Newswire*, March 14, 2008.
[115] Ernest Wyciszkiewicz, "One for All – All for One' – The Polish Perspective on External European Energy Policy," *Foreign Policy in Dialogue*, Vol. 8, Issue 20, Jan. 11, 2007, p.37.
[116] Quoted in: David R. Sands, "Romania backs alternate route for pipeline to West; Black Sea called key to stability," *The Washington Times*, March 29, 2006.
[117] Vladimir Socor, "Romanian President Concerned by European Dependence on Russian Energy," *Eurasia Daily Monitor*, Nov. 21, 2006.
[118] Quoted in: "Romania: President Pushes Country's Role As Energy Conduit," *RFE/RL*, July 29, 2006.
[119] Vladimir Socor, "Romanian President Concerned by European Dependence on Russian Energy," *Eurasia Daily Monitor*, Nov. 21, 2006.
[120] Ibid.

Nabucco project would decisively contribute to Europe's energy security and supply diversification," he made clear in 2006, and he has stuck by this position.[121] Basescu has also levied what could be seen as veiled criticism of the commercial opportunists for their flirtations with new Russian pipelines, saying at one point that "building oil and gas pipelines without trying to find other sources would be a huge mistake."[122]

Romania also supports two other pipeline projects that could transit Caspian energy to Europe around Russia. One is the Bucharest-sponsored plan for the Constanta-Trieste oil pipeline from Romania's port at Constanta to the Italian city of Trieste. To fill this pipeline Romania wants Caspian oil from across the Black Sea. Speaking before a meeting of Romania's diplomatic core in 2007, Basescu stressed the need to strengthen energy relations with Azerbaijan and Kazakhstan as a way to provide an alternative to the status quo.[123] Basescu has also hinted that he supports Georgian terminals on the Black Sea as an alternative to Russia's port at Novorossiysk.[124] This runs counter to Moscow's hope to keep Black Sea crude supplies reliant on passage through Russia's North Caucuses. The second pipeline project is the proposed White Stream natural gas pipeline. This project, still very much on the drawing board, would carry Central Asian gas from Georgia across the Black Sea to Romania.[125] In addition, Romania has proposed a LNG terminal at its Constanta port.[126] Though a project like this would likely face logistical hurdles, it serves to illustrate Romania's commitment to accessing non-Russian energy supplies.

Romania's strong westward orientation has not won many friends in the Kremlin or Gazprom headquarters. As mentioned previously, South Stream will bypass the country altogether, going through Serbia and Hungary en route to Western markets.[127] This effectively makes Romania the latest casualty in Russia's new pipeline strategy of favoring friends and punishing perceived adversaries.[128] As a result, we may see Romania re-double its lobbying efforts in favor of an alignment of interests on Nabucco. Another option would be for Romania to use its legal rights under maritime law to slow down or temporarily halt South Stream in the Black Sea (should the pipeline be routed through Romanian waters).[129]

Czech Republic: Leverage as Europe and Transit as Leverage

In general, the Czechs recognize that higher levels of gas consumption represent an energy security risk when the primary source of imports is Russia. However, in the

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[121] Press Release, Office of the Romanian President, June 24, 2007. Available at <http://www.presidency.ro/pdf/date/8904_en.pdf>.
[122] Quoted in: Vladimir Socor, "Romanian President Concerned by European Dependence on Russian Energy," *Eurasia Daily Monitor*, Nov. 21, 2006.
[123] Speech by President Traian Basescu to Romanian diplomats, "New actualities, new responsibilities, new perspectives," Sept. 3, 2007, Bucharest, Romania. Summary available at <http://www.wavemagazine.net/arhiva/12/politics/romania.htm>.
[124] Ibid.
[125] Alexandros Petersen, "Reaching the Caspian Through Ukraine," *Central Europe Digest*, April 1, 2008.
[126] "Focus on Romania," *European Gas Markets*, July 14, 2006; "Romania and Qatar discuss LNG terminal at Constanta," *European Spot Gas Markets*, March 10, 2006.
[127] Oleg Shchedrov, "Russia signs Serbia, wins 'pipeline war' with EU," *Reuters*, Jan. 25, 2008.
[128] For more on this point see: Ryan R. Miller, "Romania and Russia's Selective Transit Strategy," *Central Europe Digest*, Jan. 15, 2008.
[129] Vladimir Socor, "Gazprom's South Stream Project Can be Halted in the Black Sea," *Eurasia Daily Monitor*, March 6, 2008.

strategic pursuit of reducing Russian leverage, some in the Czech Republic favor the tactic of being an energy transit state.

Looking at official statements and policy, the Czechs clearly understand that complete energy dependence on Russia is not desirable. In fact, the Czech Republic was one of the few countries that recognized and acted on the problem early. During the 1990s, the Czechs began diversifying their gas imports, which traditionally had exclusively come from the Soviet Union (Russia). Many of the Czech Republic's neighbors laughed at the time, since energy from Russia was cheap.[130] But from 1997-2002, the share of Norwegian gas in the Czechs' import basket increased from 9.7 to 27 percent.[131] As it turned out, the Czechs had the last laugh. The Czech Republic continues to want increased access to Norwegian gas as a hedge against Russian energy dominance.[132] The country has also taken similar precautions regarding oil, building a pipeline to Germany, which served it well during the recent reduction in Russian oil supplies.[133]

Czech officials are publicly wary of Russia's reliability as a supplier. Deputy Prime Minister Alexandr Vondra noted before an October 2007 energy security conference in Vilnius that "Europe's relatively trouble-free relationship with Russia – our major energy supplier – seems to be nearing an end."[134] He further maintained that Europe needs a united response to challenges in the energy security field:

> "…unjust manipulation of 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. Successfully countering such threats necessitates that Member States of the EU stand together when dealing with other actors."[135]

Confidential Czech Foreign Ministry documents echo these concerns about dependence on Russia. A strategy paper leaked to the press last year suggested that Russia is an unreliable energy partner.[136]

Looking ahead, certain Czech officials have indicated that Prague will make energy security one of its top priorities when it takes over the rotating EU Presidency in January 2009.[137] According to Vondra, the Czech Presidency will urge that the EU become a more influential player in questions of energy, and call for policies grounded upon "real energy solidarity, which would enhance the security of all EU members."[138] The Czechs' Ambassador-at-large for energy security, Václav Bartuška, articulated in 2007 the need for

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130 Briefing in Washington, DC, May 2008.
131 *Energy Policies of IEA Countries: The Czech Republic, 2005 Review*, OECD: Paris, 2005, p.34.
132 Zoe Grainge, "StatoilHydro Signs Supply Deal with Czech Gas Firm," *Global Insight*, April 15, 2008.
133 Judy Dempsey, "Cutback in Russian oil no problem to Czechs," *International Herald Tribune*, July 18, 2008.
134 Speech by Alexandr Vondra, Deputy Prime Minister for European Affairs of the Czech Republic, "Solidarity as a Cornerstone of the EU Energy Policy," Vilnius Energy Security Conference, Oct. 11, 2007, Vilnius, Lithuania.
135 Ibid.
136 "Czech Republic must focus on long-term energy security, reduce Russian reliance – special envoy," *Czech Republic and Slovakia Business Weekly*, Jan. 22, 2007.
137 See: "Energy security to be top priority for Czech EU Presidency," *Czech Republic and Slovakia Business Weekly*, Nov. 9, 2007. (This of course assumes the EU Lisbon Treaty is not fully ratified before the appropriate EU deadline).
138 "Energy security to be top priority for Czech EU Presidency," *Czech Republic and Slovakia Business Weekly*, Nov. 9, 2007.

a common EU approach to Russia. "If Europe is able to get a deal with Russia, it can be only as a group," he said.[139]

Like the Baltic States, the Czech Republic has put the nuclear option on the table as a means to check reliance on natural gas. Though demand for gas has been stagnant since 1997, and has actually come down in last few years,[140] economic growth is driving up energy consumption, and the country may become a net electricity importer in the near future.[141] Currently, most of the Czech Republic's electricity (around 60 percent) is supplied by coal.[142] Yet the Czech government is facing pressure to reduce greenhouse emissions, ruling out an expansion of the use of coal power.[143] Czech Prime Minister Mirek Topolanek has said that the country's hydroelectric opportunities are already maxed, arguing that a "nuclear energy renaissance" offers the best way forward.[144] There is the temptation to switch to natural gas-fried plants (gas is a cleaner fuel than coal), but Topolanek and other officials have underlined the role that nuclear power can play in improving both the environment and the country's energy security.[145]

Despite apprehensions about Russia's energy dominance, the Czechs do have a working relationship with Gazprom. Pipelines owned by German subsidiary companies transport Russian gas to Europe (primarily Germany) via the Czech Republic.[146] In fact, about 40 percent of gas en route to Germany is pumped over Czech territory.[147] The Czechs import 8 bcm of Russian gas and nearly 2 bcm of this is supplied as payment for gas transit.[148] Czech officials openly use their transit role as a source of leverage in dealing with Russia. As Bartuška conveyed last year:

> "It is in our strategic interest to remain a transit state to Germany and elsewhere… we want to preserve this not just for income from transit but also for the Czech Republic's security of supply; because frankly, if there is ever Russian gas switched off going to Europe, the last country where that will happen is to Germany."[149]

There is interest on the Czech side in expanding this transit function and Gazprom has expressed interest in building a branch from the Nord Stream gas pipeline across Czech

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[139] Jason Hovet, "Bartuška: Energy security is elusive," *Czech Business Weekly*, April 10, 2007.
[140] "The Czech Republic's National Report on the Electricity and Gas Industries for 2005," Report for the European Regulators' Group for Electricity and Gas (ERGEG), July, 2006, p. 38
[141] Matthew Hall, "Czech PM Backs New Nuclear Reactors; CEZ Poised to Begin Construction Work," *Global Insight*, Nov. 6, 2007.
[142] "Czech Republic – Energy Mix Fact Sheet," EU Commission, January 2007. Available at <http://ec.europa.eu/energy/energy_policy/doc/factsheets/mix/mix_cz_en.pdf>.
[143] Matthew Hall, "Czech PM Backs New Nuclear Reactors; CEZ Poised to Begin Construction Work," *Global Insight*, Nov. 6, 2007.
[144] Ibid.
[145] Ibid; "Czech PM Topolanek sees 'nearly zero' potential for additional Czech hydro, wind power," *Central Europe Energy Weekly*, March 7, 2008; "Klaus sees nuclear energy as essential for country's future," *New Europe*, Dec. 8, 2007.
[146] Ewa Paszyc, "Gazprom in Europe: Faster Expansion in 2006," Centre for Eastern Studies (Warsaw), Feb. 2007, Appendix I.
[147] "CzechRep losing position of oil, gas transit country," *CTK National News Wire*, March 10, 2008.
[148] "Gazprom Takes Part in Celebration of Gas Supplies to Czech," *Economic News*, Nov. 6, 2007.
[149] Václav Bartuška in an interview with Interfax. See: "Nord Stream pipeline to have branch through Czech Republic - Russian Gazprom deputy chair," *Central Europe Energy Weekly*, Nov. 3, 2007.

territory.[150] Construction on the so-called "Gazela" section of Nord Stream could begin in the next year.[151] Some fears exist that the Czech Republic's transit role will decline following Nord Stream's construction.[152] Indeed, part of Russia's rationale for building the pipeline is to bypass Ukraine – and it is difficult to do so without also bypassing the Czech and Slovak Republics. In a sense, the Czechs are happy to consider Nord Stream participation in part because of their geography – the country does not border Russia or any part of the former Soviet Union, and Russia would not be able to cut off their supplies because Germany would effectively be a transit state. One problem, however, of showing interest in Nord Stream is that it could set Prague in opposition to Warsaw and the Baltic States.

Latvia: Strategic Ambiguity

Despite being another one of the EU's energy islands along with Estonia, Latvia's political establishment currently maintains a relatively ambiguous position on the subject of Russian energy. In the words of Estonian analyst Andreas Kasekamp, "Baltic unity has disappeared – Latvians have been tempted by Russian business projects."[153] One Latvian analyst speaking in Washington seemed to agree with this assessment, suggesting that the Latvian government has no coherent plan for energy security, and has essentially privatized its energy strategy to the benefit of Russian interests.[154]

To be sure, the Latvian political establishment would favor greater energy independence from Russia.[155] For example, Latvia supports the construction of Lithuania's new nuclear power plant, and looks forward to the future creation of electricity links connecting Latvia and Lithuania to Sweden.[156] Latvian President Valdis Zatlers has expressed hope that LNG and Norwegian gas can one day supply the Baltic region.[157] He has also consulted with top members of the United States' Bush administration on ways to possibly achieve greater energy independence.[158] Latvia continues to support the Amber Stream pipeline proposal as an alternative to Russia's Nord Stream – apparently after some persuasion from the Poles.[159]

However, signs of opportunism have emerged in recent months, particularly since Latvia's change in Prime Minister in December 2007. The new government led by Prime

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[150] "Nord Stream pipeline to have branch through Czech Republic - Russian Gazprom deputy chair," *Central Europe Energy Weekly*, Nov. 3, 2007.
[151] "Building of Czech 'Gazela' section of Nord Stream pipeline could ...," *Czech Republic and Slovakia Business Weekly*, February 29, 2008.
[152] "CzechRep losing position of oil, gas transit country," *CTK National News Wire*, March 10, 2008. On the other hand, the Russians have promised that the amount of gas transiting the Czech Republic will increase following Nord Stream's construction, holding out the prospect of additional transit revenues. See: Sally Bogle, "Nord Stream to Submit New Route Plan to Sweden by end-2007, May Branch Across Czech Network," *Global Insight*, Nov. 6, 2007. See also: "Czech Republic concerned about Nord Stream gas pipeline from…" *Czech Republic and Slovakia Business Weekly*, March 2, 2007.
[153] "Whatever happened to Baltic unity?," *Deutsche Presse Agentur*, Feb. 23, 2008.
[154] Briefing in Washington, DC, April 2008.
[155] See for example: "Latvian Transport Minister Calls to Assess Alternative NatGas Supplies," *Baltic News Service*, March 11, 2008.
[156] Speech by Valdis Zatlers, President of Latvia, "Solving the Problem of Energy Islands: the Case of the Baltic States," Vilnius Energy Security Conference, Oct. 11, 2007, Vilnius, Lithuania.
[157] Ibid.
[158] "Latvian President Seeks US Assistance in Solving Energy Independence Issues," *Baltic News Service*, April 28, 2008.
[159] "Poland persuades Latvia to support Amber gas pipeline project – Polish EconMin," *Central Europe Energy Weekly*, Feb. 8, 2008.

Minister Ivars Godmanis, a member of the Latvian Way party, could be on the verge of a warmer approach to Moscow. The new Foreign Minister Maris Riekstins stated a few months ago, "in natural gas we have managed to develop very good co-operation [with Russia]," adding, "we don't have a single case which might be seen to show bad will in this particular field."[160] Such statements seem to contradict the Baltic region's shared concerns about Nord Stream and could raise eyebrows in nearby capitals.

Following Russia's row with Estonia last year, some of the oil that had been transited through Estonia has since been directed through Latvia instead,[161] a development which fits well with Russian attempts to divide the Baltic States on select issues. "Right now, Estonia seems to be in the doghouse and Latvia seems to be in the good books (with Moscow)," Kasekamp argues.[162] The Latvian MP Vaira Paegle denies that voices within the country disposed to favor Gazprom have altered Latvian state policy positions to date.[163] Still, Paegle admits that Latvia lacks a clear energy security doctrine.[164] This in turn provides an opening for Moscow to warm relations with Riga and divide Latvia from its neighbors.

The Latvians might have their own reasons to favor an energy thaw with Russia. Indeed, Riga wants to make its contribution to a European-wide energy structure as a hub for gas storage. Latvia's Incukalns facility is one of the largest underground gas storage facilities in Europe with a capacity of 4.4 bcm.[165] With sufficient investment, Latvia could hold even more gas – as much as 50 bcm[166] – which could offer Central Europe a strategic reserve the next time there is a supply disruption. President Zatlers has noted that these storage facilities serve both "commercial and strategic" purposes.[167] EU Energy Commissioner Andris Piebalgs has said Latvia's storage facilities would increase the security of energy supplies to several European countries,[168] and Latvia succeeded in getting Brussels to allocate over 1 million euros for a feasibility study.[169] But the project stands a better chance of getting off the ground with Russian support. Latvia has reached out to Gazprom to get the Russians to invest in these storage facilities (and connect them to Nord Stream by building a pipeline link along the Baltic seabed), though the Russian gas giant has turned down previous Latvian overtures.[170]

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160 Robert Anderson, "Russia seeks better Europe ties, says Latvia," *Financial Times*, Jan. 21, 2008.
161 Andrew Neff, "New Oil Product Export Terminal in Russia Spells Trouble for Baltics' Transit Business," *Global Insight*, May 15, 2008.
162 "Whatever happened to Baltic unity?," *Deutsche Presse Agentur*, Feb. 23, 2008.
163 "Latvian MP discusses relations with Russia, United States," *Latvijas Avise*, BBC Monitoring Reports, April 21, 2008.
164 Ibid.
165 "The Outlook of Latvian Potential Underground Gas Storage…," United Nations Economic Commission for Europe (UNECE), Working Party on Gas. Available at <http://www.unece.org/ie/se/pdfs/wpgas/session/17_countr/latvia.pdf>.
166 A. Jesinska, Andris Kreslins, and N. Zeltins, "Increasing Role of Underground Gas Storages for Reliable Supply of Gas to Latvia, Lithuania, Estonia, Finland and NW Russia and Prospects of Development of Incukalns Underground Gas Storage," 23rd World Gas Conference, 2006, Amsterdam, the Netherlands.
167 Speech by Valdis Zatlers, President of Latvia, "Solving the Problem of Energy Islands: the Case of the Baltic States," Vilnius Energy Security Conference, Oct. 11, 2007, Vilnius, Lithuania.
168 "EU Energy Commissioner Piebalgs: Latvia's underground gas storage facility could contribute to energy supply security in Europe," Press Release, Latvian Ministry of Foreign Affairs, Jan. 31, 2007. Available at <http://www.am.gov.lv/en/news/DomesticNews/2007/january/31-2/>.
169 "Russia still strong energy player in the Baltics," *Deutsche Presse Agentur*, Feb. 22, 2008.
170 "Gazprom won't build Nord Stream underground gas storage in Latvia," *Interfax*, June 14, 2007.

According to Kasekamp, Latvia is toning down its objections to Nord Stream in the hope of convincing Gazprom to make use of the country's natural gas storage facilities.[171] Riga has declared it is not presently taking sides on Nord Stream provided the pipeline does not harm the environment of the Baltic Sea.[172] An Economy Ministry representative speaking about the Russian pipeline noted only that, "the Nord Stream decision is made by a supplier and a consumer."[173]

Another way in which Latvia seems to be siding with Russia is on the EU Commission's recent unbundling proposal. In January 2008, eight EU countries (France, Germany, Greece, Austria, Luxembourg, Latvia, Bulgaria and Slovakia) proposed a watered-down counter-proposal to a Commission "unbundling" initiative. The initiative would place restrictions on energy firms' ability to monopolize both gas production and distribution activities. Furthermore, the initiative's so-called "Gazprom clause" would restrict third party ownership of key EU energy assets to those entities that agree to function in accordance with EU standards. It would require a special EU agreement should Gazprom (or another non-European energy firm) want to own a gas distribution network or operator.[174] The so-called "third option" put forward by the eight opponents of unbundling would allow production companies to own all of the distribution networks' shares, even if the firms themselves are nominally separate. Noticeably absent from the third option is the language on the Gazprom clause.[175]

Latvia was one of only three Central European states (along with Slovakia and Bulgaria) to join countries traditionally warm to Moscow in supporting a draft that pulls back from imposing unbundling criteria on companies like Gazprom. This could conceivably be part of a campaign to convince Gazprom to change its mind regarding investment in Latvia's storage capacities. Because of such developments, this report lumps Latvia in with the "commercial opportunists," even though it is something of a battleground state.

Slovenia: Russian Gas - What's the Problem?

The exact Slovene response strategy is hard to pin down, partly because Russian gas is not seen as a major problem in the Alpine state. Like the Czech Republic, Slovenia does not feel Russian pressure as much as other Central European states in part due to its geography. Unlike all other former communist states now in the EU and NATO, Slovenia was never part of either the Warsaw Pact or the Soviet Union. Aside from Slovenia's absence from the Conventional Armed Forces in Europe (CFE) Treaty, Russia and Slovenia have no appreciable bones to pick with one another. "There is not one cloud on the horizon of Russian-Slovenian relations," remarked Sergei Yastrzhembsky, Putin's special representative on European affairs.[176] The same sentiment holds true on the Slovene side; Russia is far away and Slovenia's preoccupation lies with the Western

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[171] "Whatever happened to Baltic unity?," *Deutsche Presse Agentur*, Feb. 23, 2008.
[172] "Russia still strong energy player in the Baltics," *Deutsche Presse Agentur*, Feb. 22, 2008.
[173] Quoted in: Ibid.
[174] Simon Taylor, "EU struggles to agree on anti-Gazprom clause," *European Voice*, May 22, 2008; "'Gazprom clause' issues Russia ultimatum for energy co-operation," Euractive.com, Sept. 20, 2007.
[175] Joint Letter from the Energy Ministers of France, Germany, Greece, Austria, Luxembourg, Latvia, Bulgaria, and Slovakia addressed to Madame Angelika Niebler, ITRE Chairwoman, European Parliament, Jan. 29, 2008. Available at <http://www.euractiv.com/ndbtext/press/3rdoptionletter.pdf>.
[176] "EU, Russia may move ahead with partnership agreement," *New Europe*, Jan. 5, 2008.

Balkans. Perhaps for these reasons, Slovenia does not feel a sense of urgency about Russian energy influence.

Furthermore, the country has access to North African sources of gas via Italy (about one-third of Slovenia's gas comes from Algeria[177]), and nuclear power contributes significantly to electricity production (around 40 percent).[178] As such, Slovenia views Russian gas as a natural part of a relatively diverse energy mix.

Slovenia offers words of support for those aspirating for supply diversification, though leaders in Ljubljana do not go out of their way to make alternative pipelines a priority. "To guarantee energy security Slovenia advocates the diversification of energy suppliers, sources and transit routes," Slovenia's Development Minister recently stated.[179] But there are limits to how far the Slovenes will stick their neck out.

Notably, the Slovenian representative before the Vilnius energy security conference in October 2007 did not address the question of an external energy policy (focusing instead on environmental concerns) and did not once mention Russia.[180] In principle, the Slovenes support an LNG project on the Croatian coast, but it is really Hungary that is taking the lead there. Back in January 2006, Slovenia added its voice to those drawing up a plan to reduce dependence on Russian gas involving gas stockholdings, LNG and accelerating Nabucco.[181] But again, Slovenia was a follower, not a leader in such efforts. Moreover, the Slovene Economy Minister in June 2006 undercut the argument for a LNG terminal in the Adriatic by arguing that an additional conduit for Russian gas from Slovakia to Italy via Slovenia would be better for the environment.[182] Clearly, some in Slovenia are also concerned that LNG terminals in the Adriatic could impact the Slovene tourism industry.

The Slovenes have often touted energy security as a top agenda item for their small Alpine nation. Back in July 2006, Slovenia's then Prime Minister said energy security was a priority, and even suggested his country would like to see Iranian gas shipped to Europe.[183] On Jan. 1, 2008, Slovenia took the helm at the EU's rotating Presidency. But the government's list of presidency priorities attached greater weight to questions of internal market reform, climate change and renewable energy research than it did external energy policy.[184] For instance, the Slovenian EU presidency mentioned only the need for "energy dialogue with Russia," without referencing the need for a common approach to Russia,

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[177] Council of the Energy Agency of the Republic of Slovenia, "Report on the Slovene Energy Sector for 2005," Report for the European Regulators' Group for Electricity and Gas (ERGEG), July 21, 2006, p.83.
[178] "Slovenia," European Atomic Forum (FORATOM), updated Oct. 24, 2007. Available at <http://www.foratom.org/index.php?option=com_content&task=view&id=335&Itemid=1249>.
[179] Slovenian Development Minister Ziga Turk quoted in: Kostis Geropoulos, "Slovenian Minister Says It's Wise to Diversify," *New Europe*, May 12, 2008.
[180] Granted, Slovenia was on the verge of national elections the following month and dispatched a relatively low-ranking representative to the conference. See: Speech by Ziga Turk, Minister without portfolio, Head of the Slovenian Government Office for Growth, "Responsible Energy for Responsible Partners," Vilnius Energy Security Conference, Oct. 11, 2007, Vilnius, Lithuania.
[181] Ernest Wyciszkiewicz, "One for All – All for One' – The Polish Perspective on External European Energy Policy," *Foreign Policy in Dialogue*, Vol. 8, Issue 20, Jan. 11, 2007, p.37.
[182] "Gazprom's Pipeline better for environment than gas terminals – Slovene Minister," *Television Slovenia*, BBC Monitoring Reports, July 4, 2006. See also: "Slovenia, Russia's Gazprom negotiating pipeline construction – Russian Ambassador to Slovenia," *Czech Republic and Slovakia Business Weekly*, April 21, 2006.
[183] Nora Boustany, "Slovenia's Energy-Minded Premier Shares Hopes for a Solution on Iran," *Washington Post*, July 12, 2006.
[184] "Current topics in the area of energy during the Slovenian EU Presidency," Website of the Slovenian Presidency. Available at <http://www.eu2008.si/en/Policy_Areas/Transport_Telecommunications_and_Energy/Energy.html>.

energy solidarity or even suggesting, like the Czechs, that the EU become a more "influential player" in energy policy. Slovenian Development Minister Ziga Turk admitted to the press that his country is not actively pushing energy diversification during its stint at the Presidency, balancing these comments by saying, "as a [EU] member state and a country which is an importer of energy we are of course interested in having the option of different suppliers."[185] When all is said and done, the Slovenes seem content not to involve themselves in EU-Russia tensions.

Slovenia views the option of enhanced partnership with Russia as a logical one. A few months ago, Slovene officials held talks with Gazprom on possibly joining the South Stream pipeline. Though Slovene officials have noted the importance of Nabucco to the EU's diversification goals, the President and Prime Minister seriously discussed the possibility of the Alpine republic's participation with Gazprom CEO Alexei Miller, who in June confirmed that Slovenia would take part.[186] This latest development suggests Slovenia is ready to mimic Austria in its approach to Russia's energy monopoly. Ljubljana's mini "Aust-politik," along with those of other commercial opportunists, serves to deepen national and European dependence on Russian gas, and create a sense of momentum behind South Stream – to the detriment of the Nabucco project.

Hungary: Having One's Cake and Eating It Too

From a distance, Hungary seems to want to have it both ways. At times, Budapest appears to vacillate between its desire to support Nabucco and other diversification projects and its desire to partner with Moscow in the commercial sphere. Most recently, this point is brought home by the Hungarian government's decision to join South Stream – to the annoyance of U.S. and EU Commission officials.

In 2006, Hungary was one of the most affected by the Ukraine gas crisis (Hungary reported a loss of 60 percent of capacity on the main pipeline from Ukraine[187]), so the importance of energy security does hit home with Hungarian leaders. At the same time, however, Budapest appears to hedge its bets by playing the Gazprom card. A government spokesman summed up the Hungarian position in June 2006: "Our goal is to examine every possible project and support the realizable ones."[188] Questions of commercial viability are clearly important, but short-term cost-benefit analyses often overlook strategic-level considerations.

Undeniably, Hungary has been a voice in favor of positive solutions to Europe's energy security dilemmas. These include a LNG terminal on the Croatian coast with a pipeline running north to Hungary as a way of reducing reliance on Russian sources of gas.[189] Other Hungarian proposals have included a centralized information system; in the words of former Hungarian Economy Minister János Kóka, "a surveillance center that could

[185] Slovenian Development Minister Ziga Turk quoted in: Kostis Geropoulos, "Slovenian Minister Says It's Wise to Diversify," *New Europe*, May 12, 2008.
[186] "Gazprom Says Gas Pipeline to Cross Slovenia," Slovene news agency STA, BBC Monitoring Reports, June 10, 2008. See also: "In Slovenia, Gazprom Discusses South Stream," *European Report*, April 15, 2008.
[187] *Energy Policies of IEA Countries – Hungary 2006 Review*, IEA: Paris, 2007, p.106.
[188] "Hungarian gas co. signs deal with Gazprom," *AFX International Focus*, June 21, 2006.
[189] "EU experts to mull Adriatic pipeline as alternative to Russian gas," *AFX News Limited*, Jan. 4, 2006; "Croatia, Hungary plan sea terminal for EU-bound gas," *Agence France Presse*, May 17, 2007.

monitor gas supply and consumption across the region."[190] Yet another suggestion made at a Hungarian-sponsored meeting of Central European states in 2006 involved connecting the gas distribution and storage facilities of states in the region.[191] Connections of this kind could significantly boost the energy security of Central European states by putting an end to market segmentation and allowing countries to share gas more effectively in the event of a supply interruption. At the private sector level, MOL (Hungary's national oil company and manager of the country's gas distribution network) is working on a concept known as the New Europe Transmission System (NETS) to bring this idea into reality.[192]

And Hungary does talk of being a Nabucco supporter. Economy Ministry officials and MOL representatives have held talks with Caspian-area governments to drum up support for Nabucco.[193] In February 2008, the Hungarian government drafted the intergovernmental contract designed to lay the regulatory groundwork for the Nabucco pipeline.[194] Hungarian officials insisted that "the fact that the Hungarian government has drafted the contract in just two weeks shows the importance that Hungary attaches to the [Nabucco] project and its commitment to it."[195] But it's also possible that the Hungarian government put the contract together in such a timeframe in order to blunt criticism of an announcement – just a few days later – of increased Hungarian-Russian partnership in pipeline politics.

Over approximately the past year, Hungarian leaders have shown signs of waffling on Nabucco for the sake of commercial cooperation with Gazprom, raising the question of where Budapest's priorities lie. As mentioned previously, Hungary is Gazprom's top customer in Central Europe,[196] but Hungary wants to be a regional transit, storage and distribution center for the Russian company. This could make privately-owned MOL even more profitable and influential in Central Europe's energy sector.[197] Austria – and to a lesser extent Serbia – are regarded as competitors in a battle to be Gazprom's favorite hub.[198]

In a move that led many to question Hungary's commitment to the EU-backed pipeline, Hungary in 2006-07 offered words of support for Gazprom's plans to extend Russia's Blue Stream pipeline westward from Turkey into Central Europe. [199] Hungary was offered the prospect of being a pivotal transit point. EU officials complained that Hungary was undercutting Nabucco (and thus a common EU energy policy), but Hungary's Prime

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[190] "CEE governments led by 'Visegrad Four' meet on energy security after Russian/Ukraine gas row," *Hungary Business Newswire*, Jan. 27, 2006

[191] Ibid; "Hungary and Croatia sign energy cooperation memorandum to cut dependence on Russia gas," *Central Europe Energy Weekly*, Jan. 27, 2006.

[192] Vladimir Socor, "NETS – Joint Gas Transmission Network Proposed in Central and Southeastern Europe," *Eurasia Daily Monitor*, December 10, 2007; Zoe Grainge, "MOL to Co-ordinate Meeting to Establish South-Eastern Europe Transmission Firm," *Global Insight*, Feb. 20, 2008.

[193] "Kóka: Hungary wishes prompt delivery of Azerbaijani gas to Europe," bbj.hu, Nov. 23, 2007.

[194] "Hungary draws up framework contract for Nabucco gas pipeline," *Agence France Presse*, Feb. 20, 2008.

[195] Economy Ministry spokesman Abel Garamhegyi quoted in: "Hungary draws up framework contract for Nabucco gas pipeline," *Agence France Presse*, Feb. 20, 2008.

[196] "Distribution/Europe," Gazprom website. Available at <http://www.gazprom.com/eng/articles/article20160.shtml>.

[197] Neil Barnett, "Gazprom: the hidden hand," *The Spectator*, Oct. 31, 2007.

[198] See: "Gazprom may shun Hungary, favor Serbia," *World Gas Intelligence*, Oct. 24, 2007; "Focus – Pipelines – Planning to make Nabucco dream a reality," *Petroleum Economist*, December 2007, p.26; Slobodan Lekic, "Moscow's friendship with Serbia part of a power play rooted in economic interest," *The Associated Press*, Feb. 28, 2008.

[199] See for example: Judy Dempsey, "Hungary chooses Gazprom over EU," *International Herald Tribune*, March 12, 2007.

Minister Ferenc Gyurcsány stated that Nabucco "has been a long dream and an old plan. But we don't need dreams. We need projects."[200] It was unclear however whether this was the message the Prime Minister wanted to send. A few months later, Gyurcsány appeared to reverse course, pledging his "total support" for the Nabucco pipeline and even explicitly stated "our job is to find gas resources independent of Russia."[201]

The Hungarian government and Gazprom stepped up their cooperation in 2008. It's possible that Budapest is looking for an insurance policy should Nabucco fall through. Hungarian President László Sólyom reiterated Hungary's wish to participate in South Stream on Feb. 5, 2008, stating that he hoped the South Stream would extend to Hungary.[202] He appeared to get his wish when Medvedev flew to Hungary to meet with Gyurcsány on Feb. 25. The two men made an inter-governmental agreement to affirm Hungary's participation in South Stream, despite Hungary's Nabucco commitments just a few weeks earlier.[203]

On Feb. 28, 2008 in Moscow, Gyurcsány officially signed the accord with Putin, and seemed to voice praise for the Gazprom pipeline: "You [in Russia] were faster than Nabucco. And it is up to us to determine the tempo of implementing projects in our interest"[204] – a possible snub to U.S. requests for "sequencing" pipelines in a way that would give preference to Nabucco.[205] He also seemed to go out of his way to thank Putin's Russia for its partnerhip in the energy realm. "It is with satisfaction and gratitude that I see Russia doing everything it has promised to us. Hungary has realized that it had no alternative to cooperation with Russia."[206] Hungary is expected to sign an actual contract for South Stream this year.[207] On April 1, 2008, Hungary appointed a special Ambassador-at-large for the Nabucco pipeline. And as this report was being finalized for publication, Gyurcsány proposed to organize a summit to kickstart momentum for Nabucco.[208] The jury is still out on whether this constitutes a fig leaf or a an actual change of course.

At times, MOL seems more interested than the Hungarian government in the Nabucco pipeline. Company officials have said that the government's decision to join South Stream was a surprise,[209] and have hinted that the firm never would have made such a move from a pure business standpoint.[210] Also, MOL has proposed a political oversight group for Nabucco to deliver "the needed momentum" and harmonize political support for the project.[211] Yet MOL and Gazprom are exploring ways to cooperate on South Stream, as

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[200] Ibid.

[201] Quoted in: Ed Crooks, "Hungary's about-turn helps put Nabucco pipeline back on agenda," *Financial Times*, Sept. 18, 2007.

[202] "President Solyom backs both Nabucco, South Stream gas pipelines," *The Budapest Times*, Feb. 5, 2008. Available at <http://budapesttimes.hu/index.php?option=com_content&task=view&id=5148&Itemid=101>.

[203] Stefan Wagstyl, Kester Eddy, and Neil MacDonald, "Hungary backs Russian pipeline," *Financial Times*, Feb. 26, 2008.

[204] Quoted in: "Russia, Hungary Sign South Stream Pipeline Deal," *International Herald Tribune*, Feb. 28, 2008.

[205] See: Matt Bryza, Deputy Assistant Secretary of State for European and Eurasian Affairs, Interview with Hungarian News Agency, Washington, DC, Feb. 26, 2008.

[206] Quoted in: Vladimir Socor, "South Stream Gas Project Defeating Nabucco by Default," *Eurasia Daily Monitor*, March 5, 2008.

[207] "Hungary to Sign South Stream Contract in H1," *Hungarian News Agency (MTI)*, April 16, 2008.

[208] "Hungary to organize Nabucco gas pipeline summit," EUBusiness.com, July 10, 2008. Available at <http://www.eubusiness.com/news-eu/1215693122.68/>.

[209] Andrei Glazov, "Mol Left Out of Hungary's South Stream Deal," *International Oil Daily*, Feb. 27, 2008.

[210] Conversations in Washington, DC, April 2008.

[211] "MOL proposes political group to oversee development of Nabucco pipeline," *Thomson Financial News Super Focus*, April 1, 2008.

the Hungarian firm will now offer underground storage facilities for the Russian pipeline's gas.[212]

Hungary is pushing equally hard on the accelerator and the brake of European energy security at the same time. The country's desire for diversification is balanced with its wish to remain a major Gazprom partner and reap the benefits of being a hub for Russian gas in Central Europe. In the game of energy geopolitics, Hungary is at least making some of the right noises, but one has a hard time taking its leaders' statements seriously.

Slovakia: A Highway for Russian Gas

To the extent that relations with Russia in the energy sphere mirror political ties, Slovakia is a good case in point. Since coming to power, the current Socialist Prime Minister Robert Fico has engaged Moscow to cultivate friendly bilateral ties.[213] Slovakia is a market for Russian arms sales, and Putin and Fico have found common ground on a number of issues in foreign and security policy.[214] In the energy sphere, Slovakia is content with its role as a "highway for Russian gas."[215]

The previous government of Mikulás Dzurinda appeared ready to commit to energy diversification. Immediately after the Ukraine crisis, Slovakia under his leadership joined with Poland and the other Visegrad states (along with Austria) to insist on EU support "on both the political and financial level" to access non-Russian supplies of oil and gas as well as enlarge gas pipeline connections in the region.[216] However, Fico's entry to the political scene seems to have curbed strategic thinking in Slovakia. Slovak diplomats insist that their country views energy security as an element of national security,[217] but actions often speak louder than words.

As in the case of Hungary, Russian energy firms have developed good relations with a left-leaning coalition in Bratislava. Other explanations as to why Slovakia is so warm to Russian energy companies are more structural; a tremendous amount of Russian gas transits Slovak territory. The country transits a total of 59.2 bcm of Russian gas annually (representing an increase of 18 percent in 2008),[218] and Slovakia is Gazprom's most important customer for gas in Central Europe after Hungary.[219] Fico has agreed that energy trade will be at the heart of Russo-Slovakian cooperation moving forward.[220] In May 2007, the Slovak premier offered praise for Russia's role as an energy supplier, saying "we believe that Russia is a reliable, promising partner in energy supplies…"[221]

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[212] Zoe Grainge, "MOL to Offer Underground Storage for South Stream," *Global Insight*, May 8, 2008.
[213] "Central Scenario for 2008-09: International Relations," *Country Risk Service Select*, Nov. 1, 2007.
[214] For more on current Russian-Slovak relations see: Uba Lesna, "Searching for the Right Tone with Russia," *The Slovak Spectator*, June 29, 2008.
[215] Executives in Slovakia's gas transmission company have touted the firm as such a highway. See: "Slovakia Streamlines Gas Role," *Nefte Compass*, Nov. 21, 2007.
[216] "Poland says whole EU should be involved in finding solution to gas-supply problem," *Hungary Business Weekly*, Jan. 6, 2006.
[217] Briefing in Washington, DC, May 2008.
[218] "Russian natural gas transit volume through Slovakia to increase 18% in 2008," *Central Europe Energy Weekly*, Feb. 22, 2008.
[219] "Distribution/Europe," Gazprom website. Available at <http://www.gazprom.com/eng/articles/article20160.shtml>.
[220] "Russia's Putin, Slovakian Prime Minister discuss gas, nuclear cooperation," *The Associated Press*, May 4, 2007.
[221] Ibid.

Putin, for his part, has offered kind words about Slovakia. "The importance of your country is not limited to the volume of our energy resources you consume… you are also a most important transit country for our gas to Europe," he once told his Slovak counterpart.[222]

According to some media reports, Bratislava harbors few concerns about the security of Russian supplies, with Slovak officials saying that Russia is equally dependent on Slovakia for its transit pipelines.[223] Because the Slovaks are happy to play this transit role, Bratislava tends not to get on Moscow's or Gazprom's bad side. As a case in point, Bratislava is also against the EU Commission's proposals on energy unbundling. Rules governing external takeovers could be important for the Slovaks;[224] Russia could potentially leverage the renewal of its gas contracts with Bratislava in order to acquire additional equity in Slovakia's energy sector.

Furthermore, according to some estimates, the volume of Russian natural gas transited through Slovakia will decrease by about 10 bcm per year after the Nord Stream consortium opens its planned gas pipeline under the Baltic Sea.[225] As a result, Gazprom could serve customers like the Czech Republic and Germany without need of Slovakia – if the Russian firm so desired.[226] To get a good deal on gas supply and gas transit, the Slovaks may be tempted to offer up more of the country's energy assets to companies like Gazprom.

Alternatively, this development could push the Slovaks closer to the strategic players' side of the schism by supporting MOL and its NETS initiative. A sea change could already be underway now that Slovakia could lose out when Nord Stream comes online. Slovakia is now taking an increased interest in linking Central European pipelines to maintain Slovakia's transit importance.[227] So Slovakia could take advantage of its position at the heart of Central Europe to move NETS forward – even if the driver is perhaps not blunting a Russian-inspired supply disruption so much as preserving Slovakia's transit role.

If it wanted, Slovakia could make a more demonstrated effort at being a strategic player. For instance, Slovakia did not have to put its signature to the "Third Option" proposal that effectively would remove the Gazprom clause from the Commission's energy package (among other changes).

It is also noteworthy that Russia has often set the Slovaks in opposition to the Poles. As discussed earlier, Slovakia is keen to link Odessa-Brody up with the Druzba pipeline system passing over Slovak soil – a move which would undercut Polish aims to bring the oil corridor north. Russia has also proposed to lay a second gas pipeline across Poland to Slovakia, where it would connect with existing Russian gas lines. In effect, this would put

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[222] "Putin calls Slovakia a key transit country for Russian gas heading to Europe," *The Associated Press*, Nov. 6, 2006.
[223] Robert Anderson et al, "Moscow's past satellites take keen interest in energy talks," *Financial Times*, July 12, 2006.
[224] "Central scenario for 2008-09: International relations," *Country Risk Service Select*, Nov. 1, 2007.
[225] "Baltic Sea Nord Stream pipeline to reduce gas transited via Slovakia by 10 bln cubic meters a year," *Central Europe Energy Weekly*, Nov. 17, 2007.
[226] Sally Bogle, "Nord Stream to Cut Slovak Gas Transits by 10-bcm/year; SPP to Become Eustream from January," *Global Insight*, Nov. 19, 2007.
[227] Discussions in Washington, DC, April-May 2008.

added pressure on Ukraine by potentially allowing Russia to reduce gas flows through the ex-Soviet state – something Poland would be reluctant to do (Poland would prefer a line parallel to the existing Yamal-1 pipeline en route to Germany). But Slovakia's overall priority is not regional solidarity so much as sustaining and increasing transit revenues. Because of such actions, Slovakia gets the lowest marks among the Visegrad on its diversification scorecard.

Bulgaria: The More Pipelines the Merrier

Bulgaria's strategy centers on making good use of its location to earn a profit. The problem is that this approach effectively makes the country Russia's strategic beachhead in Southeastern Europe. Indeed, Bulgaria is emerging as a key transit point for Russian oil and gas headed to European and world markets, and the country's leaders have openly said that the more pipelines (Russian or not), the merrier. This does not mean Bulgaria is not a loyal member of the EU or NATO, nor does it preempt it from supporting Western-backed energy projects. But it suggests that Sofia looks first and foremost to acquire revenues from transit fees, which means cooperating with Russian projects regardless of whether they undermine Western-backed alternatives. In Nov. 2006, Bulgarian Energy Minister Rumen Ovcharov summed up the government's position like this: "In spite of the calls to reduce dependence of European countries on Russian energy resources, Bulgaria will not focus on diversification of fuel suppliers."[228] Displaying a combination of realism and short-sightedness, he said "we will secure long-term [Russian] natural gas deliveries first, and then start thinking about diversification."[229]

From the perspective of Russian pipeline planners, Bulgaria is a natural springboard to Greece, Italy, the Western Balkans and points in the heart of Europe. Russian state-owned firms have made use of Bulgaria's prime real-estate for advancing the reach of their oil and gas exports, and the Bulgarians have been ready to partner. "The time has come to reap the benefits from our geographic position," President Georgii Parvanov proclaimed on the eve of Vladimir Putin's visit to Sophia in January 2008 for talks on energy projects.[230]

To some extent, Bulgaria might not have much choice. Bulgaria relies on Russia for nearly all its oil and gas supplies. One could argue that only by offering itself as a transit hub, can Bulgaria placate its big brother and secure long-term energy supplies. Still, the contrast between the Romanian and Bulgarian approaches is pronounced and runs parallel to the character of bilateral relations with Moscow. When Putin promoted South Stream at an energy conference in June 2007, Parvanov indicated his country's interest in joining the project then and there.[231] To some extent, this stood in contrast to the Romanian leader's declared support for Nabucco at the same event.[232]

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[228] Quoted in: "Bulgaria Disappointed with European Energy Security Strategy," *The Russian Oil and Gas Report*, Nov. 8, 2006.
[229] Ibid.
[230] Quoted in: Anna Smolchenko, "South Stream Signed After Night Out," *The Moscow Times*, Jan. 21, 2008.
[231] Vladimir Socor, "Bulgaria Seduced by South Stream Gas Project?," *Eurasia Daily Monitor*, Sept. 14, 2007.
[232] Ibid.

Under the current setup of Parvanov and fellow Socialist Premier Sergei Stanishev, relations have grown stronger.[233] At times, the Bulgarian government has been accused by its detractors of being "pro-Kremlin."[234] When Poland, the Czech Republic, Slovakia, Austria, Hungary, Slovenia, Croatia and Romania met in early 2006 to discuss ways to accelerate projects to help Europe diversify away from dependency on Russia, Bulgaria declined an invitation to join this energy bloc.[235] Bulgaria's joining with Germany and others intending to dilute the EU Commission's energy market reform proposals in spring 2008 was also not helpful. Amid growing Bulgarian-Russian trade ties, Russian diplomats have quipped that Bulgaria could serve as Russia's "Trojan horse" in EU circles.[236] Government critics have latched onto this Trojan horse theme. During Putin's pipeline diplomacy stop in Sofia in January 2008, opposition parties and NGOs denounced attempts to make Bulgaria the "Trojan horse of Putin's oligarchy" in the EU.[237] "Putin is coming to Bulgaria to sign Bulgaria's total economic dependence on Russia," opposition protesters said in a statement.[238]

On the oil front, Bulgaria has partnered with Russia to construct the Burgas-Alexandroupolis pipeline – the first oil pipeline on EU soil with majority Russian ownership[239] – linking the Black Sea to the Mediterranean through Bulgaria and Greece. In the field of gas, Bulgaria represents an equally stalwart partner for Russia. Most notably, Bulgaria is central to Gazprom's South Stream project. As discussed above, the planned undersea pipeline will come ashore in Bulgaria and travel onward to Italy and other European markets. Russia and Bulgaria signed an agreement on South Stream's construction in January, during Putin's visit to Sofia.[240] Bulgaria could gain transit revenues possibly in the range of $250-400 million per year.[241] Gazprom and its Bulgarian counterpart are due to sign an agreement for a joint company that will plan the section of the South Stream gas pipeline passing through Bulgaria.[242]

Officially, Sofia backs both South Stream and Nabucco. Interestingly, Parvanov stated on Feb. 5, 2008, that his country was ready to visit with possible suppliers of gas for Nabucco, and that he expected a "much more active position" from both Brussels and Washington.[243] This could be an effort to say that Bulgaria is prepared to play for the Western team, provided that a team captain is put in place.

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[233] Janusz Bugajski, *The Eastern Dimension of America's New European Allies*, Carlisle Barracks, PA: Strategic Studies Institute, U.S. Army War College, Oct. 2007, pp.147-148; "Vladimir Putin had a conversation with Bulgarian Prime Minister Sergei Stanishev," Website of the President of the Russian Federation. Available at <http://www.kremlin.ru/eng/events/chronicle/2007/03/119764.shtml>.
[234] Claudia Ciobanu, "Bulgaria: Addicted to Russia's Energy," IPS News, May 4, 2007. Available at <http://ipsnews.net/news.asp?idnews=37610>.
[235] Sally Bogle, "Bulgaria Reconsiders Central European Energy Bloc; Poland Mulls Norway-Sweden Pipeline," *Global Insight*, May 1, 2006.
[236] Russian official quoted in: Mark Leonard and Nicu Popescu, "A Power Audit of EU-Russian Relations," Policy Paper, European Council on Foreign Relations, November 2007, p.27. Original source: Interview with Vladimir Chizhov, Capital magazine, Nov. 10, 2006. Available at <http://www.capital.bg>.
[237] Elena Koinova, "Days of Putin in Bulgaria," *The Sofia Echo*, Jan. 18, 2008.
[238] Vladimir Isachenkov, "Bulgarian PM says pipeline deal will be signed with Russia," *Associated Press*, Jan. 18, 2008.
[239] Russian companies own 51 percent of the project. Vladimir Socor, "First Russian-Operated Pipeline on European Union Territory Rears Its Head," *Eurasia Daily Monitor*, March 2, 2007.
[240] "Moscow, Sofia to sign South Stream agreement in January," *European Gas Markets*, Nov. 16, 2007.
[241] Elitsa Savova, "Putin to discuss South Stream construction during visit to Bulgaria," *The Sofia Echo*, Jan. 14, 2008. Available at <http://www.sofiaecho.com/article/putin-to-discus-south-stream-construction-during-visit-to-bulgaria/id_27035/catid_67>.
[242] "Bulgargaz and Gazprom joint venture to build pipeline," *New Europe*, May 5, 2008.
[243] "Bulgaria, Hungary discuss diversification of energy resources in Europe," *The Associated Press*, Feb. 5, 2008.

For the time being, however, Bulgarian leaders effectively support whichever pipeline gets to Bulgarian soil first. To the country's credit, President Parvanov visited Azerbaijan on March 10, 2008, and stated that Bulgaria was committed to Europe's energy security and that he was there "with the message to boost work on the European Nabucco project."[244] But this by itself is not enough. Bulgaria has thus far shied away from articulating a clear preference between Nabucco and South Stream. Should the Bulgarians involve themselves with the MOL-led NETS initiative on inter-connector pipelines, this could move their country away from Gazprom's crib. Disappointingly, Bulgaria's company declined the invitation to attend the first meeting (March 2008) of the gas transmission companies considering the project.[245] On a more positive note, Bulgaria's state-owned Bulgargaz is now in talks with Romanian firms on ways to connect the two countries' gas networks.[246]

The Emergence and Deepening of Central Europe's Schism

An important point to take away from the picture painted above is that Central Europe's energy security schism has gotten deeper. Each of the latter five states – Latvia, Slovenia, Hungary, Slovakia and Bulgaria – have edged closer to the Russian position in one way or another during the past two years. To review: Latvia seems to be breaking with Baltic solidarity in pursuit of a more ambiguous relationship with Russian energy companies; Slovenia has recently prepared to join South Stream; Hungary has been flirting with Gazprom for the past two years in an effort to be a Russian gas hub; Slovakia's new government is pursuing entente with Moscow on a number of levels, including energy, being eager to maintain its transit importance; and Bulgaria is renting itself out to Russian energy projects, regardless of their implications for other pipelines favored by the West. Interestingly, there is a weak link of sorts in every corner of Central Europe – the Baltic region, the Visegrad, the Southern tier and even geographical outlier Slovenia.

A number of important questions present themselves: is this schism likely to persist into the future? In moving forward, which approach – the strategic or opportunistic – will predominate? The crystal ball is murkier than a Gazprom intermediary, so only time will tell. But in thinking about these questions it is worth exploring how and why the schism looks the way it does, and why Central European divisions have become more pronounced in recent years.

One reason is a divergence as to how elites in Central Europe understand the admittedly vague concept of "energy security." For some, simply getting stable energy supplies at predictable prices in the short-term is enough. In essence, not having enough Russian gas is the real fear. Further complicating matters is the penchant today among some states – Slovenia, for instance –to throw environmental concerns into discussions on energy security. For those reluctant to place their eggs in the Kremlin's goody basket – such as the Poles and the Lithuanians – energy security implies diversification of suppliers in

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[244] "Bulgaria Ready to Buy Gas from Azerbaijan," *Bulgarian News Agency (BTA)*, BBC Monitoring Reports, March 10, 2008.
[245] "Eastern Europe To Study Integrated Transportation," *Nefte Compass*, March 20, 2008.
[246] "Transgaz, Bulgargaz to interconnect natural gas networks," *SEE Security Monitor*, June 10, 2008. Available at <http://www.csees.net/?page=news&news_id=67590&country_id=6>.

order to create a greater freedom of choice. They rightly recognize that energy security is linked to national sovereignty.

Obviously, the country-by-country breakdown of energy security perceptions is partly a function of historical and structural factors. For instance, Poland and the Baltic States have historically had cooler relations with Russia than the other countries of Central Europe. As a result, they are more inclined to see energy security questions through a strategic lens. Romania too is wary of Russian influence, and Romanian interests in the Black Sea region sometimes run counter to Russian policy. Another factor is national resource endowments. Romania and Poland's domestic energy deposits serve as a confidence-booster for the two strategic players.

However, it would be silly to pretend that national political parties (and particular leaders) do not matter. Other things being constant, center-Left governments in Central Europe are less Atlanticist and more inclined to tack towards commercial opportunism. In the energy sphere, this means countries governed by left-leaning leaders are more likely to be tempted by Russian policies designed to trip up the strategic players. Government changes can therefore serve as serious exogenous shocks to Central Europe's energy security schism. Elections in Romania, Lithuania and Hungary loom on the horizon.

A second factor is clearly Russian policy. The Kremlin utilizes a number of measures, notably the tactic of "supply preemption," which is used to exacerbate schisms among Central European states. As a case in point, Russia's South Stream competes with Nabucco for both customers and suppliers; it is not clear that Southeastern Europe can absorb an additional 60 bcm of gas (equal to the combined volume of both proposed pipelines), and both projects hope to access Turkmen gas.[247] South Stream also has certain advantages in the pipeline race. The Gazprom-backed pipeline comes with the promise of both gas and capital investment (Nabucco is currently having a hard time coming up with either).

The Putin-Medvedev tandem has closely managed this Russian campaign against Nabucco, meeting personally with the leaders of countries along Nabucco's route. Doing so, they have aimed to convince local politicians that Western hopes for Nabucco are unrealistic and that these countries would be better off with the immediate transit revenues from Russia's South Stream.[248] The prospect of becoming an energy hub is another sweetener to defect from Western energy security priorities. Some officials involved in the Nabucco project now appear ready to admit defeat, even suggesting that the pipeline could be filled with Russian gas[249] – a move that would defeat the original purpose of the pipeline.

Third, the lack of any common EU energy policy contributes to a schism-prone environment. Many in Europe talk about the need for a common approach to Russia in

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[247] Vladimir Socor, "Agreement to Integrate Bulgaria Into Russia's Gas Network," *Eurasia Daily Monitor*, Jan. 24, 2008. See also: "Turkmen Leader to discuss Nabucco in Turkey," *Reuters*, March 24, 2008.
[248] See Katinka Barysch cited in: "Dreams of gas hubs," *Petroleum Economist*, April 2007.
[249] See: Judy Dempsey, "EU-sponsored pipeline to open up to Russian gas," *International Herald Tribune*, Feb. 6, 2008; Vladimir Socor, "Nabucco Gas Project Facing A Cascade of Defections," *Eurasia Daily Monitor*, Feb. 28, 2008; "Turkey says Nabucco may take Iranian, Russian gas," *Turkish Daily News*, March 19, 2008. Available at <http://www.turkishdailynews.com.tr/article.php?enewsid=99398>.

the energy sphere, but in practice the EU keeps hitting the snooze button, being unwilling or unable to wake up to the problem. The Union's executive branch (as embodied by the European Commission) often finds itself at odds with Europe's constituent parts (the member states). EU legislation is very clear in granting responsibility for determining one's energy mix to national governments. So coordination in the energy sphere is undermined by a prisoner's dilemma; rather than cooperate, many EU states aim to lock-in their own gas supplies and enrich their national oil and gas companies at the expense of European unity. National interests have undermined support for certain common policies, including movement towards a common external approach to Russia, commission proposals on energy market liberalization and diversification projects like Nabucco.

Select member states in West Europe serve as particularly bad role models for their partners in post-communist Central Europe. In particular, the policies of a number of large European countries revolve around the interests of their respective national oil and gas firms. Because they are reluctant to confront Russia on its energy monopoly, bilateral deals with Russia (instead of European unity) are sadly the norm.

Due to Great Britain's distance from Russia and its remaining indigenous gas resources, energy relations between London and Moscow are less salient. Still, Britain is conscious of the need to avoid jeopardizing British Petroleum's (BP) extensive operations in Russia. Across the English Channel, Total and Gaz de France also pursue business opportunities in Russia's energy sector – something which is not missed inside the *Palais de l'Élysée*. Gaz de France extended its natural gas contracts with Gazprom in 2006,[250] and Gazprom awarded Total a major stake in its offshore Shtokman gas project in the Barents Sea last year.[251] Such moves can be seen as Russian attempts to create stakeholders in the Franco-Russian relationship and increase the likelihood that France will be a voice on which Gazprom can rely. Furthermore, the Italian government and Italy-based energy firms like Eni have bought the Gazprom argument. Eni worked with Gazprom on creating the Blue Stream pipeline under the Black Sea to Turkey, even though this move undercut efforts to build a trans-Caspian pipeline (backed by the United States and others in the West).

Austria, though small, holds special importance for Russia in the energy sphere. Last year, Putin praised Austria as "the biggest and, I stress this, the most reliable transit agent for Russian gas."[252] Earlier this year, Gazprom and OMV struck an agreement for turning Austria's Baumgarten gas transmission center into a joint venture.[253] At the time of this writing, it is unclear whether this deal will move forward because of Gazprom-OMV disagreements. In any case, the move illustrates how Austria can be something of an energy turncoat; the Baumgarten facility is the designated endpoint for the Nabucco pipeline, and offering joint ownership to Gazprom could have deprived Nabucco of its final outlet.[254] Along with Austria, Greece is another member of Western Europe eager to

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[250] "Gaz de France and Gazprom extend their natural gas supply agreements until 2030," Gaz De France Press Release, Dec. 19, 2006. Available at <http://www.gazdefrance.com/EN/A/2640/gaz-de-france-and-gazprom-extend-their-natural-gas-supply-agreements-until-2030.html>.
[251] "Gazprom and Total sign Shtokman deal, which Total says will allow it to book reserves," *International Herald Tribune*, July 13, 2007.
[252] Karin Strohecker, "RPT-ANALYSIS-OMV-Gazprom deal revives fear of Russia," *Reuters*, May 25, 2007.
[253] Brian Whitmore, "Russia: Gazprom's Advance into Europe Continues," *RFE/RL*, Jan. 25, 2008.
[254] Vladimir Socor, "OMV Joins With Gazprom to Undercut Nabucco," *Eurasia Daily Monitor*, Jan. 29, 2008.

be part of South Stream. In late April 2008, Greek Prime Minister Costas Karamanlis praised Putin as "a great European leader and a friend of Greece"[255] before flying out to Moscow to sign a deal with the Russian leader on Greece's participation in the pipeline.[256] Russia's relationships with Austria and Greece are complemented by increasingly close ties to Serbia in the energy sector.[257] The presence of this Vienna-Athens-Belgrade energy axis puts pressure on other states in Southeastern Europe to bandwagon with Russia on its pipeline projects.

But Germany is the prime culprit standing in the way of a common EU energy policy. Under former Chancellor Gerhardt Schröder, Germany snubbed multilateral approaches to energy security in favor of a more unilateral pursuit of German business interests.[258] In particular, Germany's willingness to partner with Russia on Nord Stream without consulting Poland or the Baltic States undermined European trust and solidarity. Though there is a rational argument for getting more Russian gas to German markets, the route looks entirely political; designed to punish Central Europe's Northern tier for joining NATO and increase their susceptibility to Russian pressure. Germany, as an important ally and neighbor to Central Europeans, should have shown greater solidarity with its Polish and Baltic partners and supported an overland option instead of Nord Stream.

Since the 2005 parliamentary elections in Germany, Chancellor Angela Merkel has worked to alter German policy and distance herself from the excessive *Ostpolitik* of her predecessor. Although her efforts have met with some success, it is difficult to change policy in such a manner due to domestic political concerns. As Ed Lucas describes:

> "Merkel is fighting on two fronts: against the anti-American left, and against the pro-business right, both of which are willing to overlook the Kremlin's shortcomings for reasons of their own. Even her own party allies seem open to the blandishments of a special friendship with Russia. For all Merkel's efforts, the fact remains that Russia has unparalleled influence in Germany, which seems to survive even a sharp change of political tone at the top."[259]

Soon after the 2006 Ukraine crisis, German officials called for "a more powerful approach" by the EU in its external energy relations.[260] However, Germany has yet to put its money where its mouth is.

To some extent, commercial opportunists in the region know Russia's gas deficit is coming, and thus feel the need to strike bilateral deals with Gazprom – especially when states like Germany have already reserved their gas early. Bulgaria's Energy Minister Roumen Ovcharov put it like this: "We all talk about how bad Gazprom and Russia are… But this talking did not stop France from signing a 30-year contract for Russian natural

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[255] Quoted in: "Greece readies for Russian energy Bear Hug," *New Europe*, April 28, 2008.
[256] Olga Rotenberg, "Russia, Greece ink deal on South Europe gas pipeline," *Agence France Presse*, April 29, 2008.
[257] See: "Serbian govt approves oil, gas accord with Russia's Gazprom," *Prime-Tass*, May 12, 2008.
[258] Kirsten Westphal, "Germany and the EU-Russia Energy Dialogue," in Pami Aalto (ed.), *The EU-Russian Energy Dialogue: Europe's Future Energy Security*, Burlington, VT: Ashgate, 2008, pp.93-119.
[259] Edward Lucas, *The New Cold War*, New York: Palgrave Macmillan, 2008, p.174.
[260] Frank-Walter Steinmeier, "Energy Security: Avoiding Conflict Over Fuel," *International Herald Tribune*, March 23, 2006.

gas, nor did it stop Germany from doing the same as well as Austria."[261] The Minister continued, "What should Bulgaria do? Stop talking to Gazprom and be left without gas?"[262] Central Europe lacks good role models in the face of a common problem. Germany not only sets a bad example, it is also something of an obstructionist when it comes to a common energy policy. As already discussed with respect to Latvia, the EU Commission put forth an energy liberalization proposal in September 2007 that contained a robust "reciprocity clause" for energy relations with third countries.[263] Germany has been a major obstacle to the Commission's energy proposals, including the Gazprom clause, even though many observers recognize the clause's necessity. "We need to take precautions against gas companies who come in and take over gas pipelines," said Member of the European Parliament Anne Laperrouze.[264] Russia is able to rely on German energy firms, keen to preserve their "national champion" status at home and acquire additional business abroad (including in Russia), to lobby in concert with Gazprom's interests. Germany remains unsympathetic to Poland's strategic view of energy security, and continues to be a serious obstacle to the formation of a common EU energy policy. This, in turn, helps fuel the emergence of the energy security schism in Central Europe.

A fourth factor driving the schism is that attempts at regional unity within Central Europe have not panned out. There was a chance following the Ukraine crisis when the Visegrad Group showed leadership, but hopes for an energy security "caucus" have since faded. Right after the Ukraine gas crisis of Jan. 1, 2006, the Visegrad states of Poland, Hungary, the Czech Republic and Slovakia took the lead, holding a conference call on Jan. 3 to develop a common position on the Russian-Ukrainian gas dispute.[265] A Polish statement stressed that "the Visegrad Group thinks that it is necessary that the European Union provides support for [supply diversification measures] on both the political and financial level."[266]

These states then brought other capitals in the region on board, and the energy ministers of eight countries (the V4 plus Austria, Slovenia, Croatia and Romania) met on two occasions in spring 2006 and agreed to a broad plan in the area of energy security.[267] But the movement towards Central European unity soon hit a few bumps in the road. To begin, Russia stepped up its lobbying efforts in Central European capitals in an effort to co-opt select countries (Austria and Hungary) and tempt them with lucrative energy deals. Bulgaria, a key player in the Balkans and a close Russian partner in the energy sector, did not join the Visegrad-8 grouping. Second, elections in Slovakia brought in a Socialist government that was keen to warm up to Moscow. Meanwhile, the European Union showed no signs of developing a common position or thinking seriously about alternatives to Russian gas supplies.

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[261] Quoted in: Claudia Ciobanu, "Bulgaria: Addicted to Russia's Energy," *IPS News*, May 4, 2007. Available at <http://ipsnews.net/news.asp?idnews=37610>.
[262] Ibid.
[263] "'Gazprom clause' issues Russia ultimatum for energy co-operation," Euractive.com, Sept. 20, 2007.
[264] MEP Anne Laperrouze of France quoted in: "Energy security fears stoked by the "Gazprom" clause," *New Europe*, March 3, 2008.
[265] "EU needs common energy policy – Hungary,"*Agence France Presse*, Jan. 3, 2006.
[266] Polish government statement cited in: "Poland says whole EU should be involved in finding solution to gas-supply problem," *Central Europe Energy Weekly*, Jan. 10, 2006.
[267] Christopher Condon, "Central Europe seeks EU help over Russian gas supplies," *Financial Times*, Jan. 28, 2006.

As a result of these four dynamics, commercial opportunism has begun to surface and the Central European game plan on energy security is largely disaggregated. Looking ahead, some of these schism-drivers will continue to exist. Those disposed towards a more relaxed view of energy security are unlikely to change their mind anytime soon, especially since non-Russian options for gas diversification are admittedly limited. Russia will not offer any relief, for it will continue to aggressively play its cards in Central Europe's energy geopolitics, using a combination of bilateral deals, supply pre-emption and transit preference. This in turn will complicate both EU and Central European unity in energy matters. In short, energy divisions look to be here to stay.

One possible wild card further down the road could be the completion of a NETS-like system for Central Europe that reduces market segmentation. This is one project that practically all European countries can support; creating inter-connector pipelines in the region would essentially emulate that which exists already in parts of Western Europe. It's possible that inter-connector pipelines will give countries like Hungary, Slovakia and Bulgaria greater self-confidence in treating with Russia, prompting them to move closer to the strategic camp. At any rate, inter-connector pipelines are still in the distant future. A system like NETS for Central Europe won't happen overnight, nor will it be done free-of-charge. For the time-being, Central Europe will therefore continue to be split between strategic players and commercial opportunists.

Commercial Opportunism and U.S. Interests

Aside from undermining EU attempts at unity and contributing to a disjointed transatlantic approach to Russia's energy monopoly, Central Europe's energy security schism challenges U.S. interests. For starters, commercial opportunism of the kind described creates hurdles for U.S. diplomats engaged in pipeline diplomacy. Second, the opportunists could create a pro-Gazprom (and possibly pro-Russia) caucus within the European Union and NATO.

Though European countries are the ones who will ultimately access any non-Russian sources of oil and gas in Eurasia, it seems at times as if the EU has outsourced its Caspian energy diplomacy to Washington. On the whole, folks in the Black Sea-Caspian energy corridor looked first to the United States, rather than the EU, to play the role of an aligner of interests to bring projects like Nabucco to fruition. The U.S. State Department's official justification for getting involved in European energy security is first and foremost its position that energy monopolies are not desirable,[268] especially "when they threaten at least the economic security of [America's] most important allies."[269] From a realist point of view, the U.S. stake in Central Europe's energy security is both altruistic and selfish at the same time.

On the altruistic side, Washington genuinely does want to help its partners realize their own goals. As such, U.S. support for pro-diversification voices centers around the concept

[268] Matthew Bryza, "Outflanking Russia's energy grip on Europe," *European Affairs*, Vol. 8, No. 2-3, June 22, 2007.
[269] Matthew Bryza quoted in: "US official: Europe needs alternatives to overpriced Russian gas," *The Associated Press*, Feb. 22, 2008.

of strengthening Europe's position vis-à-vis Gazprom. As Deputy Assistant Secretary of State Matthew Bryza describes:

> "Our approach is to help Europe and help our European allies achieve their goals in diversification and to put them in the strongest possible negotiating position with a Gazprom partner who will be around for a long time. Strength in negotiations comes from diversification."[270]

The United States is therefore keen to boost Central Europe's access to non-Russian hydrocarbons. Norway is an obvious supplier to Poland and the Baltic region, but the United States has not been that active on this front, realizing that this is largely a bilateral issue for the Poles to work out. U.S. officials have thus limited themselves to saying that a pipeline from Norway to Poland makes good sense from a foreign policy standpoint.[271] "We're in constant touch with our Polish friends and we think that Polish strategic interests, their strategic view of this problem makes a good deal of sense," said Daniel Fried, Assistant Secretary of State for Europe and Eurasia.[272]

Washington has been more vocal with respect to Nabucco. Indeed, U.S. officials have made an honest effort to get the interested parties – from Central Europe to Central Asia – talking to each other about mutually-beneficial opportunities for governments and industry to work together, develop alternative energy resources and bring them to market in a way that cuts out Russia. Bryza has stated that U.S. efforts on Nabucco will be of "the same commitment, the same intensity" as were Washington's efforts in making the Baku-Tbilisi-Ceyhan (BTC) pipeline a reality.[273]

Enter the commercial opportunists, who have made things difficult for Bryza and his team by signing up to South Stream, Nabucco's competitor.[274] Hungary, Bulgaria and (possibly) Slovenia join opportunists Greece, Austria and Serbia in a kind of inadvertent pro-Gazprom caucus. Their commitment to Russia's pipeline, together with Nabucco's supply challenges, undermines the Brussels and Washington-backed pipeline.

U.S. officials have rightly expressed their frustration when some of its Central European allies – Bulgaria and Hungary in particular – have signed with South Stream. "We want to keep the countries that Nabucco will pass through – Austria, Hungary, Romania and Bulgaria – focused on achieving it," Bryza said last spring.[275]

As Hungary was signing a deal with Gazprom on South Stream in February 2008, U.S. officials presented a last-minute case for Nabucco over its Russian competitor. Bryza told the Hungarian media that "we [in the U.S.] hope Hungary will make clear Nabucco is its top priority because getting in place a diversified supply source will make coexistence

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[270] Matthew Bryza interview with Hungarian News Agency, Washington, DC, Feb. 26, 2008.
[271] Assistant Secretary Daniel Fried, Interview with Marek Walkulski, Polish Public Radio, May 25, 2007.
[272] Ibid.
[273] Quoted in: Michael Ritchie, "US Gets Behind European Gas Pipeline to Thwart Russia," *International Oil Daily*, Feb. 25, 2008.
[274] For an overview of the Nabucco-South Stream competition, see: Guy Chazan, "Energy Race: Russia Outflanks EU's Pipeline Plan," *The Wall Street Journal*, June 16, 2008.
[275] "US Urging Greater EU Unity on Finding Non-Russian Suppliers," *European Report*, April 4, 2008.

and cooperation with Gazprom all the more fruitful and successful."[276] He added that the order in which competing pipelines are built matters:

> "…it's very important to sequence pipeline projects in a way that strengthens ones own negotiating position with Gazprom, so Hungary will find itself in a much stronger position to develop future cooperation with Russia on natural gas if it first has in place or is making clear it will succeed in realizing the Nabucco pipeline… You need diversification first so that you have a better relationship with who is now your primary supplier."[277]

Fried also reacted negatively to Hungary's wavering, writing in a Hungarian newspaper, "Now is not the time for our attention to be diverted by South Stream, a pipeline that will be at least three times more expensive than Nabucco, and that is designed by a monopolist to stifle competition."[278]

On the oil side, Bulgaria's support for Bourgas-Alexandroupolis undermines pipelines that America supports. As previously discussed, Polish and Lithuanian firms have helped set up a consortium to open up the first Caspian-Baltic sea energy corridor without relying on Russian transit. Though the United States has been less active in recent years with respect to Odessa-Brody, U.S. officials continue to support the pipeline's extension in order to help the Baltic region diversify its oil imports, relieve pressure on the Bosporus, augment Ukraine's petroleum security and reinforce Ukraine's westward orientation.

Contracts for Caspian oil have yet to be signed to give Odessa-Brody necessary momentum. Azerbaijan has expressed support for shipping oil to Odessa,[279] but it remains to be seen whether the country has enough oil leftover after its existing commitments. Kazakh oil – transited via Russian territory through the Caspian Pipeline Consortium (CPC) system to the Black Sea – is another option. But the Kazakhs have been keeping their distance for fear of upsetting Russia. The Russians have up until now blocked the CPC's expansion, fearful that this extra oil will go to outlets not under the control of Russian companies.

This is where the Burgas-Alexandroupolis pipeline becomes important. Aside from bypassing the overcrowded Bosporus and offering Caspian oil exporters an outlet from the Black Sea, the pipeline also advances Russia's position in Southeastern Europe. As Vladimir Socor of the Jamestown Foundation describes:

> "The project's fourfold strategic goal is to increase Russian physical control over the transit of Kazakh oil, Russian state rents from that oil's transportation, Russian political leverage over U.S. and European oil majors that have no other outlet from Kazakhstan, and Russian economic and political clout within Bulgaria and Greece."[280]

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[276] Matt Bryza, Deputy Assistant Secretary of State for European and Eurasian Affairs, Interview with Hungarian News Agency, Washington, DC, Feb. 26, 2008.
[277] Ibid.
[278] Portions of article published in the Hungarian newspaper *Nepszabadsag* (Feb. 28, 2008) reproduced in: Andrew Neff, "U.S., Russia Spar over Gas Pipelines as Hungary Inks South Stream Deal," *Global Insight*, Feb. 29, 2008.
[279] Alexander Bor, "Azerbaijan prepared to supply crude to Odessa-Brody," *Platts Oilgram News*, Jan. 29, 2008.
[280] Vladimir Socor, "Bulgaria's Ambitions for Caspian Oil Transit," *Eurasia Daily Monitor*, Sept. 13, 2007.

If Russian and Kazakh producers commit the majority of their supplies from the Caspian Pipeline Consortium (CPC) pipeline to Bulgaria's port at Burgas, this weakens the hand of those pushing for making Poland's port at Gdańsk a Baltic hub for Caspian oil. In short, the United States has an interest in helping its Central European allies in the strategic players' camp realize their own projects.

On a more selfish note, it is not in America's interests for any foreign power (particularly a great power rival like Russia) to be in a position where it can successfully seduce or intimidate U.S. allies. If commercial opportunism runs rampant, American foreign policy priorities in Central Europe could suffer.

From a geopolitical perspective, Poland and Romania in particular represent pro-American bulwarks against Russian influence in Europe's periphery. It would not serve U.S. interests to have these states beguiled or bullied away from their Atlanticist tilt. If carried far enough, Russia's energy grip could be used to pressure Poland into ceasing its support for democratic reform in Ukraine and Belarus, or perhaps intimidate Romania into changing its policy regarding Moldova.

Another nightmare scenario for Washington would see a country like Hungary, Slovakia or Bulgaria – coerced via energy blackmail – block a U.S.-supported policy within NATO that Russia opposed (such as MAP for Ukraine or Georgia). Alternatively, one could envision a country foregoing the hosting of U.S. missile defense facilities in order to guarantee that they remain transit corridors for Russian gas. Even a partial and temporary reduction in supplies – as happened this month with Russian oil – could send a warning shot to the Czech parliament that their country would be wise to not ratify the U.S.-Czech treaty on missile defense. More extreme scenarios could involve Russia using its energy grip to pressure Central European states into recognizing a future Russian annexation of Georgia's breakaway province of Abkhazia.

What of the next time Washington wants to build a coalition of the willing in support of a military operation in the Balkans, the Middle East or beyond? Imagine if the lead up to the Iraq War took place with the stronger, more assertive Russia of today. If the Kremlin really wanted, it could have manipulated its energy monopoly with an eye towards disaggregating the so-called Vilnius-10.[281] The time may come when Central European states are called on to offer peacekeeping forces for areas that run up against Russian state interests, such as Moldova, Georgia or Armenia. Would the Kremlin get a veto on who could join a U.S.-led operation? To be sure, these are distant counter-factual scenarios, but they should drive home an important point: the West and Russia will not always see eye to eye, and as Russia regains its strength, it may increasingly be willing to say "nyet."

In the nearer-term, the energy security schism frustrates the ability of U.S. diplomats to back strategic players and encourage supply diversification in the Central European region. At present trajectory, U.S. efforts will run up against the commercial opportunists' willingness to bandwagon with Russia. Under the right circumstances, even those Central European countries most committed to energy supply diversification could throw in the

[281] This refers to the letter (dated February 5, 2003) signed by the Foreign Ministers of Albania, Bulgaria, Croatia, Estonia, Latvia, Lithuania, Macedonia, Romania, Slovakia and Slovenia expressing solidarity with the American position on Iraq's breach of UN Security Council Resolution 1441.

towel and surrender to Russian companies like Gazprom. This would seriously undermine U.S. interests.

For these reasons, the United States has an interest in buttressing the energy security of its allies. In doing so, American policymakers cannot ignore the obstacle of energy security schisms. Washington must be proactive, not passive, in tackling this problem.

What Should the Next U.S. Administration do?

Can or should the United States be doing more to heal the Central European energy security schism and support the strategic camp? Clearly, U.S. policy levers are limited in affecting what is nominally a European problem. The reality is that Brussels needs to be the first line of defense against Russia's energy grip by acting as a coalescing force so that individual member states are in a better position to negotiate with Russia. Unfortunately, Europe has not played this role. If Washington is concerned about a loss of influence in Central Europe to the benefit of Moscow, then it should find ways to step up its involvement and fight both the symptoms of Central Europe's energy security schism as well as the disease itself. This type of action would help diffuse Russian influence.

Thus far, the United States has been very clear about what it is not willing to do in support of Central Europe's energy security. To illustrate, in 2006 some in Polish circles hoped to recruit Washington to co-finance a gas pipeline through Ukraine (what would now be called a variant of White Stream) in exchange for Poland's agreement to host U.S. missile defense facilities.[282] But this idea never went anywhere. The United States argued that it cannot strong-arm private companies into funding diversification projects, and Poland would be naïve to expect the United States to foot the bill for pipelines that Poland supports. If, at the time of this writing, Washington is having a hard time coming up with more than $20 million to supplement U.S. military aid for Poland,[283] then imagine the difficulty of finding $400-500 million to extend Odessa-Brody, or perhaps billions of dollars to construct White Stream. From Washington's perspective, it is not worth it to be more concerned about Central Europe's energy security than the Central Europeans themselves, nor is it acceptable to bend the private sector to the whims of foreign policy elites.

Washington has also made clear that it does not support Iranian gas for Central Europe. One U.S. official bluntly characterized America's game plan for European energy security as follows: "Get more [energy] coming in from every possible direction – except Iran, of course."[284] Iran, though presently a net-importer of natural gas, holds the world's second-largest gas deposits and has expressed an interest in supplying the European market.[285] However, the dispute surrounding Iran's nuclear program takes Iran out of the game of energy geopolitics. The threat of unilateral sanctions – applied extra-territorially to non-U.S. firms – is used to dissuade European companies from investing in Iran's energy

[282] "U.S. help possible in funding Kazakhstan gas pipeline extension to Poland ruling party MP," *Poland Business Newswire*, September 4, 2006; *Interfax Central Europe*, Sept. 4, 2006.
[283] Desmond Butler, "Bush asks for defense money for Poland," *The Associated Press*, May 2, 2008.
[284] U.S. official quoted in: Steven Mufson, "Politics of the Pipelines; U.S. Seeks Ways to Route Natural Gas Around Russia," *Washington Post*, July 11, 2006.
[285] Noah Adams, "Iran's Rich Oil Fields Attract Foreign Investors," *National Public Radio (NPR)*, March 21, 2008.

sector.[286] U.S. diplomats have hinted that America will withdraw its support for Nabucco should Iranian gas become earmarked for the gas conduit in the present international environment.[287]

Stepping back for a moment, one should realize that America has a long list of foreign policy priorities, and managing Central European energy schisms does not rank near the top. Balancing Washington's willingness to be out in front is an understanding that America has bigger fish to fry. Importantly, there is a U.S. desire not to antagonize Moscow. The raw truth is that Washington does not want to further strain U.S. relations with Russia over an issue of perceived secondary, not primary, interest to U.S. national security policy; especially at a time when the State Department is recruiting Russian assistance on other global hotspots like Iran or Afghanistan. Yet the United States should avoid compromising on issues like pipeline diplomacy, for such a move could set a bad precedent and embolden the Kremlin to seek greater U.S. concessions in the future.

Some in the U.S. government might be tempted to let Europe sort out its own mess. Looking to 2009, the next U.S. President could be attracted to the idea of just cutting America's losses on European energy security, and focusing on other, seemingly more pressing issues in the Middle East. It could be argued that doing so would ease relations with Russia and spare Washington any embarrassment should projects like Nabucco fall through. In practice, however, washing one's hands of Central Europe's energy security would likely be seen as a slap in the face by many in the region who would like even greater U.S. support than currently exists. At a time when Washington and Brussels (whether consciously or not) are competing for the affections of the EU's recent entrants, this would also not help endear Central European capitals to America.

Moving forward, the United States needs to manage five sets of relationships to maximize the contribution of a renewed push on Central Europe's energy security: (1) U.S. relations with the states of Central Asia and the Caucuses; (2) U.S. policy as regards Russia and Russian energy firms; (3) U.S. relations with commercial opportunists; (4) U.S. relations with Germany; and (5) U.S./EU relations with the Islamic Republic of Iran.

1. The United States must demonstrate a more senior-level political commitment to the Nabucco pipeline. The State Department's work at lower echelons has been generally well-executed, and the March 31, 2008 appointment of C. Boyden Gray (who serves as U.S. Envoy to the European Union) as America's Special Envoy for Eurasian Energy is encouraging. But the next U.S. President and Secretary of State must make a personal effort to reach alignment among the governments of Azerbaijan, Turkmenistan, Turkey and other relevant states. Showing a greater commitment to helping Europe reach non-Russian supplies should hopefully send positive ripples into Central Europe. Some in the Black Sea-Caspian corridor question how serious the United States is about Nabucco, which sends confusing signals to countries like Hungary or Bulgaria. Getting firmly behind the Nabucco project at a more senior level could help reduce these latter states' susceptibility to South Stream's temptations.

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[286] See for example: Frank Nieto, "Major LNG Companies Shy Away from Iran," *Gas Processors Report*, May 7, 2008.
[287] "US Urging Greater EU Unity on Finding Non-Russian Suppliers," *European Report*, April 4, 2008.

2. U.S. officials should come out in formal opposition to both Nord Stream and South Stream. The first is a politicized route that undermines European solidarity and could put U.S. allies like Lithuania under the knife; the second derails competition and monopolizes the flow of gas to Europe's Southern tier. Thus far, U.S. diplomats have shied away from making such a concrete statement. Articulating America's opposition to both projects will provide much-needed clarity for commercial opportunists in Central Europe looking to see what Uncle Sam will let them get away with.

3. The United States should make clear to opportunists that actions that undermine Western-backed diversification projects are severely unhelpful. U.S. diplomats have been making an earnest effort, but the United States should be more willing to clearly state when nations like Bulgaria or Hungary undercut projects that America supports. As of yet, no official in the U.S. administration has publicly stated that "Washington strongly disapproves of Country X's policy with respect to South Stream." This will no doubt have to be done carefully; first in private, but in public if necessary. The last thing Washington wants is to further alienate itself from its allies. Yet if the U.S. always concentrates on garnering tactical victories in dealing with Central European capitals, it will loose the energy war, so to speak, with Russia.

4. Washington should consider ways to coax Germany away from its special relationship with Russia in the energy sphere, and towards a more multilateral approach that takes the new member states' interests into consideration.[288] Doing so could remove a major impediment to a common EU energy policy and rehabilitate one of Europe's worst energy role models for Central European states. As a first step, the United States could express its disappointment with Germany's participation in Nord Stream. The pipeline is viewed in Poland and the Baltic States as a direct threat to these states' energy security. U.S. officials will need to take up such concerns with Germany, and urge Berlin to consider the overland Amber pipeline as an alternative.

Second, U.S. diplomats should talk to their German counterparts about enhancing the European Union's role when it comes to energy security. Washington has favored European integration before, and it would serve America's interests to have Europe speak (to Russia, in this case) with a common voice. As a number of experts have already noted, the EU could make use of its anti-trust provisions to target Gazprom's monopoly – just as the Europeans have done with respect to Microsoft.[289] EU legislation specifically prohibits abuse of a dominant market position or linking contracts to obligations with no relevance for the contracts themselves (e.g. linking gas supply terms to infrastructure acquisitions).[290] The United States should urge Berlin and other major European capitals to recognize both the reality of Gazprom's monopolistic practices and the hypocrisy of applying EU rules to an American software firm but not a Russian energy behemoth.

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[288] Kirsten Westphal, "Germany and the EU-Russia Energy Dialogue," in Pami Aalto (ed.), *The EU-Russian Energy Dialogue: Europe's Future Energy Security*, Burlington, VT: Ashgate, 2008, p.112.
[289] See for instance: Zeyno Baran, "EU Energy Security: Time to end Russian Leverage," *The Washington Quarterly*, Autumn 2007, p.141.
[290] Treaty establishing the European Community (Nice consolidated version), Title VI, Common Rules on Competition, Taxation and Approximation of Laws, Chapter 1, Rules on Competition, Section 1, Rules Applying to Undertakings, Article 82.

While the German energy entente with Moscow is partially mercantilist, it is also done out of trepidation vis-à-vis Russia. America should offer its political support to help European heavyweights like Germany stand and face Russia with self-confidence. To be blunt, the United States should encourage Europe to bear its teeth in relations with Gazprom and Russian energy firms. One idea to bring up with Berlin would be for the EU to explore ways to threaten to regulate away Gazprom's profits unless the company agrees to abide by ECT principles and accepts that it must compete with other gas suppliers for buyers' affection.[291] In theory, the EU could insist that, unless Gazprom permits freer competition, it would see its profits capped at a standard rate of return. Germany needs to be brought into a coherent and productive transatlantic game plan on Central Europe's energy security.

Some might find it awkward to bring up energy security with Berlin when Washington is working closely with the Germans on issues in Iran and Afghanistan. Clearly, there is a danger of making too many demands. On the other hand, the United States should be careful not to let Central European energy security (and by extension, America's long-term influence) fall hostage to a U.S.-German rapport, anymore than it should the U.S.-Russian relationship.

5. The United States should sponsor a high-level inter-governmental energy security summit in Central Europe in order to take stock of where things stand and elaborate a way forward. Often, Central Europe's internal differences contribute to regional unity's failings and greater U.S. leadership is required. As the ultimate underwriter of the region's security, the United States can potentially play the role of an honest broker to bring everyone together and encourage a coalescence of viewpoints on an energy security strategy. In recognition of Poland's leadership role on these issues, and to indicate which side of the schism the United States supports, the summit could be held in Warsaw. To show America's commitment to its allies, the U.S. Secretary of State could chair the first summit.

In terms of substance, the summit should focus on modalities for giving new impetus to Central European regional unity on energy issues. Technical items can be prioritized on the agenda. These should include: (1) the Nabucco pipeline and prospects for Caspian and Middle Eastern sources of energy; (2) NETS; (3) proposals for making LNG work for Central Europe; and (4) nuclear power options, which could involve opportunities for U.S. firms.

Another goal to work toward could be the creation of a new, multilateral energy security organization; in essence, a Central European gas consumers' and transit states' forum. This could provide opportunities for Central Europeans – strategic players and commercial opportunists alike – to talk out their issues under a U.S.-sponsored tent. If the new organization develops successfully, and should EU attempts to form a common external energy policy fall through, it could serve as a platform for negotiating as a bloc with Russia on energy deals. Washington should offer U.S. diplomatic support as a backstop for any new organization, which could be headquartered in Bucharest in order to cement Romania's pro-Western orientation and build up the country's role as the go-to-

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[291] For example, ECT rules could force Gazprom to allow Western companies to use its pipelines for transiting supplies through Russia. See: Stephen Castle, "EU and Russia agree to new series of wide-ranging talks," *International Herald Tribune*, May 21, 2008.

guy for energy security in the Black Sea energy corridor.

6. Washington should be prepared to drop its opposition to greater EU-Iranian energy trade as part of any comprehensive understanding over Iran's nuclear program. To be sure, the geopolitics of natural gas should not be allowed to dictate Western efforts to keep atomic weapons out of the hands of the Mullahs. But preventing Iran from acquiring nuclear arms will undoubtedly require a careful coordination of sticks and carrots – potentially including energy carrots. Assuming the Iranians cooperate, EU gas markets can be offered as a reward for good behavior.

By leaving Europe's door open to Iranian gas should the Mullahs change their intransigent position, the West could help guarantee the commercial viability of diversification projects like Nabucco, and if and when the right conditions arise, offer Iran a lucrative carrot. Furthermore, Iran could become a transit state for Turkmen gas en route to Europe (obviating the hassle of building a pipeline across the Caspian Sea to Azerbaijan). This would yield positive externalities for Central Europe. Without a doubt, managing the entry of Iranian gas to European markets successfully could put a dent in Russia's energy monopoly. Different analysts arrive at different estimates, but some say that if sanctions on Iran were lifted and Western investment poured in, then Iran's gas export capacity could eventually reach 40-50 bcm per year. Such volumes could easily fill a future Nabucco and offer Gazprom meaningful competition in Europe.

Using Iran to blunt Gazprom's energy grip in this way would not entirely be without precedent. It already appears that the United States may have acquiesced to Georgia's recent substitution of Russian for Iranian gas.[292] The same logic could be extended to Central European states, should progress be achieved on the nuclear issue. As explained in a recent article, "if Gazprom is allowed to pursue a policy of 'divide-and-conquer' with individual EU customers, should not the Central Europeans be able to balance two producers (Iran and Russia) off one another?"[293]

Besides, if sustained high energy prices make it likely that Iran will become a net gas exporter in the long-term with or without U.S. sanctions, the United States might prefer that this gas go to its allies rather than rival powers like China. From Iran's perspective, of course, it is preferable to deal with the Europeans since it is Western oil and gas majors that have access to the latest technology. To entice the Iranians out of the hole they have dug for themselves, the United States should offer to lift sanctions (or the threat of sanctions) on Western gas deals with Iran if Tehran's leaders comply with the international community's demands.

These six steps, while no complete solution to the problem of Russian energy supply dominance, could go a long way towards blunting the expansion of Russian influence into Central Europe. Without a doubt, if the goal were to upset Russia's position as the top energy supplier to the region, then it would already be "game over." For better or worse,

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[292] "U.S. not against Georgia buying gas from Iran," *Central Asia & Caucasus Business Weekly*, Nov. 21, 2006.
[293] Ryan R. Miller, "Energy Carrots for Iran: Killing Two Birds with One Stone," AtlanticCommunity.org, April 15, 2008. Available at
<http://www.atlanticcommunity.org/index/articles/view/Energy_Carrots_for_Iran%3A_Killing_Two_Birds_with_One_Stone>.

Russia's Gazprom is here to stay. Yet there is everything to play for in terms of mitigating the political consequences of a monopoly supplier. As discussed, this will involve helping Central Europe in opening the door to alternative supplies, and encouraging a common EU policy as well as other European supply-solidarity measures.

And importantly, one does not have to view Russia as an existential threat – to Central Europe or otherwise – in order to justify the recommendations laid out here. One merely has to recognize that the United States and European nations are rivals with Moscow on a number of fronts. This does not mean that the West cannot partner with the Russians on global strategic issues, but it does mean that competition between the poles in the system (in this case the United States and the EU on one hand, and Russia on the other) is not going away anytime soon. Everyone should be thankful that the United States is now competing with Russia over economic and diplomatic chips, rather than under the threat of nuclear holocaust.

Regardless, the nature of international politics means that states will still jockey with one another for power and influence. If the United States wants to remain a power in Europe with a voice on important political and security questions, then it must have strong allies in Europe's eastern periphery. To this end, Washington must not give the Kremlin a pass on its game for energy dominance in Central Europe.