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Review

Invisible but not indivisible: Russia, the European Union, and the importance of "Hidden Governance"

Morena Skalamera

Geopolitics of Energy Project, Belfer Center for Science and International Affairs, Harvard Kennedy School, 1 Brattle Street, Office 518-B, United States

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ABSTRACT

Several scholars studying energy relations between Europe and Russia have grappled with the question of why such fragmented governance architecture has emerged between these two actors. While this question seems obsolete in the context of the current EU–Russian political impasse, it is, at the very least, odd that despite the standoff, plans for the South Stream pipeline have until recently proceeded almost apace.[1] How has this been possible? It is now widely, albeit reluctantly, accepted that Europe depends on Russia's gas and that Russia, in its turn, cannot do without the lucrative EU market. While this reality is basically indisputable, at the *macro level* this energy trade relationship has been marked with controversies since the breakup of the Soviet Union.

Despite the frostiness at what I will call the *macro-level*, in the past decade, individual EU states and the Kremlin have signed a handful of IGAs for joint pipeline development. Even more importantly, EU companies have concluded a number of important deals with Gazprom: pipelines have been built together, asset swaps concluded, and joint ventures implemented. All this has occurred against the background of increasingly tense relations at the macro level. Therefore, the biggest dilemma when looking into the black box of the EU-Russia gas relationship is how we might make sense of such a vast, multi-faceted, and yet deeply fraught relationship, occurring at so many different levels with varying actors. This article considers a number of political explanations for gas policy and shows that it is usually the economic interests of big energy firms that frequently take precedence, although these are often ignored and *hidden* as factors.

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E-mail addresses: morena_skalamera@hks.harvard.edu, m_skalamera@hotmail.com

[1] Most recently, Putin personally declared that Gazprom would abandon the South Stream pipeline; it will build a large pipeline to Turkey instead with a possible gas hub on the border with Greece. Insiders close to the Kremlin noted that even Gazprom's CEO Aleksei Miller had no prior knowledge of President Putin's sudden decision (Interview with Russian gas executive, May 2015, Moscow). The gas hub by the Greek border could be used to supply Southern Europe if there is demand. See for example, http://www.nytimes.com/2014/12/02/world/europe/russian-gas-pipeline-turkey-south-stream.html.

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1. Introduction

An extensive debate in the literature on EU-Russia energy relations revolves around the following question: Given the high degree of EU–Russia energy interdependence, why has such fragmented governance architecture emerge between the two actors? More specifically, the questions I pursue in this paper: Why is there no binding energy-governance structure regulating this relationship? Who are the main actors that have influenced such an outcome and where do their interests lie? What are the key events and developments that have influenced their priorities?

The paper endeavors to disentangle the complex, sophisticated and multi-level dynamics at what I call:

- The *macro level*: energy cooperation between the EU and Russia.
- The *meso level*: the internal arm-wrestling between the European governments and gas firms on one side, and of the European Commission (EC) on the other.
- The *hidden level*: the ties between the European energy firms and Gazprom, supported by the respective governments.

In examining these three crucial levels at which the EU-Russia natural gas trade takes place, it is necessary to:

1 Identify the main actors at each level,
2 Re-think the way the main actors form their preferences when pursuing their interests and
3 Test how, if at all, this impacts the legal formalization (or lack of thereof) of the EU-Russia gas trade.

In order to make my conceptual point, I go back to the bedrock of the assumptions undergirding the other explanations for the state of EU-Russia gas trade in order to see how my concept contrasts with their hypotheses. The first question is to identify where the interests of the main actors lie. This article shows that, when it comes to energy within the EU, the competing interests of member states still outweigh shared interests; major national interests, therefore, are not represented in the common EU energy institutions. Nor, clearly, do they represent the current interests of crucial Russian actors. However, the crucial finding is a positive causal relationship between the centrality of the corporate actors in the EU-Russia energy relationship, and these actors' tendency to dismiss legally binding energy governance structures.

The geopolitics of European energy has fundamentally commercial origins. Hence, instead of looking at the "clash of identities" at the macro-level, one should rather look to what I call the *hidden level;* the level where corporate interests operate, and where the actual outcomes of Eurasian gas trade and geopolitics are determined. It is here, rather than at the EU–Russia *macro level,* that both profit and identities matter. This is an area that Culpepper[2] would call 'quiet politics'–a set of technical arrangements, which are too complex for average citizens to understand and thus not an easy topic to engage the public; issues revolving around energy pricing, infrastructure, trade clauses and the like, that require a high level of technical knowledge to be fully grasped and therefore are often easily susceptible to firms' lobbying. This is the reign of energy firms where not only profit considerations, but also conventions, identities, and deep-seated beliefs do matter. As noted by Abdelal [4], European energy firms respond to profit-related considerations and have multiple institutional structures in place to help them channel their will. These companies retain a huge influence in the decision-making process involving EU–Russian gas cooperation and in many cases are the decision-makers actively shaping the process.

My article relies on more than twenty in-depth semi-structured qualitative research interviews, held in Brussels and Moscow, in 2012, 2014, and 2015. Interviews featured senior level energy experts, gas executives, academics, EU and Russian officials involved in EU–Russian institutional cooperation, as well as diplomats from Russia and the EU. I used "snowball" sampling – personal references and introductions from respondents we met – to identify other potential respondents. Public figures – including appointed and elected officials and well-known political observers – are identified by name, except in cases where they asked to remain anonymous. All other respondents, including energy industry insiders, remain anonymous and are identified only by the nature of their expertise.

2. Explaining hidden energy governance

In the gas governance, the hidden level involves issues that apparently have low salience and that are not easily grasped by voters. For example, voters certainly care about their monthly energy bills, but the complexity of paradigm shifts in energy governance occurring in Europe (in respect to long term contracts vs. short term gas trading, or oil price indexation vs. hub-based pricing of natural gas) dissuades both the media and politicians from investing their own limited capital in convincing the layman to explore these issues in detail.

The context in which these gas contracts operate is extremely complex, which means that both journalists and political entrepreneurs have difficulty convincing the general public to become knowledgeable about their key elements. The governance of natural gas, just as corporate control (which has been extensively examined by Culpepper),[3] is an ideal combination of circumstances for energy managerial groups, to wield disproportionate political influence, as they both understand and care about the issues of natural gas trading. Moreover, when voters are faced with complex matters, they frequently use short cuts or informational cues to form an opinion. In the case of gas contracts, voters often get the information directly from the energy companies' managers, whose hierarchy of objectives may be different than those of energy consumers. For instance, while the consumers typically strive for liberal, competitive energy markets, gas companies may put a stronger emphasis on achieving energy security with "traditional" tools such as long term contracts, or take or pay clauses, which for gas executives are oftentimes still prioritized over achieving liberalized and competitive gas markets. Despite the recent regulatory changes in the EU gas market, geared toward more competition and liberalization, the industry is still reluctant to fully embrace

[2] Culpepper ([19], p. 8).

[3] Culpepper ([19], p. 9–11).

those changes. Especially in nations where energy companies are still mainly state-owned, the links between the will of the corporate sector and what political entrepreneurs see as necessary are strong and direct. Where the energy industry is privately owned, the government is freer from corporate intervention, but corporate actors exert control and influence through lobbying, working groups, and press framing. For several decades,[4] many in Europe (especially the regulators) wished essentially for natural gas markets that would resemble oil markets: liquid, interconnected, and dominated by spot pricing. But many European executives, together with Gazprom, wondered if Europeans ought to be more careful what they wished for. For example, in the current low oil price environment, spot prices are gradually becoming more expensive than oil-derived ones. In fact, in a world of lower oil-indexed prices, Gazprom, who has the dominant market share in Europe, may swing supply to manage the spot market at a level acceptable to Russia.[5]

The tension between the political aspirations of governments and the commercial objectives of the industry has been much more nuanced than what is usually portrayed. There are inevitably some points of disagreement between governments and energy firms; however, businesses and governments in most cases work together to address long-term challenges, policies, and investments. Most interestingly, the actions that governments take are often informed and guided by corporate preferences. Corporate actors bring managerial expertise and money in order to secure the preference for their own energy ties, which in turn have path-dependent characteristics [24].

There is already a well-established discussion on EU–Russian energy governance architecture came is so fragmented who yields most influence in the two blocs' gas trade. These two issues of fragmentation and power, in turn, are considered in terms of the relative power of the member states versus the energy companies and versus that of the EU Community institutions (above all the Commission). I will not review this long and lively debate, ranging from Youngs [92] to Westpha [87], Locatelli and Boussena [51] and Kuzemko [45]. My intention is rather to show that the loss of control by member-state governments, has not necessarily curtailed their capacity to act. Most importantly, I highlight the centrality of the corporate sector in the EU–Russia gas trade (already argued by Abdelal [4]. Provided that the key-actors in the EU-Russia energy relationship are the heads of the big gas firms with their respective governments, these players have no inherent interest in being locked in multilateral institutions. *At the hidden level*, they often mitigate the risk of investments through a business discourse built on trust, and therefore, at the macro-level, support shallow governance structures. As noted by Abdelal,[6] initially firms on both sides of the EU–Russia gas trade created flows of molecules and hard currency by writing contracts that made the price of gas exogenous to the behavior of either party; eventually they came to rely at least as much on trust engendered by years of inter-firm cooperation. These relationships allowed gas to flow, unhindered, throughout the Cold War as well as during the collapse of the Russian state in the 1990s and its later restoration. In fact, in Culpepper's words,[7] being able to set the debate at this *hidden* governmental level is no silver bullet to ensure managerial victory, but is, rather, another weapon in the energy companies' powerful arsenal.

Indeed, when it comes to energy, factions in Europe have changed their positions according to the issue at hand. This article demonstrates that both Gazprom and the European firms have skillfully exploited these divisions. For example, as regards oil indexation (and take-or-pay clauses) we see the EC and the European energy companies directly opposing Gazprom. But as regards access to the European downstream gas market, Gazprom and the EC are united against the European energy companies, which are resistant. To make things even more complicated, as regards third party access, Gazprom and the European energy companies have changed their position to challenge the EC. Hence, EU–Russian gas cooperation is much more complex and multilayered than it appears at the surface. That is why all the major explanations of the EU-Russia institutional impasse have proven unsatisfactory. For example, Aalto [1,2] remarkable analyses of the different dimensions of EU-Russia energy politics provide an excellent theoretical account of all the energy interrelationships already in place, the ways leading actors pursue their interests, and the resulting outcomes. Aalto's research however, does not help answer the fundamental question guiding this inquiry: why didn't the tight energy interdependence between the EU and Russia result in legally binding instruments ruling their energy relationship? Other insightful studies stress the need for global governance structures to cope with the rapidly changing and increasingly interdependent global energy markets [84,24,16] but they do not provide persuasive answers to why such structures have not already emerged.

On a more general level, classic realists emphasize the "security dilemma,"[8] liberal literature stresses the structural unsoundness of the EU and the defects of an undemocratic Russia,[9] and constructivist scholars point out the identity gap between the two partners. The closest position to my argument is the "moderate" realist school, which recognizes the importance of the private sector, and among these, the most sophisticated work is Abdelal's analysis of the private sector's influence on energy policy outcomes in the Eurasian gas trade. This article builds on Abdelal's persuasive intuition that it is actually gas firms, rather than governments', that produce political outcomes in the Eurasian gas trade. My work goes on to examine the causal links between the centrality of energy companies and the lack of binding governance structures regulating the EU–Russia energy relationship.

Other scholarly work along these lines includes Locatelli and Finon [49], and Locatelli and Boussena's [52] analysis of firms' behavior in the EU–Russia gas trade. Westphal's work [88] also identifies the interests of firms as significant drivers of change in energy governance. In fact, these scholars, among others, already clarified that gas firms drive political outcomes and that, in doing so, they are motivated by profits. The novelty of this study lies in linking the influence of the main actors (the big gas companies) to the lack of binding governance structures in a comprehensive way. In fact, no study to date analyses the lack of ad hoc legally binding structures regulating the EU-Russia energy interdependence from the analytical angle of an increased role of corporate actors' leverage and their reluctance to change the current struc-

[4] In Europe, after the adoption of the Single European Market (1985), the European Commission (EC) undertook a process of gradual restructuring associated with neoliberal ideas. In the early 1990s, the EC promoted a series of laws aimed at privatizing previously public sectors of the economy, such as the energy sector. In gas, the EC issued its first directive in 1998, in which core issues of harmonization (such as access to pipelines, market opening and regulation) were still left to the judgment of individual member states.

[5] See: http://www.nohotair.co.uk/index.php/shale-gas-2014/224-gas/3228-from-lower-oil-derived-spot-prices-in-europe-to-a-potential-price-war, accessed in March 2015.

[6] Abdelal ([3], p. 16)

[7] Culpepper [19].

[8] For an extensive analysis of the ënergy security dilemma,ṡee Monaghan [60] *Russia-EU Relations: an Emerging Energy Security Dilemma*, in T̈he Power of Oil and Gasëdition of the *Pro et Contra* journal (volume 10, No. 2–3, 2006), the Carnegie Moscow Center.

[9] Especially the semi-authoritarian developments of President Putin's second term in office and his distrust of multilateral organizations.

tural arrangements. The article unfolds its argument in two steps. First, it suggests that despite of the plethora of legally binding rules that govern the EU's relationship with Russia (such as contractual provisions, BITs, WTO rules, the EU internal market rules, and Russia's national legislation), EU–Russia attempts to transform mutually acceptable principles of energy trade into ad hoc legal mechanisms, such as the ECT and the PCA, have failed. The relationship soon thereafter entered a period of stagnation at the macro-level. Second, unlike other analyses, this article finds that the central influence of the industrial gas lobby on the decision-making processes is the direct cause of the lack of such distinctive types of binding governance structures. In turn, *hidden* company-to-company contractual provisions provide the architecture and axis points around which, amid parallel breakdown of consensus, the wider EU-Russia macro-level system turns. This article provides little empirical support for the liberal proposition that economic interdependence paves the way for the flourishing of international regimes, or in this case, binding energy governance structures.

Some of the great liberal analysts of world politics, such as Koehane and Nye [40], Keohane [38,39], Ikenberry [35,36], and Ruggie [75] put forth the proposition that ever increasing economic interdependence creates the need for appropriate institutions to facilitate trade by reducing uncertainty, lowering the transaction costs, and setting commonly accepted rules and standards. In the energy realm, too, reputable scholars such as Florini [23], Lesage et al [46] and [82], further the proposition that energy interdependence, ipso facto, fosters the desirability for a common umbrella of rules. This is how they lay out the problem: such an active energy cooperation necessitates an overarching structure regulating investment and providing legal security for pipeline transit, which would encompass all actors along the pipeline stream. Their additional contention is that in a world of growing economic interdependence the costs of brushing aside multilateral rules inevitably rises. This article tests these liberal propositions and finds that high economic interdependence does not necessarily spur the creation of new international regimes. This is not so because the EU's espousal of democratic norms is blocked by Russia's manifest *realpolitik* objectives and old-fashioned modes of foreign policy at the macro-level, as the liberals would have it. Evidence has already accrued that indicates that on the existence of institutions the EU side favors "demand—side explanations." Insitutions are created by those who stand to benefit from them [40,37] . In that sense, trade and capital flows increase the demand for "good" institutions [18]. There is another approach to explain where institutions come from, which emphasizes the "supply side": institutions are the imposition of foreign powers (e.g., the EU) and the adoption of imported legal norms and rules. To a degree, Russia favors this explanation. Given this state of affairs, liberal political scientist continue to exhibit a normative longing for signs in Russia of a metamorphosis towards the EU's *modus operandi*. In sum, Moscow is allegedly pressing for non-binding political declarations of a "strategic partnership," essentially confirming Russia's status as a Great Power on an equal plane with the EU, while limiting pressure over adherence to common rules. The EU preference is for a series of more substantive and complex agreements that could be concluded from time to time for specific tasks (such as energy investment). Yet the problem is that many in Russia lean towards a "low-cost" variant that would not require any binding agreements, but that would provide more visible statements on energy security. In sum, while the EU has became the most advanced world's bloc in pooling sovereignty, Russia has been historically determined to guard both the principle of self-determination and that of sovereignty.

But here is the provocation—is a liberal (rule of law) polity featuring a democratic franchise a sine qua non for transnational cooperation? We know that despite its political system, Russia aims to join the international institutions that could further its interest, such as the WTO. Russia does not inherently oppose multilateral organizations due to its autocratic regime, but it selects those that are perceived as advancing Russia's national interest and, most importantly, those that are pushed by the most important actors in the system. In energy that actor is Gazprom.

In fact, I take a rational-choice approach to study the behavior of the crucial actors on both sides of the energy interdependence spectrum to argue that, at a hidden level, Gazprom's prosperity may be larger without clearly defined rules. Therefore, the latter wants to protect its interests by preventing the emergence of binding institutions. The same holds for EU companies. In sum, this article proposes to look at the issue through a different pair of lenses—given a decades-long, dense relationship, at the hidden level, the corporate sector has other ways to solve possible coordination problems.

Despite estimable contributions, the liberal approach mainly focuses on why it has proven so difficult to forge binding energy institutions between the EU and Russia. Unfairly, perhaps, the question of whether such institutions are desirable and necessary ventures far from the liberal approach. In fact, my approach further differs from the liberal literature, in that it questions the desirability of such institutional arrangements right from the outset, rather than focusing overwhelmingly on the need to harmonize the two sides' institutional asymmetry [73]. My findings suggest a tension between the pull towards "deepening" institutionalization at the macro-level, and the interests of key players on both sides of the energy relationship. Through extensive empirical evidence, the article demonstrates that enhancing the multilateral aspect of the relationship is not within the priorities of the key decision-makers.

For instance, the geopolitical tumult between Russia and Europe over Ukraine has had a negligible effect on the EU's corporate actors' business strategies. Not only they have downgraded Donald Tusk's proposal to create a single European buyer for Russian gas, but in the wake of the crisis they have also fostered an expansion of Nord Stream, a Russian–German link through the Baltic Sea. The 'gas wars' between Ukraine and Russia provide additional illustrative examples. As noted by Yafimava [90], while in the aftermath of the 2006, the political mood in Europe regarding the reliability of Russian supplies was that of extreme nervousness on the part of the old member states, and an outright insecurity on the part of its new member states, the prevalent attitude among major players of the European gas industry, by contrast, was calm and even optimistic. This is suggested by the fact that nearly all European gas buyers, including E.ON Ruhrgas and Wingas (Germany), EDF (France), OMV (Austria), and ENI (Italy), renewed their long-term contracts with Gazprom between 2004 and 2006 for the subsequent 30 years.

By relaxing the assumption that interdependence is conducive to legally binding international regimes, this article argues that energy dialogue between the EU and Russia is to be achieved rather through the coexistence of differentiated models, where policy coordination becomes a central and desirable tool. Coordination is desirable only as long as it respects the consolidation of different national regulations, standards, and practices. In fact, as a secondary point, the article holds that defining the rules of interdependence is difficult between actors that have so different immediate interests and different domestic institutional arrangements (see Table 1). This gives us the reason for the lack of binding governance structures between the EU and Russia: The de facto existence of different jurisdictions is a response to the historical and geographical developments in these regions. Hence regulations and norms should strive to reflect national conditions and preferences. Eliminating the transaction costs of cooperation through coordination is desirable, but if national interests, tastes, or conditions lead to different laws, the playing field of international energy trade will not, and should not, be level.

Table 1
Institutional asymmetry between the EU and Russia.

Institutional domain	The EU ideal	Russia's pattern
Property rights	Private, enforces by the rule of law	Private but govt authority occasionally overrides the law
Corporate governance	Shareholder ("outsider") control, protection of shareholder rights	Insider control
Business-government relations	Arms' length, rules based	Close interactions
Industrial organization	Decentralized, competitive markets, with tough anti-trust enforcement	Horizontal and vertical integration in production; government-mandated cartels
Financial system	Deregulated, securities based, with free entry. Prudential supervision through regulatory oversight	Bank based, restricted entry, heavily controlled by the government, directed lending, weak formal regulation
International capital flows	"Prudently" free	Restricted (until the 1990s)
Public ownership	None in productive sectors	Plenty in upstream industries

Source: compiled by the Author.

In sum, in contrast to Liberal Institutionalism's optimism that economic interdependence fosters the desirability for international regimes, this article shows that there is no reason to believe that energy interdependence is a sufficient condition either for the emergence of shared governance structures or for adherence to their rules.

3. How to make sense of the macro level?

Recent scholarship has yielded a number of explanations for the inability or unwillingness of the EU and Russia to turn their energy interdependence into legally binding governance structures at the macro level.

Explanations have differed according to the lenses through which one has examined the question; the differences being linked to the ways the three major traditions in International Relations – neo-realism, liberalism and constructivism – tackle broader issues of world politics. In Table 2 I will summarize these approaches.

I argue that at the *macro level*, the constructivist approach offers the most adequate lens to explain the main impediments to fruitful cooperation. However, at the *meso* and at the *hidden politics levels*—(where the national governments offer support to their respective energy companies), this lens alone is not satisfactory. For Locatelli and Boussena [52], the crucial question is whether the international standards generated by the EU through the Energy Charter Treaty (ECT) are consistent with Russia's institutional environment. In fact, as noted by Kuchins and Zevelev [43], for Russia, the central debate today and going back at least two hundred years revolves around the West: to what extent Western liberalism is an appropriate model and how closely should Moscow ally with certain actors in the West to achieve its goals. However, in contrast to these scholars' view of institutional dichotomy between Europe and Russia, empirical findings detailed at length in this article suggest a more nuanced picture. The crude juxtaposition of the European system of governance based on a competitive economy framed by the rule of law as opposed to the Russian system of asset swapping is not the correct one, because there is an area of overlap, constituted by the shared interests of the corporate sector on both sides.

I will look at four issues to illustrate my point: the Southern Gas corridor, Russia's reluctance to adhere to the ECT and renew the PCA, the so-called Third Energy Package, and the quest for removing oil indexation and the relaxing of the take-or-pay clause in the contracts with Gazprom. But let us first review the still ongoing debate at what I call the *macro level*, which in this article is considered the *less* decisive one.

4. The neo-realist literature

From a standpoint of political realism, there are certain things that are built into the nature of world politics. States pursue their national interests. In doing so they count on a relative "balance of power" achieved with bilateral alliances and "power politics." The highest value is accorded to the preservation of sovereignty, territorial integrity, and independence, while the most important principle of international law is non-intervention. Security of energy supply and security of demand are included in the sphere of 'high politics', which pertains exclusively to states. In domains of crucial national interest such as energy policy, international institutions are regarded with suspicion. Therefore, arch-realist literature has been quick in dismissing any chances of an EU–Russia energy governance structure by arguing that states, which are considered the main units of world politics, seek to enhance their power at the expense of other states in a climate of low trust. Thus, any advancement of one side is seen as a loss for the other, creating a well-known security dilemma [60]. This means that any increase in Europe's security of supply is perceived to cause a diminution of Russian security of demand. In this state of affairs multilateral cooperation is seen as undesirable and impracticable. In sum, the tight energy interdependence between the EU and Russia is not sufficient produce legally binding governance structures and, in turn, deter the two blocs from securitization in energy relations.

Under conditions of high mutual dependency that are perceived as alarming, the EU's suddenly desperate drive to diversify forces Russia, in response, to diversify away from the EU, which now appears less dependable. The fear of both sides that the other might diversify its imports/exports leads to a downward spiral of mistrust and weakens the prospects for cooperative endeavors.

Given the irreconcilability of Russian and EU's interests and their mounting competition in the shared neighborhood, according to this narrative, only very sporadic, low profile cooperation is indeed attainable. Moreover, the risk of conflict is not avoided merely in virtue of economic interdependence. In sum, given the frantic efforts to diversify against one another, over time, interdependence between Russia and the EU will inevitably be reduced.

Yet I argue that this mutual diversification should not be considered inevitable. Gazprom has been complaining heavily about an EU that is requesting more gas supplies from Russia while at the same time claiming that it wants to diversify away from Russia. Gazprom's interest is to secure long-term agreements with its main European customers, guarantees for investments, and direct downstream access to the attractive European market. True, in face of a growing politicization of this relationship, Gazprom has responded in kind by announcing a two-fold strategy that involves: diversifying exports by increasing shares of liquefied natural gas (LNG), and diversifiying export markets, primarily to Asia. In fact, the EU's increased diversification of supply with the goal of "more independence from Russia" triggered decreased 'security of demand' for the latter. Since the first Ukrainian-Russian gas war a process of "securitization" of energy relations between Russia and the EU has started, which has continued despite the current "gas glut" in the EU, in line with the neo-realist view. In recent years Moscow did

Table 2
Existing explanations for the lack of EU-Russia energy governance structures.

Schools of thought	Main concerns	Reasons for the lack of energy governance structures
Realism	1.The "Security Dilemma"—a self-interested effort to maximize energy security amid anarchy in world politics	1. Energy cooperation is a zero-sum game where the interests of producers and consumers do not coincide and any gain of one results in a loss for the other (Monaghan [60]).
	2.The balancing of each other's sphere of influence in the shared neighborhood 3.The precedence of national interests and the gains made by domestic companies	2. General distrust in the utility of multilateral structures of governance—when it comes to issues of strategic importance the basic unit of world politics is the state (Lesage et al [46] p.183).
Liberalism	1. The reluctance of the main member states to transfer energy competencies to the EC	1. The EU does not speak with one voice in energy matters, which weakens its leverage vis-à-vis Russia—an anomaly of the EU's structure (Schmidt-Felzmann [76], Helm [30] and Helén [29])
	2. The bigger and smaller EU member states' asymmetries in interdependence with Russia 3. Russia's reluctance to institutionalize the relationship legally with a new PCA and the ECT	2. Russia is an assertive rising power unwilling to abide by the principles of International law (Baran [9], Rosner [74], Umbach [80])
Constructivism	1. Clash of Identities that impedes commonly held views on governance structures 2. Incompatible views on leading norms, such as reciprocity, sovereignty, and information sharing 3. Due to this clash of paradigms, interdependence leads to discord instead of cooperation	1. The identity dilemmas of the EU as such worsen the prospects of a shared identity between Russia and the EU (Belyi [13]) 2.Insufficient mobilization of the peripheries for a bottom-up, regional and cross-border approaches to cooperation (Romanova [72], Morozov [62])

Source: compiled by the Author.

use pipeline politics to expand its share of Europe's gas markets, to retain a dominant position in the CIS markets, and to secure a place among the great international powers. The EU, on the other hand, was widely predisposed towards the export of economic and regulatory norms, as tools in the pursuit of its own material interests [26]. At the heart of this is a 'security dilemma' between the EU and Russia, where 'the actions of one [the EU], in trying to increase its security, causes a reaction in the second [Russia], which in the end, decreases the security of the first.'

Yet, the scale of mutual diversification is not even close to what is feared by the "security dilemma" proponents. Russian gas still is and will remain in demand. There are simply no viable alternatives that can replace the EU's sizable gas imports from Russia. Coincidentally, the mixture of Vladimir Putin's personal political style, his conviction that natural resources are the means to restore Russia's economic (and political) strength,[10] and the general growth in the importance of executive power in Russia all fueled concerns about Russia's willingness to use "the gas weapon." However, unlike some other petro-states, Russia does not threaten the use of 'the energy weapon' against Europe, its main customer. On the contrary, it takes great pains to remind Europe that it has always been a reliable energy supplier both during the Cold War and today (see [12,28]. Russia is aware that the European market is far too important to the survival of the Russian state[11] and that if challenged, the EU could turn to other producers or alternative energy sources. The realists argue that precisely because there are many "Europes" whose level of dependency on Russia varies, decentralized, national decision-making is more suited to accommodate these national differences. Moreover, given that energy is a strategic good, states simply do not tolerate a compromise of their sovereignty in this field ([46] p. 183). In this view, states should have the freedom to maneuver instead of being locked into large, multi-faceted bureaucracies and stringent transnational agreements. Moreover, the shared EU–Russian Neighborhood remains a crucial terrain of geopolitical battle. Once again, the recent Ukraine crisis confirms the validity of the neo-realist approach.

The main criticism of the neo-realist position is its failure to recognize the predominance of the private sector in energy geopolitics on both sides. Realists place states and their pursuit of power at the center of empirical evaluation and, therefore, their analyses of EU–Russian energy cooperation fail to see the importance of non-state actors (such as Gazprom, the European "national champions" and the other NOCs and IOCs). Although companies do exert some influence by securing long-term preferential deals on broader geopolitical aspects of energy security, energy companies are commonly considered to follow, rather than to influence, the positions of their respective governments (see [79,92]. In stark contrast, this article argues that the current lax governance structure reflects the preferences of the key actors in EU-Russia energy cooperation, namely the big gas firms. In fact, this article sides with Abdelal in his view that "*A Realist account would identify neither the most important agents nor their essential logics. Instead of states 'pursuing security amidst anarchy, we find firms' pursuing profit in the face of uncertainty. The geopolitics of European energy has fundamentally commercial and ideational origins.*"[12]

5. The liberal literature

More moderate, but quite Eurocentric views have in the past pointed to Russia's autocratic regime and its resource nationalism as the main obstacle to more fruitful cooperation. This situation, so the argument goes, makes the Putin regime less conducive to liberal trade and interdependence. Works arguing that stronger central political guidance is required in Brussels in the face of forceful Russian rhetoric continue to be widely read (e.g. Umbach [80], Helén [29] and Schmidt-Felzmann [76]). The closure of so-called "Fortress Europe" has been one such response to the Kremlin's growing assertiveness.

On the other side, more "objective" observers within the liberal school stress that the EU has contributed to the strain, too. The EU,

[10] Energy was the topic of Putin's doctoral dissertation, which he defended in 1996 at the St. Petersburg Mining Institute, arguing for state control of energy companies and invoking limits to the rights of private owners.

[11] Simply put, the Russian budget, and by consequence the sheer survival of the Russian state depend heavily on the export of energy to the EU, much more than any of the EU-28 states depends on Russian gas. Noël [63], for example, has argued that Russia is in fact very much dependent on its gas exports to European countries, while the EU relies on Russia only for 6.5% of its total primary energy (not just gas) consumption.

[12] Abdelal ([4], p. 2).

so the argument goes, has been historically weak because of its notorious divisiveness, which is due to the bigger member states' inexplicable skepticism that a truly common European energy policy is in their best interest. This approach highlights the historical differences in national energy mixes, showing how tricky it can be to maintain a common stance in face of large differences between the constituent parties. However, the problem could be solved if member states accepted a common internal energy market and a coherent external voice that would eliminate the actual structural differences. The European Commission (EC) would take the lead in speaking under the slogan of "one-for all."

According to this view, the remedy for Europe's inconsistencies is to be found in delegating more powers to the supranational level. This would be done by enhancing the EC's strength and devising an instrument to "speak with one voice"[13] in energy matters, which would in turn increase the EU's leveraging power as a whole in relations with Russia. The particular energy situation of each member state would then cease to matter.[14] For instance, this is how Pierre Vimont, Secretary-General of the European External Action Service sees the problem, "*we are very far away from achieving a strong and coherent position on what a common vision on "External Energy Policy" should be. States want to retain their national sovereignty because they think that by working on their own they have better leverage and better deals. In the meantime, Russia plays putting one country against the other*."[15]

Upon analysis, this approach is found to be flawed, but most importantly, I think that even the resolution of Europe's internal divisions and a one-voice Europe would prove unsuccessful in speaking with Russia at the macro level, for reasons that the constructivist lens evinces. Europe's diversity is the result of its relationship with Russia, not the cause. Institutional diversity is so persistent because of the very fact that the energy mixes, and thus each member states' level of dependence on Russia varies greatly.

In Europe, historically, energy has been a sector of the highest national priority and different member states found different strategies to manage their energy mixes. If there is no single EU energy mix, the Commission's advocated "convergence" is difficult to assess: one might ask, convergence on what? No EU member state displays the same economic political, historical, and cultural background, and the geographic proximity or distance from Russia makes their policies diverge. The different political and societal incentives at home place the member states in vastly different positions. For example, a country such as the Netherlands might not focus on North Africa, but Italy, due to territorial proximity, is more prone to do so. If, due to these geographic circumstances or other incentives there is no convergence toward one homogeneous European energy mix, then there should be no unified European external energy policy dictated by Brussels. A European energy policy is rather to be achieved through the coexistence of differentiated models, where policy coordination becomes a central and desirable tool. Hence, I would argue for shallow coordination that corresponds better to the needs of a still pluralistic Europe. Shallow energy integration promotes accountability of governments to local concerns and is preferable, due to the sensitivity of the issues of energy supply. An interconnected internal market for natural gas[16] would per se "Europeanize" bilateral relations with Russia, as transmission operators, suppliers, and governments would have to take into account not only their own markets, but also that of the EU as a whole. Yet the lack of connecting infrastructure within Europe is still an impediment in the process of developing a unified gas market, much more than the individual firms' competition to seek favorable deals with Russia. In fact, this paper holds that a solution to EU energy security concerns lies in an overall EU-wide integrated gas market rather than in common EU external energy policy.

Many liberal observers have criticized the behavior of European gas companies for their resistance to the completion of the internal gas market [30], p. 38–39; [56]. In contrast, this article shows that corporate actors are simply moved by self-interested profit considerations. If retaining their special, long-standing relationships with Russia secures them lower prices, the companies will do so at the expense of solidarity among EU states. This economic realism might clash with the EU's multilateral approach, but instead of encouraging EU's leadership in external energy policy, it should spur more solidarity-based mechanisms at the macro level. Potential disruptions crises require the possibility of moving gas quickly and efficiently among European states, which in turn requires interconnector pipelines and the possibility to reverse gas flows in the West-East direction. In recent years, a benign action of the EU has revolved around increased infrastructure connectivity at the macro level, along with the implementation of regulations on energy efficiency and the use of renewable sources. As noted by Goldthau and Sitter,[17] the EU made significant strides in the use of regulatory instruments to achieve foreign policy objectives, which in line with Liberal arguments, confirms the strength of the EU policies at the macro level. Two prominent steps to deal with gas supply threats were establishing the European Network of Transmission System Operators for Gas (ENTSOG) and the Agency for the Cooperation of Energy Regulators (ACER). It remains to be seen whether ACER ought to be given a strengthened mandate to establish gas market regulations, including the power to overrule national regulators on issues connected with security of supply and the operation of cross-border transmission systems. A common regulatory framework could in fact become the EU's most potent negotiating tool, as it would allow coordination at the EU level and the creation of a more liquid gas market. In 2015 Brussels gave teeth to its rulings by launching the so-called CESEC group,[18] aimed at raising the connectivity of the Balkans through a mosaic of existing and developing interconnections. In the words of an European official, "the Ukraine crisis highlighted all our weaknesses and built the necessary momentum to make these changes happen. We now spent $ 5,1 bn on connecting Europe; this may have dragged on if it wasn't for the Ukraine crisis..."[19] With the expansion of the EU's LNG infrastructure more gas can be moved and swapped between member states. Nevertheless, Brussels' bark often has been greater than its bite in terms of capability and effectiveness in taming the corporate sector. As Klaus Welle, Secretary General of the European Parliament observes, "*Interconnecting Europe has caused very complex disputes. Now a special, multi-billion gas infrastructure fund has been launched.* " However, as Welle admits, "*we are still not very strong on making the corporate sector follow our legislation*."[20]

Most recently, despite the EU's efforts to keep transit through Ukraine a viable option, Gazprom and its European partners signed a shareholders' agreement on the Nord Stream-2 gas pipeline

[13] See for example, Špeaking with one voice—the key to securing our energy interests abroad,ËU Press Release, Brussels, 07 September 2011, Accessible at: http://europa.eu/rapid/press-release_IP-11-1005_en.htm?locale=en.

[14] Therefore, the EU states are encouraged to change their narrow definition of national interest, by endorsing the EC's benign influence.

[15] Interview with the author, Harvard University, October 11, 2011.

[16] Which is the self-proclaimed EC goal for the completion of an internal energy market. One in which, indeed, the EC's lead is beneficial and desirable, to be supported by internal gas interconnectors and joint crisis mechanisms, in a spirit of solidarity.

[17] Goldthau and Sitter Šoft power with a hard edge: EU policy tools and energy security.Řeview of International Political Economy, 2015, 1–25.

[18] http://europa.eu/rapid/press-release_STATEMENT-15-4281_en.htm.

[19] Official at the EU's External Action Service, Interview with the author, Brussels, Belgium, May 21, 2015.

[20] Interview with the Author, Harvard University, October 3, 2011.

project,[21] which once again, confirms the primacy of corporate actors at the hidden level.

In sum, a liquid gas market would ensure EU-wide solidarity by working out better emergency plans through the development of new interconnectors and reverse flows, and by developing crisis prevention mechanisms at the EU level, with the European Commission acting as the vector for coordination [30]. Such an integrated European gas market is at the very core of the EU energy policy triangle of achieving security of supply, competitiveness, and sustainability, given that it increases the competitiveness of the energy markets and at the same time it strengthens security of supply. However, despite what Liberals say, it is not attainable, desirable, or even democratically justifiable for the EU leadership to "speak with one voice" while a handful of external supplies, such as Russia, act as oligopolies. Therefore it should not even be attempted.

6. The constructivist literature

With a higher level of sophistication, Constructivist theory calls greater attention to the role of identity, norms, and culture in its explanation for the EU–Russian predicament. I accept the value of this theory at the *macro* level, and I will evince its main postulates.

Constructivists argue that there is a "clash of paradigms" in the EU–Russian relationship [27,50], a consequence of the different "framing" of the main norms accompanying energy trade. The insufficient clarification of common standards poses an immense challenge in negotiating binding multilateral and bilateral agreements, such as the Energy Charter Treaty (ECT), as well as in the continuation of the Partnership for Cooperation agreement (PCA).

In the 1990s Russia was "weak" and forced to be a "norm-taker" [48]. The Russian energy sector was expected to "learn" from European expertise. The learning revolved around economic liberalism that included support for relatively unhampered energy markets and the "spill-over" of European regulatory practices into the Russian energy sector.[22] The rapid decline of the Russian economy and weak political development in the 1990s were all the more reason why the EU approached Russia on the basis of an unequal power relationship. For example, the ECT was crafted in the early 1990s on the initiative of the EU, with the purpose of fostering the "governance of the pipelines" and extending European energy policy to the rest of Eurasia. The Charter was signed in 1994 and it incorporated 51 member states, replacing no less than 1275 bilateral investment treaties (BITs) with a single multilateral regulatory framework, with especially notable provisions in the area of investment protection.[23] Its importance lay in that it was the only multilateral framework for exchanges between producer, transit, and consumer countries [86,90]. Despite that, the ECT did not sufficiently reflect the interests and concerns of producers. This was in fact the most proximate cause of Russia's ultimate withdrawal: the country simply did not see anything to gain from accepting ECT-like discipline.[24] The fact that the final decision to opt out came after the possible verdict in the Yukos expropriation case stimulated a lively scholarly debate on how Russia's withdrawal could be of political significance [81]. However, this quite overlooks the fact that none of big producing countries (e.g., the United States) or suppliers of Europe (including Norway and Algeria) is a member of the ECT.

The fact that it was an EU initiative also meant that the EU had a "first mover advantage" in defining its structure.[25] Most importantly, the ECT has been integrated into the EU's *acquis communautaire*.[26] Despite its weakness, Russia firmly refused to adopt several of the EU-sponsored rules, such as the ECT. Many Western scholars pointed out that the ECT has been written with a purely EU conception of how relations with Russia should be organized [86,17]. In that context, the then President Medvedev presented an alternative Treaty, the "Conceptual Approach to the New Legal Framework for Energy Cooperation",[27] which from one European diplomats' perspective had "strong borrowings from the ECT."[28] Medvedev's concept complemented the ECT, including improvements to the country's unappealing business environment, a stronger legal system, and more individual freedoms [17]. Despite Westphal's [86] persuasive point at the time that the renewal of a constructive dialogue with Russia should begin from taking Medvedev's proposal more seriously, the latter has been greeted with little enthusiasm in Brussels. The EU has shown no interest in discussing the new 'conceptual approach' to energy cooperation, and it has ignored ex-President Dmitri Medvedev's proposals for a general EU–Russia agreement on energy infrastructure.[29] A strategy group has been put in place in 2010 for the modernization of the ECT, but for the EU the review process was simply a non-starter. In the words of an EU diplomat: "*A way to accommodate legitimate Russian interests has to be found. Russia is now pushing for a completely new Treaty. Yet replacing the ECT with a new legal framework to accommodate Russia is very difficult. Why should the EU consider dramatically changing a treaty codifying elementary rules to safeguard energy investments and trade, which has been already ratified by 46 countries? The EU would incur in a huge reputational cost should it step back now.*"[30] In the aftermath of Russia's refusal to adopt free-market legislation in the energy sector, despite the efforts to keep the process formally ongoing, a large gap was created in the EU–Russian dialogue. The EU struggled to find a new position on Russia by incorporating some of the principles of the ECT into the new PCA [63,92] but the Russians were firm in their refusal. Since then, all alternative approaches involving a diplomatic solution to modernize the ECT have largely failed.

One could argue that if Russia accepted the ECT and its controversial Transit Protocol, the whole debate about the Southern Corridor would have become superfluous and the EU–Russia energy predicament would have been solved with less cash and political battling. Yet instead of multilateral cooperation, Russia's nascent business model revolved around bilateral relations, in which it could prevail over weaker partners and reward friends. The Kremlin itself has not denied that energy is an important foreign policy tool, although it responded vehemently to accusations that it uses its energy abundance as a political weapon.[31]

The increase of oil prices starting after 1999 facilitated the Russian economic recovery. In 2000 Putin took office and resuscitated

[21] Euractiv, Germany helps Russia bypass Ukraine via "Nord Stream-2", September 4, 2015.

[22] For literature on šspilloveršee for example, Haas, P.M *Introduction: Epistemic Communities and International Policy Coordination*, International Organization, vol. 46, no. 1, Knowledge, Power, and International Policy Coordination. (Winter, 1992), pp. 1–35.

[23] See: The Energy Charter Treaty Secretariat website, www.encharter.org.

[24] The United States, for example, did not sign the ECT because it does not include the necessary clauses for a pre-investment climate and treats purely post-investment situations.

[25] In fact, the ECT had been always regarded as Ëuropean,ẅhich has been at times its strength, at times its major weakness. After all, its headquarters are located in Brussels, the EU funds more than 65% of the budget.

[26] Which are the accumulated legal acts, and court decisions that constitute the body of European Union law.

[27] The five-page Čonceptual Approach to the New Legal Framework for Energy Cooperationẅas posted on President Medvedev's official website.

[28] European Diplomat at EEAS, Interview with the Author, May 2012, Brussels

[29] See: *EU readies 'pragmatic' answer to Putin's energy agenda*, December 18, 2012, Euractiv.

[30] European Diplomat at EEAS, Interview with the Author, May 2012, Brussels.

[31] Mitrova, *The Geopolitics of Russian Natural Gas*, White Paper, Harvard University's Belfer Center and Rice University's Baker Institute Center for Energy Studies, February 2014, p.7 [59].

a strong state, thus ending the political chaos and economic turmoil of the 1990s. Acutely aware of the importance of the energy sector for Russia's state budget, but also keen to restore Russia's "rightful place" in the world,[32] President Putin began to restructure the energy industries away from full privatization, setting limits to foreign private capital.[33] Henceforth, the direct influence, or the "spillovers", of the EU's ideas into Russia began to be seen as improper interference. The 2000 Foreign Policy Concept, drafted under Putin's supervision, already stated that '*Russia must be prepared to utilize all its available economic levers and resources to uphold its national interests*,' with an obvious reference to the energy resources [61]. In Putin's view, this was a field where Russia had competitive advantage over other world powers. Thus, preserving its role as Europe's main supplier while simultaneously developing energy ties with China and other Asian countries was set as the chief priority.[34] In that setting, intellectual relationships with the West became less welcome.

The EU was accused by Russia of acting as a "norm entrepreneur," pressing it to conform to its behavioral standards. Russia was no longer willing to accept norms from the outside that it did not help to craft, and wanted to show that the Western model was not the only right one [62]. In Russia's view, the West has had a "first mover advantage" in defining concepts such as democracy, sovereignty, and reciprocity. Putin claimed that Russia did not reject entirely this model, but wanted to propose an alternative. This resulted in the reversal of the trend toward democratization that occurred through the 1990s, with the Kremlin now controlling the appointments of governors and the upper house of parliament, and consolidating control over most broadcast media [65,67].

Developments such as the imprisonment of Mikhail Khodorkovsky alarmed European observers, who in the aftermath of the 2006 energy crisis with Ukraine began to highlight the risks of market power resulting from Gazprom's monopoly and the possibility of the Kremlin's playing the 'gas weapon' card as an instrument of foreign policy. Most of the scholars that adopted this alarmist tone, were also stressing the need to decrease the dependence on Russia by diversifying gas supplies constructing new pipelines directly from the Caucasus and Central Asia. This position was strongly backed by the United States. Meanwhile, Russia responded at times by threatening to re-route its exports towards the East, or in a milder tone, by pointing out that a new understanding of energy security was needed, one that goes beyond security of supply and takes into consideration the interests of all participants in the energy market [41]. By 2008, Russia declared diversification of its energy supplies towards China, Japan, and South Korea as its top priority [70].

Obviously enough, the expected privatization and liberalization of the Russian energy sector did not materialize. Rather, the Kremlin intervened and partially renationalized oil and gas resources to develop a predominantly Russian-based industry. It orchestrated a change in rules for parties and appointed Kremlin officials to corporate leadership positions in gas, oil, rail, airline, shipping, and other industries. With power thus centralized, President Putin rejected in hostile tones any external criticisms of Russia's political system and policy choices. Powerful insiders within the presidential administration (such as the Kremlin's chief ideologist Vladislav Surkov, and Rosneft's Igor Sechin) were now promoting a new vision for the country, embodied in terms such as "sovereign democracy," "financial sovereignty,"[35] "multipolarity in world politics" and "state capitalism."

Fully unprepared, the EU has struggled to find a common position on Russia's increasingly assertive stance on energy politics, and at first resolved to continue with its EU-wide "market and institutions" approach. Yet, in 2006, after the first Russia-Ukraine crisis, this approach was widely criticized for not having provided energy supply security. Many critics pointed out that Europe was rather naively expecting that exporting regulations and economic ultra-liberalism alone would provide for energy security [84,92,10]. Therefore, at the *macro level*, the liberal paradigm that prevailed in the 1990s was getting slashed by a growing "regions and empire" logic, a label that Van der Linde and Correlje [83][36] employed to describe the newly-introduced neo-realist style of problem-solving between Russia and the EU.

For instance, the political uproar surrounding a rumor that Gazprom was interested in buying Centrica, of the UK, in February 2006 was indicative of the EU's rather protectionist mindset at the time, which had been formally enshrined in the 2008 Commission's "reciprocity clause," dubbed as 'the Gazprom clause.'[37] That provision forbade foreign-producing companies to own part of transit and transmission companies' stock, despite the EU's liberalization principles[38] [22].

This closure in what was also dubbed "Fortress Europe"[39] was accompanied by an effort to defy the realities of interdependence by elevating narrow definitions of national interest. To make things even more complicated, while the European Commission and the constituent member states at the supranational level were moving hand-in-hand with the United States towards a harder and more politicized stance towards Russia, *at the hidden level*, individual member states were supporting their energy companies, which continued to cultivate fruitful energy relations with Gazprom, in line with European Commission's own market paradigm.[40] In sum,

[32] President Putin was quick to recognize the importance of energy as a strategic tool, arguing that it is energy which '*to a large extent determines Russia's place in World Politics.*' See: Energy Strategy of Russian for the Period up to 2020, approved by the Decree No.1234-p of August 28, 2003, issued by the Government of the Russian Federation, Accessible at: http://ec.europa.eu/energy/russia/events/doc/2003_strategy_2020_en.pdf.

[33] In 2000, Putin met with his country's business leaders and said he would back a proposal that would withdraw judicial investigation of the dubious privatizations that took place throughout the 1990s and produced the so-called oligarchs. But, in return he asked that these öligarchsS̈tay out of politics.

[34] Russia still supplies around a quarter of Europe's gas imports and despite the current 'gas glut' in the long run gas imports are projected to stay stable.

[35] The idea of sovereign democracy directly challenges the West's idea of democracy and human rights as a set of universal values and practices. This normative concept helps Russia to put forth its own d̈emocratic modelïn competition with the West. The first aim is to give ideological foundation to Putin's authoritarianism, and then to export it to Russia's neighbors. See, for instance Herd in Kanet, [33] p. 59 and Light [47].

[36] In a buyers' market situation, consumers favor a liberalized system integrated through 'markets and institutions' while in times of the sellers' market an 'empires and regions' scenario dominates, reflecting a fragmented global energy system dominated by power politics [83].

[37] The T̈hird country clause,öften dubbed the änti-Gazprom clausep̈aved the way for discriminatory and protectionist treatment as far as foreign investments are concerned, despite the Energy Gas Directives.

[38] Thus, it prevented foreign companies from acquiring energy assets in Europe unless their home countries reciprocated.

[39] Admittedly, Europe was somewhat forced to adapt to a more tense geopolitical context after 9/11, but in gas relations towards its main supplier (i.e., Russia) the switch has been quick and sudden; from somewhat extreme, ultra-liberal, Washington-consensus-type policies Europe went to quite the opposite, with the EU distancing itself from its own market principles and thus undermining its credibility and legitimacy.

[40] True, there were countries (and national energy companies) that welcomed this change of political wind in Brussels and its distinctly hostile view of Russia. Notably, countries such as Poland and the Baltic states (which rely on Russia for two-thirds of all their gas consumption), have seen in Russia a potential threat to their political independence and even territorial sovereignty, and relied on the US approach that firmly opposes Russian assertiveness. However, Russia's traditional customers and Öldm̈ember states (i.e., Germany, France, Italy) have often distanced themselves from such a stance and have sought to work in partnership with Moscow, warning that by promoting engagement with post-Soviet Eurasia largely through integration initiatives that are de facto closed to Russia, the United States and Brussels have

at the supranational level, the stronger role of national governments coincided with the phase of low-trust divisive globalization, where governments were taking more decisive and active roles. But oftentimes, at the *hidden-level* these very same governments were acting as supporters of their respective companies (or national champions) in their dealings with Gazprom.

Predictably, after the two Ukrainian crises (2006 and 2009), the EU–Russia institutional macro-dialogue had slowly but inexorably wound down and prospects for its recovery are slim. The ECT, for example, lost its institutional strength after it failed its main test: addressing the two Ukraine–Russian energy wars [90].[41] The Russian side, too, highlighted that the inaction on part of the political leaders of the Energy Charter Secretariat before and during the Russia-Ukraine gas conflicts undermined the credibility of the Treaty [41]. At last, the ECT became less relevant due to the new gas transit-avoidance geography (that began with the construction of Nord Stream), which was promoted by key European companies together with Gazprom.

In sum, in the 1990s, it was believed that the EU-Russia dialogue would result in growing similarity between the two. Yet to achieve this, Russia was implicitly expected to "transition" to Western standards, which would have reinforced cooperation. Thus, so the thinking goes, everybody would have benefited in the long run. However, from 2000 onwards, the incompatible EU-Russia narratives at the macro-level have hampered these efforts. Indeed, adjusting the 'rules of the game' to match both sides became a fertile source of contention Locatelli [50], Bressand [17], Yet, the EU simply has difficulties articulating a position towards this new dominant neighbor and offering incentives that do not include the export of Brussels' criteria, norms, and rules. This is why deep commercial interconnectedness is accompanied by a very weak institutional system. Table 3 illustrates some the main issues discussed thus far.

To be sure, overall, EU–Russian energy interdependence is managed with a dense web of relationships, but with no binding energy-governance structure. Therefore, somewhat paradoxically, despite the plethora of high-level meetings and summits, uncertainty pervades EU–Russian energy politics. In general, this article praises Constructivist theories and shares the opinion that norms do indeed matter a great deal at the EU-Russia macro level. In Locatelli's [50] words: "*The Russian state' s growing role in the hydrocarbons industry, exerted through various state-controlled companies, through the imposition of tougher conditions of access but also through the introduction of some form of competition, can be seen as an attempt to introduce an alternative organizational model more consistent with the country's institutional environment.*"[42] Nevertheless, these perspectives fail to capture, or at very least, fully explain, instances in which, at the *meso and hidden* level, in the midst of the large identity gap created by the Russo–Ukrainian crisis (in January 2006), individual gas companies (supported by the respective member states) did not think twice about negotiating new contracts with Gazprom, without fears of having to accept long-term commitments.[43] As eloquently described by Yafimava [90], the long-term contracts that the EU Majors renewed with Gazprom in 2006—before their expiry and despite (or, because) political tensions created by the Russo–Ukrainian crisis in January 2006, bear witness to the autonomy and bargaining power of these big companies. For instance, in November 2006, ENI and Gazprom signed a strategic partnership, which envisaged a commitment to jointly develop projects in the entire gas chain for the next thirty years.[44] There were instances when, in the midst of the worst political stagnation, EU companies initiated joint ventures and large-scale pipeline projects in collaboration with Gazprom. In July 2011, Gazprom announced a strategic partnership with the German utility RWE, just a month after one of the coldest EU–Russia Summits (June, 2011).[45] In contrast, the prevalent attitude among major players of the European gas industry was calm and even optimistic. The history of the EU–Russia energy relationship is full of such seemingly puzzling examples.

Moreover, in the 1970s the "normative gap" did not hinder a successful energy relationship between the Soviet Union and individual member states, at a time when "ideological irreconcilability" should have prevented such contacts from the outset.[46] Despite an even wider ideological divide, multi-decade contracts were signed, starting in the 1970s, between the Soviet Union and Austria, France, Italy, Finland, West Germany, and Sweden. If anything, changes in the international environment after the collapse of the Soviet Union have induced a closer notion of European and Russian identity that transcends traditional ideological boundaries. Hence, how do we explain a relationship that has been characterized both by conflicting patterns at the EU–Russian macro level and fruitful bilateral dealings at the company level?

Overall, at the macro level, the EU–Russia case demonstrates that, contrary to neo-liberal theories holding that high levels of economic interdependence enhance the need for predictable rules and standards as they lower the costs of cooperating, when a plethora of norms and identities do not match, mutual dependence causes serious impasses, rather than cooperation. In fact, when a multitude of disputed interests converge with high stakes for all involved, interdependence can lead to conflicting patterns. Another example of this logic would be the financial interconnectedness between China and the United States, which, amid very different institutional landscapes, in the final analysis leads to discord at the macro level.

Yet, while accounting for the deadlock at the macro level, the discourse on identities and values sheds only a partial light on EU–Russian energy cooperation. For the reasons described in detail in the next sections, the European Commission is challenged not only by the Russian reluctance to adhere to its rules and norms, but also, and most importantly, resistance stems from internal dynamics inherent in Europe, i.e. the energy firms as well as individual countries that benefit from the status quo. In fact, the tension between the EU and Russia is subtle.

(often unintentionally) forced Russia to make zero-sum choices. Most importantly, the older member states were wary about alienating Moscow on energy policy. These are the member states with the energy companies, which this article treats as key.

41 As noted by Yafimava [90], the failure to use the ECT to prevent, resolve, or at least assess the 2009 crisis has further undermined the instrument and made it less relevant to future disputes. The perception of the Treaty as a weak instrument during the crisis further undermined its legitimacy in the view of all the contracting parties, including the EU's member states and the corporate energy sector.

42 In e-mail correspondence with the Author, October 2012.

43 While in the aftermath of the 2006 Russia-Ukraine gas crisis, relations at the macro level were hitting one of their lowest points, all major European gas buyers, including German E.ON Ruhrgas, WIEH and WINGAS, French EDF, Austrian OMV, and Italian ENI renewed their long-term contracts (LTSCs) with Gazprom. The fact that these LTSCs were prolonged well before their expiry date suggests that the renewals took place at the request of the European gas companies, probably precisely because of the 2006 Ukraine crisis, where the EU buyers wanted to prevent a potential reaction of the Commission against Gazprom's activity in the European market ([90], p. 100).

44 ENI's Press Release, Ëni and Gazprom sign strategic agreementävailable at: http://eni.com/en_IT/media/press-releases/2006/11/Eni_and_Gazprom_sign_strategic_14.11.2006.shtml, Accessed in June 2013.

45 For a more detailed discussion see: Makarychev and Sergunin [53] EU-Russia: Divergent logics of communication, CEPS Policy Brief, no. 244, 17 June 2011 .

46 Instead, the first supply contract for Russian natural gas with a West European company was signed with OMV in 1968. In the same year, an agreement covering supplies of gas to East Germany was concluded. The first Russian gas flowed to West Germany on May 1, 1973. A year later, in 1974, Italy launched the first gas pipeline originating from the USSR. Ever since, Russia has continuously supplied these markets, which along with France became its most lucrative markets for natural gas.

Table 3
Constructivist key Reasons for the lack of EU-Russia energy governance structures.

Norms	Sovereignty	Reciprocity principle	Information sharing	Interdependence
EU	Liberal democracy	- Diffuse reciprocity - Market and rules-based governance but directed towards the export of the "*acquis commaunataire* "	- Transparent, accountable, and free exchange of information - Pluralist channels of information provision	- Interdependence enhances reciprocity and learning among countries and actors - Interdependence constrains a nation's ability to undertake autonomous policy initiatives
Russia	Sovereign democracy	- Quid-pro-quo reciprocity based on equality in power - Based on swaps of assets of similar market value or utility	- Independence from external influences - State control of strategic information - Provision of selected information	- 'Responsible interdependence' - Guarding state interests in energy requires concerted political action

Source: Own analysis, based on secondary data and interviews.

In order to fully implement its regulatory agenda, Brussels will need to overcome not only Gazprom's resistance, but also the hindrance of key European energy firms, which indeed are the main and most shrewd lobbyists[47] within the EU. Just like Gazprom, these firms oppose higher levels of institutional integration between the EU and Russia, and fear being institutionally locked into interdependence. These crucial actors, along with Gazprom, have benefited from the status quo. Thus, to say that the EU is a unitary actor promoting a certain organizational model that is resolutely rejected by Gazprom is not a valid criticism per se. With this in mind, we now turn to the illustrative cases.

7. The case studies

The aim of this article is to construct a strong explanatory model of the key players' behavior, while illustrating and testing the main hypotheses in the literature and adding my hypothesis about the centrality of energy firms and their profit motives. A comprehensive empirical analysis of EU–Russian energy cooperation requires a time frame of approximately 25 years in order to adequately grasp the "paradigm shifts" that have taken place. However, the period between 2000 and 2010 will be particularly important[48] to understanding why such a high degree of interdependence has not led to 'more institutions.'

Starting from 2000, the EU–Russia energy relationship has been characterized both by conflicting patterns at the *macro level* and fruitful bilateral dealings between Russia and single member states and companies at the hidden level. The case studies focus on all three levels. First, I examine the *macro level* . Parties to these relationships are the EU and Russia, national governments, and gas industries. Second, I look at the national, *meso level* where countries and gas companies develop energy policies and strategies that put them at odds with the EU. Third, a *hidden level* will be analyzed, with an emphasis on long-standing, intimate, company-to-company ties, which enhance this level's strategic importance. In this case, bilateral frameworks and bilateral contractual arrangements come into play.

The article also takes into consideration the broader impact of external factors such as recent technological developments in energy. The impact of such exogenous factors has been little predicted, let alone understood, in the energy policy literature. For example, neither the effects of the economic recession (which in large part explain the 2010–2012 gas glut in Europe) nor the groundbreaking technological developments in shale gas exploration were foreseen.[49] Therefore, more research on exogenous factors and how they impact the Eurasian gas business is certainly worthwhile.

7.1. The Southern Gas Corridor

The Southern Gas Corridor is the case that best illustrates the complex interplay between the three levels described, where the biggest conflict stems primarily from the tensions between:

1 The European Commission and Russia
2 The European Commission and Europe's national gas giants (backed by their respective governments) and Gazprom (backed by the Kremlin).

The previous section stressed that a lack of harmonized "rules of the game" at the macro-level exacerbates discord despite obvious energy interdependence. In some cases, it even stimulates the two sides to non-cooperative solutions in order to increase their respective "security of supply" and "security of demand." One example of this 'securitization' drive at the macro-level is the Nabucco pipeline and Gazprom's response, South Stream. Many have interpreted the Southern Corridor as the epitome of the fact that geopolitics is "back in" and that energy is not 'just another commodity.' The European Union as a whole and Russia are clearly adversaries in the race for the Southern Corridor. However, there is another level, one in which

[47] For example, within the Energy Charter Secretariat in 2004 an *Industry Advisory Panel* was put in place with members comprised of all the big gas (and oil) utilities in Europe. Within the EU-Russia energy dialogue, *a Gas Advisory Council* was founded, which is a platform for dialogue on issues of common interests, and consists mainly of representatives of the leading EU and Russian gas companies. Not to mention that some companies such as the Italian ENI, have their Delegations to the European Union. For more information: http://ec.europa.eu/energy/international/russia/dialogue/dialogue_en.htm, http://www.encharter.org/index.php?id=23, and http://www.eni.com/en_BE/eni-belgium/eni-profile/eni-profile.shtml.

[48] Because formal energy relations with Russia commenced in 2000 within the EU-Russia Energy Dialogue, in a period of high-energy prices and peculiar political changes in Russia.

[49] While ëasyöil and gas may be quite exploited globally, today we can be confident that there is no shortage in hydrocarbons on the horizon. Thanks to the breakthroughs of horizontal drilling, fracking in tight rocks, and many other new innovations, the perceived shortage of reserves was defied. In gas, these new technologies brought immense new supplies of gas on the market and lowered the American price for gas to an unprecedented level. In oil, the new techniques discredited the theories of þeak oil,änd have more recently acted on the price front, too. In other words these new technologies have developed techniques that are now, under certain circumstances, able to put a downward pressure on the price of oil. Oil prices continued to rise in the 2010s, although Maugeri's [55] study foresaw a collapse in oil prices in this decade.

specific geography and national politics have slowed the exit of the state, but have also shown that the real, albeit quiet, protagonists are the energy firms. It is at this level that Russia and specific European partners are not adversaries. On the contrary, they are often strategic partners united by trust and a shared corporate etiquette.

At the macro-level the Southern Gas corridor symbolizes that efforts for legal formalization of the EU and Russia's energy relationship failed, resulting in a gradual political drifting apart of the two neighbors. Instead of a shared "governance of existing Eurasian pipelines," various new pipeline projects such as South Stream, Nord Stream, Nabucco, and several smaller projects, respond to the 'securitization'[50] that started in the early 2000s and are tangible proof of the ECT's failure to address energy security concerns across Eurasia in a multilateral (and much cheaper) way.

At the surface, the battle over the Southern Gas Corridor's pipelines seems to indicate a classical zero-sum philosophy and mentality, in which one party's gains result only from equivalent losses or concessions by the other party. But the Southern gas corridor is more, and less. It is a multilayered, variegated economic competition for profits to be gained from privileged access to the southeastern quarter of the European energy market, where both strategic concerns and profit rationale play a role. But much of this pattern simply reflects the multi-level, intertwined dynamics that I have illustrated through my analytical framework at the beginning.

After the Russian–Ukrainian gas conflict in January 2006, energy security had re-emerged in European foreign policy agendas. The EU's active diplomatic efforts of these years are well documented in the European Green Paper "*A European Strategy for Sustainable, Competitive and Secure Energy*" in March 2006,[51] the First Strategic Review (in 2007) "*An Energy Policy for Europe* " and the Second Strategic Review in November 2008,[52] where the EU stressed the importance of energy solidarity among member states through the adoption of a collective "crisis management" strategy against possible disruptions. These objectives were to be achieved through a liberalized "liquid" gas market, the possibility for pipelines to operate in "reverse flow," more gas storage, and increased cross-border gas trading within the EU.[53]

Despite these admirable goals, the path towards a common internal gas market has been fraught with obstacles. The measures to ensure "resilience" [58,91] through an unbundling of the ownership of production and transportation capacities met with resistance from Russia and European gas firms. The owners of the pipelines resist these measures because they might attract competition. In this context, it is understandable why the path towards a common internal gas market has been accompanied by the EU's strong backing of the Southern Gas Corridor as part of a new 'Energy Silk Road' between Europe and the Caspian region, independent of Russia. In the aftermath of the first Russo-Ukrainian crisis the narrative at the macro-level in the EU had been all about diversification. This was considered indispensable for increasing energy security, since Russia allegedly was an unreliable supplier, and one that could use the "energy weapon" against Europe, its main customer. In more reasonable views, diversification was seen as necessary because of European skepticism about Russia's ability to provide enough gas for the growing needs of the EU economy (which was indeed growing at the time). This skepticism was based on Gazprom's risky, Kremlin-backed strategy to secure foreign markets and strategically lock up reserves, which has apparently pushed the company to its financial limits [24,32]. Essentially, for these reasons, the Nabucco pipeline became the cornerstone of the EU's strategy to tackle the impending 'Russian risk.' Nabucco was designed as a 3900 km pipeline from Turkey to Austria via Bulgaria and Hungary that would deliver up to 31 billion cubic meters (bcm) of gas to Europe per year and would cost roughly 8 billion Euros.[54] Russia responded to these attempts to "push Gazprom out of Europe" by announcing a 'transit avoidance' pipeline that would diminish the "Ukraine risk." To that end, Gazprom and the Italian ENI signed an MoU on the construction of an offshore gas pipeline, South Stream, in the Black Sea,[55] in addition to their collaboration over Blue Stream.

This bilateral agreement received much criticism from several member states, some of whom later signed on to the project. In 2009, a new Russo–Ukrainian gas dispute exploded in the middle of the winter, in addition to the already controversial 2006 crisis. This time, the dispute lasted several weeks and was the first time that Gazprom completely halted the flow of gas into Ukraine.[56] Proponents of both Nabucco and South Stream used the crisis as an argument in support of their own project [5].

At the *macro level*, in the spring 2007, Nabucco was granted the highest political priority, as laid down in the guidelines for trans-European energy networks (TEN-E).[57] To bring Nabucco to life the EU allocated $200 million from its own budget, which provided sufficient finance to carry the project through all the preliminary feasibility and detailed engineering study phases [71]. Although this may not seem a large sum, considering that the EU budget amounts to only about 1% of the member states' total GDP, it was quite significant. As documented by Kusznir [44], the Nabucco consortium also received 4 billion Euros from European banks: 2 billion of which came from the European Investment Bank, 1.2 billion from the European Bank for Reconstruction and Development, and 800 million Euros from the International Finance Corporation. Moreover, relying on a mandate of the then EU-27 states, the European Commission was strongly involved in the talks between the Nabucco consortium and the potential suppliers. It was the first time that the Commission was given such authority in regards to an energy infrastructure project. As noted byPirani ([69], p. 100), the proponents of the Nabucco line could hardly have asked for a stronger political backing to be sent to the Shah

[50] The concept of securitization as defined by Buzan and Weaver and more generally by the Copenhagen school, best captures what happened in EU–Russian energy relations at the *macro level* since 2006. According to Buzan and Weaver, securitization in energy issues ought to be portrayed negatively, because it is almost never successful. Because it is carried out at the international level it usually results only in politicization (Buzan, Weaver, Wilde, 1998. p. 71). Securitization is seen as a failure to deal with issues as normal politics, therefore de-securitization should be a preferred option when it comes to energy (energy security itself can be seen as a part of what Buzan et al. call the environmental sector within their relatively new concept of wider understanding of security, see f. e. Buzan, Weaver, Wilde 1998: 71–94). In this sense, de-securitization refers to the shifting of the issue out of the existential mode back into the normal political sphere.

[51] See http://ec.europa.eu/energy/strategies/2006/2006_03_green_paper_energy_en.htm.

[52] See http://ec.europa.eu/energy/strategies/2008/2008_11_ser2_en.htm.

[53] See Article 100 I of the new Lisbon Treaty: http://europa.eu/lisbon_treaty/glance/index_en.htm

[54] See, http://www.nabucco-pipeline.com/portal/page/portal/en/company_main/about_us, Accessed in December 2012.

[55] See, http://www.south-stream.info/en/pipeline/route/.

[56] For an analytically rigorous assessment of the dynamics between the EU and Russia, we need to take into consideration the risk that gas could be piped through transit countries, especially Ukraine. In the context of transit, fruitful contributions in which the relationship between Russia-transit countries [8], and Russia-the transit countries-the EU Yafimava, 2012 have been major objects of analysis, offer more detail. This section sketches the challenges that transit posits and the implications for the EU and Russia's relationship, but it explicitly abstains from going into detailed assessment of the responsibility for the gas disruptions. Suffice it to say here that at the time, formally, West European governments declined to take sides and rather apportioned blame to both sides for their shady dealings, insensitivity to European concerns, and downright incompetence [54].

[57] See Kusznir, J. *The Nabucco Gas pipeline project and its Impact on EU energy policy in the south Caucasus*, Caucasus Analytical Digest No. 33, 12 December 2011, p. 10.

Deniz consortium.[58] But the main actors in the process, energy companies both from the potential supplier countries and from the consumer countries, did not participate by splitting the risks. Thus, the EU's reinforced efforts to forge an energy relationship with Turkmenistan, with high-profile visits of Energy Commissioner Oettinger and Commission President Barroso to Ashgabat, turned out to be in vain. The realization of how difficult the process is without serious motivation from the corporate sector came in August 2012, when the EU Energy Commissioner Gunther Oettinger, having certified that Turkey was on board, visited Ashgabat to talk to president Berdymukhammedov, but was not received.[59]

In pursuing support Nabucco encountered several difficulties, the main one being the question of its resource base. There was simply not enough gas available to justify such a huge pipeline (31 bcm). But also, on the supply side, Europe did not need such a large pipeline, having slipped into economic recession in 2008.

However, the less favorable the economics looked, the more the European Commission tried harder to be a broker of Nabucco for the EU as a whole (a position that changed in 2011–2012 amid realization that, given that the economics simply did not work, the illusion of the original Nabucco coming to life could not be protracted any longer). Predictably, the EU's efforts to line up a coalition in favor of Nabucco failed. But the fragility of the Nabucco coalition was not due to the absence of convergent interests inside of the EU; most crucially, it was the dubious economic rationale for the pipeline that ultimately destroyed it. In an attempt to fudge these inconsistencies, starting in 2011, the Commission suggested its 'neutral' position on the Southern Corridor-related matters.

In the words of an EU's top civil servant: "*We do not support any particular pipeline-project. Nabucco didn ' t have the needed volumes, so other alternatives are now discussed. Having said that, we strongly support at least one project that will be able to satisfy the criteria of capacity requirements, dedicated infrastructure, transparency, and scalability. The final decision has to be a commercial one*."[60]

Although the mixed effects of an unprecedented economic recession, the advancement of the EU's Third Energy Package, and the availability of new gas supplies due to the shale gas revolution in the US, froze gas demand and signaled profound changes in the EU gas markets, the pipeline coalitions on both sides (i.e., Nabucco and South Stream) ignored these developments and proceeded regardless, granting an ever-increasing priority to their preferred projects. Yet, there is a substantial difference in the two coalitions. While Gazprom can afford such policies, due to a unique and symbiotic overlap of Gazprom's corporate interests with the Kremlin's goals,[61] Nabucco had to stay profitable in order to get built, which made Nabucco less commercially attractive for private investors. Gazprom had the necessary gas, deep pockets, and a top down approach to be able to pass the cost on to consumers. To a degree, the high cost of new gas export infrastructures could have a negative effect on Gazprom's ability to generate profit on the domestic market.[62] However, as a state-owned company, Gazprom could count on political support in exerting pressure for its preferred solution to the Southern Corridor question (i.e., South Stream), while maintaining a dominant position in the Russian gas market.

All that is not possible with EU-sponsored projects, where investment decisions based on political calculations (i.e., Nabucco) inevitably tend to fail. In a market economy, an unsound business proposition simply has trouble finding the needed financial investment to sustain it.[63] And, as stressed before, the EU is not a geostrategic actor *per se*, able to further a foreign policy goal corresponding to the 'common good' of 28 member states.[64]

As a result, by 2008 all the countries of the Nabucco Consortium were leaning toward South Stream, with Serbia, Slovenia, Austria, Bulgaria and Greece welcoming the project as a significant additional route that would enhance the EU's energy security.[65] Hungary, a country that initially fully supported Nabucco made an impressive u-turn toward South Stream. Thus, by mid-2009 the most vulnerable East European countries, precisely those for which the Nabucco pipeline was promoted as indispensable i.e., Bulgaria, Hungary and Serbia,[66] all agreed to play an instrumental role in the construction of South Stream, further undermining Nabucco.

Moreover, the very same bilateral pact between Gazprom and ENI that received much criticism was enlarged, with a great deal of controversy, in 2009 to welcome EDF, a French company, and in 2011 the German BASF, all of which boosted the credentials of South Stream as a European project. Actually, it was quite an easy game for Gazprom to deter the interest of Nabucco's investors; The investors only had to see that South Stream offered not only a more rapid construction schedule but also defined supplies of (Russian) gas, all of which Nabucco did not have. Thus, the French and German firms jumped on board with the Italian–Russian plan for the offshore part of the pipeline. Plus, as already noted, an increasing number national companies in Eastern Europe were eager to join South Stream in the attempt to protect their respective interests.

To be sure, Russia's role in undermining Nabucco was not negligible. After the death of the Turkmen isolationist leader Saparmurat Niyazov,[67] Gazprom had been prepared to offer sizable increases in the price paid for Turkmen gas in order to secure gas supplies

[58] Moreover, the project benefitted from the exemption of third-party access for half of the pipeline's capacity (in Austria, Bulgaria, Hungary, and Romania), in contrast to South Stream. During this time the European Commission was officially shifting into a 'Nabucco neutral' position, given the evident difficulty in reaching the initial gas input for the pipeline. Therefore, not only has the European Commission supported the pipeline, both politically and financially, but also in doing so it has stretched well beyond its legitimate powers, while failing to abide by the obvious limitations of its energy diplomacy.

[59] T̈urkmenistan Snubs EU Over Trans Caspian Pipeline, NefteCompass, 20 September 2012, quoted in Pirani ([69], p. 101).

[60] Interview with the author, May 2012, DG Energy, Brussels, May 2, 2012. Interviews were conducted with heads of businesses, high officials both in Russia and the EU and influential energy experts. Due to the sensitivity of the information, most of the information obtained during interviews was 'non-attributable.'

[61] The fusion of Russia's external agenda and gas strategy has reached such a degree that it is almost impossible to establish whether it is foreign policy that serves Gazprom's interests, or whether Gazprom is an instrument for restoring Russia's g̈reatness,b̈ut suffice it to say that the interests of Gazprom and the Russian state are profoundly linked. Energy policy is a domain of strategic importance both for the Kremlin and Gazprom, and the crucial question whether there is a symbiotic coherence between the two has attracted increasing academic attention (see among others [79,28,14,21].

[62] It is the epitome of Russia's risky strategy to invest more in the construction of strategic pipelines than in its own infrastructure or storage capacity. Gazprom has generally sought ownership of downstream assets to ensure European outlets for its gas, instead of tackling its stagnating domestic exploration projects, which are necessary to make up for falling production. And in fact, recent studies suggest the possibility that Gazprom, which is becoming more reliant on production from remote and relatively expensive fields, may soon fail to produce enough gas to meet its own domestic and export demand (see [24,34].

[63] Because it has to guarantee profit to shareholders and banks right from the outset.

[64] It is important to note that liberal-style denunciations of Nabucco's geopolitical fiasco as being due to an incoherent and nonchalant approach on part of the EU should not discount the limits of an EU-led foreign policy.

[65] Simply by circumventing Ukraine.

[66] Countries such as Bulgaria, Greece, Slovenia, and Hungary all rely on Gazprom for more than 50% of their gas imports.

[67] Throughout the 2000s Russia relied on two techniques to block European diversification and keep the status quo in the Caspian region: (1) Gazprom bought Central Asian gas at one price, transited it to Europe, and sold it for a higher price; or, (2) Gazprom bought cheaper Central Asian gas for domestic Russian consumption and saved its own gas for higher priced exports to Europe. Up until 2009, with demand for gas booming and seemingly unstoppable, Gazprom counted on imports of large volumes of gas from Central Asia as its own production stagnated. Without it, it was believed that the Russian giant might have not been able to honor its export contracts and meet the growing domestic demand. All that changed with the European

for the domestic market and to discourage Turkmenistan from non-Russian pipeline projects, especially aiming to head-off any possibility of Turkmenistan committing supplies to Nabucco. Europeans were also unimpressed by Gazprom's purchase of gas from Azerbaijan, which it clearly did not need, with the apparent objective of reducing the supply available to the Southern Corridor. As noted by Stern ([77,78], p.99), the Russian side had a far greater familiarity with most of the potential Southern Corridor suppliers than did most European stakeholders and could therefore defend its interests from a position of strength. While Moscow's efforts to secure the largest share of the cake for itself were undeniably in line with its geopolitical realism, the EC's meddling in the Southern Corridor too was, starkly in contrast with its own multilateralism at the EU level.

Nonetheless, what made Nabucco an unviable proposition is simply the fact that political factors are of far less importance than business rationale in pipeline construction. Nabucco, did not fail because of insufficient political will and unity, which was on the contrary unprecedented for such an infrastructural project, but rather because of Nabucco's irreparable economic flaws and the fact that its coalition did not feature the main European players: EDF, ENI, and Wintershall.

Therefore, in light of my analytical framework, it is important to look "deeper" in order to answer the question: *was it really in everyone's interest within Europe to advance the Nabucco plan? Who would have been the winners and who the losers of such a pipeline? Most crucially, where did the dominant actors stand?*

Many have thought that if the Nabucco project failed, South Stream would have been abandoned. This did not happen (until the recent unexpected decision to scrap the project),[68] because South Stream was mainly conceived with the purpose of cutting Ukraine out and was, therefore, the epitome of Gazprom's eagerness to remain the key player in the European gas market.[69]

While Gazprom restlessly stressed that South Stream was not meant to outcompete the other Southern Gas Corridor projects, its target markets were roughly the same as Nabucco's. As acquiescently pointed out by a European diplomat, "*There is no outright competition since South Stream is mostly promoted to circumvent Ukraine and hence it does not guarantee new sources. Investors though, don't see it that way. They remain risk averse in the current gas glut.*"[70]

Gazprom had always claimed that South Stream would not bring new volumes of gas to the EU, and would only redirect already contracted volumes. But it was bizarre, at the very least, that Gazprom was prepared to invest so much money for the shipment of old gas through a new pipeline. This seems to point to Gazprom's *hidden* interests as the real cause of their actions. Moves such as securing markets instead of enhancing product quality or output and marginalizing competitors by controlling market access and infrastructure fulfill the criteria of a textbook monopoly rather than point to politicized motives [24].[71] The Kremlin, on the other hand, backed a strong expansion course of its state-owned monopoly, because its own survival depends on the revenues that Gazprom (and Rosneft) are able to generate on the foreign markets. However, the strategy to seek ownership of downstream assets to ensure outlets for gas *is distinctively* Gazprom's, and has been declared risky even by the Russian government, amid stagnating domestic exploration and production projects, which are needed to make up for falling domestic output.

In addition to the declared objective of definitively eliminating the risk of Ukrainian gas transit (despite the unsoundness of this project from a wider economic perspective),[72] there may have been hidden corporate insiders within Gazprom who were interested in building a project of such dimensions. These insiders, due to the symbiotic relationship between Gazprom and the Kremlin, managed to sell Putin on the necessity of the project. The costlier the project is, the greater the potential profits made by these insiders. Despite such a reality, the increased importance of internal power bargains, not to mention personal favors involving money in the Russian decision-making processes, has been continuously underestimated by Western experts ([20], p. 207). The difference both in principle and in substance with the Nabucco project is that, in order to look feasible, the latter had to guarantee an acceptable rate of return right from the outset and contrarily to Gazprom, it could not transfer the financial burden on to consumers.

Hence, in contrast to authors that refer to Gazprom as a mere proxy of the Kremlin [9], or, as 'synonymous' with the Kremlin [47], or even the more moderate literature arguing that while business is important, the Kremlin is the head and Gazprom is the hand in achieving strategic goals decided on by the government [92,79,66,10], it seems right to agree with Grigoriev [28] and Demakova and Godzimirski [21], in their view that Russia's approach in gas trade largely mirrors Gazprom's own interests. As the case on the 'third energy package' illustrates, Russian state-capitalism creates fewer constraints to Gazprom than regulations in a competitive market economy do with the European companies. To a certain extent, Gazprom is free to do almost anything to boost its profits and fill state coffers. Admittedly, during the 2000s the company was facing two often-incompatible tasks: aligning with the state's geopolitical interests and boosting profits. For example, Gazprom viewed the discounted prices that the CIS countries were paying on the grounds of their status as 'zones of privileged interests' as inadmissible, and thus it has pushed for a market-based relationship with the whole FSU.[73] Gazprom's insistence on higher prices in the 'near abroad' coincided with substantial uncertainties over its sales to European markets, which were increasingly looking for other sources of gas, meaning that their commercial viability would need to be underpinned by domestic (and CIS countries) sales[74] to guarantee a minimum rate of return ([31] p.15).

It suffices here to say that Gazprom's will prevailed over the government. If we take a more nuanced view of their relationship, we recognize that Gazprom has often clashed with the government in the pursuit of its economic interests, which were not always aligned with the state's political design.[75] Yet, it is clear that a project such as South Stream was conceivable thanks to a unique symbiosis between Gazprom and the Russian state's leadership.[76]

recession in 2008. Suddenly, Gazprom had excess supply and did not need Central Asian gas to cover its commitments in Europe.

[68] See note 55 on page 24.

[69] The EU has always feared that as Gazprom gains interests in downstream assets as well as controls upstream supplies, its market power will grow at the expense of EU's consumers.

[70] Interview with the author, May 2012.

[71] Gazprom's strategy of increasing its vertical integration and marketing its gas directly to the consumers is sensible and perfectly in line with a monopoly's behavior. This is a purely rational move by a market actor aiming at exclusive delivery to a profitable market ([24], p. 33).

[72] The EU's economic recession lowered gas demand, in turn triggering a 'gas bubble', which put a question mark over the economic rationale of building 63 bcm of new capacity in addition to the already existing one.

[73] For more a detailed analysis on the quid pro quos with Ukraine and the other CIS see [68].

[74] As of 2011, Gazprom still accounted for 70 per cent of domestic Russia's consumption, although the shares of Non-Gazprom producers were rapidly growing ([31], p. 2).

[75] Since the subsidized prices in the CIS and in Russia itself were undermining the firm's profitability, they were gradually adjusted. Of course, Gazprom would prefer a faster adjustment [28].

[76] It seemed that the political value of transit risk reduction, plus the economic value of remaining the only pipeline supplier to Europe, compounded with the profit motive of some Gazprom's insiders (interested in promoting a huge project, whose cost would be then passed on to consumers) were seen as justifying the investment.

This raises the question of why foreign partners are willing to invest in Gazprom-sponsored projects?

Western companies, indeed, are eager to invest in upstream gas projects in Russia, and so they find it difficult to resist an invitation from Gazprom ([77,78], p. 78.) For instance, the Gazprom-ENI 50-50 agreement on South Stream, signed in 2006, was part of a massive *quid pro quo* that expanded Gazprom's access to the Italian end-use market, in exchange for a long-term gas contract [41]. In 2011, when the big German company RWE was left seriously out of money, Gazprom offered a discount in exchange for a strategic partnership with RWE that would expand Gazprom's access to the German market (European Energy Review, 2011). The arrangements between Gazprom and the European companies are based on a quid pro quo concept of reciprocity, while at the macro level, the EC lobbies for diffuse reciprocity, based on common rules and values [13].[77] The Russian notion of reciprocity is "specific." In energy, that essentially means swapping assets of similar market value or utility [51]. For example, in 2009, the German utility company E.On AG has gained a stake in the Iuzhno-Russkoe natural gas venture under an asset swap deal with Gazprom.[78] In 2010 Gazprom and ENI finalized their asset swap in Libya.[79] And again, in 2012 the German group Wintershall, agreed to swap parts of its oil and gas fields in the North Sea for a stake in a Siberian field owned by Gazprom.[80] Such business deals are entangled in a traditional web of bilateral ties between Russia, Germany, France, and Italy.

The failure of the Nabucco proposal shows that the EU as a whole has a substantially different relationship with Russia than the European energy firms, who are backed by sovereign EU states. The Southern Gas Corridor is well suited to shed light on this two-tiered relationship between Europe and Russia: on one level there are the fruitful business alliances of Gazprom and the European gas giants such as Gaz de France, Wintershall and ENI. On the second level there is a mostly ineffective working relationship between Russia and the EU. In this dynamic, the sovereign states play mainly supportive roles. Political support is welcome, especially when dealing with giant counterparts such as Gazprom (and Russia). But the Southern Gas Corridor demonstrates that the key corporate influence on Eurasian energy policy is indeed well documented. In this respect, the case study finds an inverse relationship between the intensification of the 'battle of the pipelines' and the likelihood for the EU and Russia to form multilateral rules-based partnerships.

7.2. Russia' s reluctance to adhere to the ECT and to renew the PCA

The Partnership and Cooperation Agreement (PCA) with Russia was signed in June 1994 but entered into force only in 1997. The PCA was set up to enhance the political dialogue between Russia and the EU. The ambition was to promote democracy, trade, and legal convergence. Yet the first PCA is a product of the 1990s [87] when 'policy convergence with Russia' essentially meant Russia's alignment with EU values and institutions. Within the PCA, energy is dealt within Article 65, and indirectly in Article 12, which refers to the freedom of transit.[81] The agreement covered a ten-year period that expired in 2007, but anticipated automatic extension until the conclusion of a new agreement. Negotiations over the follow-up began in July 2008, but were suspended one month later because of the war in Georgia. They resumed next year, but both sides were disappointed with the slow progress of negotiations.[82] The question of what type of agreement should replace the old PCA became an increasing point of contention.

The years 2000-2007, after Putin's rise to power marked a considerable change in Russian state identity [11]. The first PCA substantially reflects Europe's optimistic belief that Russia would rapidly adopt Western (or, more precisely, European) values regarding human rights, the rule of law, democracy, and free markets. Yet when negotiations about the renewal were held, Russia's political stability had been restored and energy prices were at their highest peak. As a result, Russia wanted a more "equal partnership."[83]

At a *macro* level, negotiations on extending or replacing the PCA have been held up by "normative" objections. The EU was pressing for a relationship based on adherence to common values while an increasingly autocratic Russia was torn between deepening the cooperation with the EU, and guaranteeing "high" Russian sovereignty and freedom of action. This divergence resulted in the emergence of different ideas, ranging from a minimalist (i.e., Russian) approach to an ambitious (i.e., EU) vision of the new PCA [54].

Many scholars pointed out that conflicting normative views and psychological factors continued to plague ongoing talks on the new PCA. For example, Article 55 implied approximation of Russia's legislation with the *acquis*.[84] Also, the document stipulated the respect of human rights, a market economy and democracy as its general principles. However, the EU's general focus on complex, often low-level projects was seen as at odds with Russia's preference for less substantive but more visible statements. In short, Moscow thought to have discarded the PCA because of its form, because the same instrument was offered to all former Soviet states [6], and because Russia would have preferred if the new PCA granted the Russia the status of a strategic partner with Europe (see [86,54].

While these scholars' explanations have analytical utility, they only tell part of the story, and not the crucial one. *At a hidden level*, Moscow's objections to the new PCA did not stem from a rejection of the EU's norms and principles, but rather from objective calculations of national interest. The EU was hoping that Russia would accept the incorporation of some of the ECT principles in the post-PCA agreement, in return for a free trade agreement (FTA). But Moscow had little interest in better EU market access: three-quarters of its exports to the EU consist of raw materials, which are hardly affected by trade rules anyway. EU tariffs on Russian goods are already rather low and energy, which makes up the bulk of Russian sales to the EU, passes tariff-free. Thus, an FTA offer, in return for Russia signing on to bilateral, binding rules on energy trade, transit, and investment, was simply not seen as sufficiently

[77] Belyi's study displays great theoretical sophistication in showing that, given the EU-Russia conflict of interests and principles, ñegative reciprocitÿbecomes an inherent factor of international practice and hence a norm in EU–Russia gas trade.

[78] Gazprom Press Release, *Gazprom and E.ON close asset swap deal*, October 30, 2009

[79] Ria Novosti, *Gazprom agrees asset swap with ENI to join Libya's oilfield project*, April 12, 2010.

[80] Bloomberg, *Gazprom Offered New Assets by Wintershall in Siberian Swap*, Jun 6, 2012.

[81] European Commission, Summaries of EU Legislation: http://europa.eu/legislation_summaries/external_relations/relations_with_third_countries/eastern_europe_and_central_asia/r17002_en.html, Accessed in September 2012.

[82] Currently the öldP̈CA continues automatically because neither side took any steps to renew it.

[83] The second set of concerns was linked to Russia's disappointment after the EU's 2004 and 2007 enlargements, which left Russia frustrated. In Moscow's view, its concerns on critical issues (Kaliningrad transit, the Russian minorities in Latvia and Estonia) were not taken sufficiently into account. Amid Russian complaints the EU responded curtly; ünless the PCA was applied to the EU-25 without precondition or distinction by 1 May 2004, Russian–EU relations would be seriously affected.R̈ussian concerns are set out in a report, 'The Effect of the EU Enlargement on Russia's Economy', Moscow, 2004: Quoted in Light [47].

[84] See Art 1. T̈he Parties recognize that an important condition for strengthening the economic links between Russia and the Community is the approximation of legislation. Russia shall endeavor to ensure that its legislation will be gradually made compatible with that of the Community.¨http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:21997A1128(01):EN:NOT.

attractive by Russia. Instead, the latter was busy developing its own FTAs with the CIS countries, where Russia aspired to an economic and political sphere of influence. In fact, in June 2012, Putin added insult to injury by making clear that his country cannot advance negotiations on a new PCA unless Brussels formalizes relations with the so-called “Common Economic Space”—its Customs Union with Belarus and Kazakhstan. In 2012 an EU official said “*Russia highlights that it is a sovereign country with independent decisions. Yet, our FTA offer is not easily compatible with the Customs Union* ”, adding, “*currently we are in a fairly vague state of affairs.*”[85]

Ever since, non-tariff barriers and approximation of legislation became a critical point of contention. Russia has shown no intention of accepting a deep and comprehensive FTA with the EU as long as it entails approximation with the EU’s *acquis* . The reasons are straightforward: as already mentioned, energy, which makes up the bulk of Russian sales to the EU, passes tariff-free. Thus, the gains of a deep FTA with the EU do not outweigh the cost of amending its regulatory structure and being locked in a legally binding agreement that would limit Gazprom’s freedom of action.

Similarly, the EU spent years trying to get Moscow to abide by the provisions of the Energy Charter Treaty (ECT), which would compel Russia to open up its hydrocarbon reserves and pipelines to foreign commercial involvement. Moscow, on the other hand, signed the ECT and applied its rules on a provisional basis, but never ratified it. For years, Russian officials complained that the ECT was outdated and favored consumers. At last, in August 2009, then Prime Minister Vladimir Putin signed an order withdrawing from the Treaty [81]. Broadly unsatisfied with accepting a system of laws that it did not help to craft, and which it considered highly disadvantageous for producers, Moscow came up with the idea of a new global energy regulation system. In the aftermath of the January 2009 crisis, President Medvedev tabled an alternative to the ECT: ‘the Conceptual Approach to the New Legal Framework for Energy Cooperation.’[86]

Again, at the *macro* level, Russia lamented the EU’s aim to expand its value system and laws through cross-border gas value chains, stretching from the EU to gas producing countries. In Russia’s view, the EU’s first directives, which had obviously been tailored without Russian participation were ‘exported’ through the ECT [42]. Russia increasingly pointed to the one-sidedness of the treaty and its failure to address Russia’s concerns.

In an effort to go beyond the macro level, this article holds that the non–ratification of the ECT is above all in Gazprom’s interest. In 2011, Gazprom still accounted for 70% of Russia’s domestic consumption, although the shares of non-Gazprom producers were growing ([31], p.2). It is often forgotten that Russia, unlike any other major energy exporting country, is one of the world’s leading energy consumers. Russia is the world’s second largest consumer of natural gas, and accounts for 54% of Gazprom’s annual sales.[87] Yet, given that the domestic market is heavily subsidized, the main sources of Gazprom’s hard currency are the EU countries. In the 2000s, when both the domestic and the EU markets were booming while Gazprom’s production growth was virtually zero, Gazprom had troubles meeting its delivery commitments both at home and in Europe. The resolution lay in an interesting *escamotage*. Gazprom started to increase the volumes of gas it bought from Central Asia. The strategy consisted in importing Turkmen gas for the domestic market, while Siberian gas was sent to Europe. That is why Russian diplomacy in Turkmenistan was so active, and Russia even increased the price it paid for Turkmen gas just to keep this indispensable country on board. This allowed Gazprom to be the intermediary and, at least until 2009,[88] the sole buyer of Turkmen gas, which it received for relatively cheap and then resold for much more in the EU market, or kept for domestic consumption. Therefore, Gazprom’s strong lobbying was arguably the main reason for Russia’s rejection of the ECT. As already noted by Milov ([57], p. 92) Gazprom never actually tried to hide its intention to capture Turkmen gas through its transit monopoly, and has openly denied the right of European consumers to conclude direct gas-purchase contracts with Turkmenistan. This has been the primary (and probably the only) cause of Russia’s refusal to ratify the ECT and its Transit Protocol[89]; Gazprom had always defended its right to exert the transit monopoly over Turkmenistan and arbitrarily decide on Turkmenistan’s access to international gas markets. Yet there is another important factor missing from this analysis. EU companies, which are the main drivers of the EU’s energy-related unity and disunity, also favor non-ECT ways of managing potential risks in their business relations with Russia. Typically, European firms choose to mitigate risks with measures such as joint ventures/asset swaps and diversification of supply sources and routes, which ensure “resilience” (with gas storage, interconnectors, etc.). Gazprom manages the demand side with diversification of export markets, mergers and acquisitions [85]. Therefore, the European companies and Gazprom are united in opposing the ECT.

To be sure, EU companies would benefit if Gazprom opened up its pipelines. However, Gazprom’s traditional friends within the EU are already rewarded with cheaper prices for gas (compared to other European counterparts), and thus have everything to lose from spoiling the atmosphere with Gazprom. They are wary about any radical moves that might upset Gazprom. As documented by Youngs [92] p. 39) a number of member states reject the notion of transparency and information sharing with the EU on the bilateral deals they conclude. That is hardly surprising, considering that Gazprom likes to strike deals country-by-country, which enables it to reward friends and punish enemies. Germany, for example pays among the lowest gas prices in Europe. Lithuania, on the other hand, which has pushed ahead with unbundling and had strong EU support for it, now has almost the highest gas prices in Europe. The intuition is simple: consumer countries do indeed have an incentive to contract supply on a bilateral basis and renounce EU or ECT-based rules, because that enables them to secure the best deals.[90] As Barkanov [11], p. 360) argues, on certain questions EU business actors are sympathetic to Russia’s policy. Thus, within the EU, a corporate-driven version of balance of power prevails. Consequently, for key EU energy companies backed by their respective governments, the European angle is secondary, and instead they prefer explicit modes of *realpolitik* in the pursuit of profit [4].

[85] Interview with the author, European External Action Service, Brussels, May 3, 2012

[86] At the end of April 2009, then President Medvedev said that Russia feels the need to provide its own legal basis for the relationships with energy consumers and transit countries. The new document was posted on Medvedev’s official website, but right from the outset met with skepticism within the EU. In the view of an EU official,¨*it is pretty comprehensive, including strong borrowings from the ECT. The slight ambiguity is on its legal nature; it was transmitted as a draft legal text resembling the ECT, but with many provisions clearly in producers’ interests.*”

[87] See: http://www.gazprom.com/about/marketing.

[88] When the massive Turkmenistan–China gas pipeline was inaugurated.

[89] Article 7, Transit, ECT.

[90] Energy companies that receive preferential prices and have different gas tariffs might be unenthusiastic about provisions such as Article 29 of the ECT, which stipulates: “*Each signatory to this Treaty, and each state or Regional Economic Integration Organization acceding to this Treaty, shall on the date of its signature or of its deposit of its instrument of accession provide to the Secretariat a list of all tariff rates and other charges levied on Energy Materials and Products at the time of importation or exportation, notifying the level of such rates and charges applied on such date of signature or deposit. Any changes to such rates or other charges shall be notified to the Secretariat, which shall inform the Contracting Parties of such changes.*” Or, for example, Article 3 which stipulates, “an *efficient functioning of market mechanisms including market-oriented price formation and a fuller reflection of environmental costs and benefits.*”

Largely to fill the legal vacuum that emerged following Russia's non-ratification of the ECT, an EU-Russia energy dialogue was put in place.[91] However, the energy dialogue is, as the name implies, a non-legally binding consultative mechanism. Throughout its existence, it reflected the growing mistrust between the EU and Russia at the macro level. Its launch in 2000 was marked by political optimism, when the Prodi Plan foresaw the doubling of Russian gas imports to the EU [89]. According to this plan, the EU would use its political influence to channel foreign investment in the Russian upstream and provide technical assistance for the exploitation of gas reserves. In return, Russia would guarantee secure supplies of gas, in view of an ever-closer common energy space. Yet, Russian energy nationalism was growing in parallel with the soaring price of hydrocarbons, and by the mid-2000s, Russia was less prone to accept any formal integration. Once again, at the macro level the dialogue reflected two different approaches. Brussels assumed that the dialogue would essentially facilitate investment in the Russian energy sector and allow European companies unrestrained access to Russia's pipeline network. Furthermore, the EU approach consisted in linking energy security to climate and environmental protection. Russia, on the other hand, aimed at maintaining its dominant position in the European gas market, as well as Gazprom's monopoly structure and long-term oil indexed supply contracts. Both sides were disappointed. When gas prices increased Russia reintroduced steady state-control over the oil and gas industries, and Gazprom's monopoly of the pipelines was only reinforced with a law on the pipelines in 2006.[92] Nevertheless, the EU had a significant victory within the Energy Dialogue when it succeeded in abolishing the restrictive 'destination clauses' in Russian long-term contracts [74]. For Russia, the main results were the agreements that no quantitative restrictions would be placed on the EU's imports on fossil fuels. Moreover, within the Dialogue, *a Gas Advisory Council* was founded[93]; a platform for dialogue on issues of common interests that consists of representatives of the leading EU and Russian gas companies and of experts from the Russian and European academic research organizations. Before the seizure of Crimea, gas contracts renegotiations[94] were among the most contentious issues disputed at the Advisory Council. Moreover, Russia feared that the EU's ambitious decarbonization targets would have a negative impact on its gas exports, making this a significant topic of dialogue. Whether, when, and how these different views can be reconciled at a macro level remains a thorny question. In the blunter words of a Russian energy insider: "*There has been an overly long, unsuccessful negotiating process, and hardly anyone in Russia believes that a satisfactory working formula can be found. The EU is not offering anything attractive and these summits are largely symbolic. Outcomes are expected and predetermined long before the actual meetings.*"[95] The Ukraine crisis polarized the two positions even further with the EU now seizing the moment to advance with its Energy Union[96] and to push for reform and influence in Ukraine, and with Gazprom becoming even more intransigent on Ukrainian transit. In turn, the two sides' dialogue froze and this, in turn, impeded the ability to work on preexistent issues (like the Third Energy Package, the EU's anti-trust case against Gazprom for market abuse through country-by-country pricing, and the wrangling over the exemption for the OPAL pipeline) through the Gas Advisory Council and other diplomatic channels.[97]

Meanwhile, the European corporate sector responded negatively to the EU's aspirations to put teeth in its external energy policy. Through Eurogas,[98] the European gas sector has recently increased its activity, fearing that the Energy Union measures have been trying to squeeze natural gas out of the EU energy market. Moreover, controversies generated by the gas disruptions and (most recently), the geopolitical predicament over Ukraine did not significantly complicate the EU companies' fruitful relationship with Gazprom.[99] The three major recent deals with some of Europe's biggest energy companies, which Gazprom clinched at the Eastern Economic Forum in Vladivostok in early September 2015, underscore that point.[100] One of the most important is the deal between Gazprom and its European corporate partners to expand the Nord Stream gas pipeline, but there is also the revival of a lucrative asset swap between Gazprom and Wintershall—a German subsidiary of BASF—a deal that will effectively transfer 100% of the company's gas trading business, as well as a 50% stake in exploration and production activities in the North Sea to its Russian partner, in return for a 25% share in block development of Russia's Achimov deposits in the Urengoskoye region. BASF had abandoned that swap arrangement in December 2014 because of the geopolitical consequences of Russia's invasion of eastern Ukraine and its annexation of Crimea. The deals confirm the extent to which Russia is determined to end Ukraine's role as the major transit route for Russian gas to Europe. But most importantly, the asset swap and other deals show that European companies are loath to abandon Russia and that the latter's pivot to Asia will likely not be as quick and lucrative as the Russians have hoped for—with Europe remaining the most reliable, lucrative, and the most painfully essential market for Russian gas.[101]

7.3. The Third Energy Package

At the macro level, today the conflict between the EU and Russia is focused primarily on the implications of the "Third Energy Package." This touches upon the very core of the EU–Russian deadlock at the visible, grand level. Moscow's aim is to distance itself from the EU institutional model, and to promote a legal framework that is consistent with Russia's institutional choices. For example, Gazprom's strategy for the European market is based first and fore-

[91] The Energy Dialogue was launched in the occasion of the 6th EU-Russia Summit (Paris, October 30, 2000).

[92] On 20 July 2006 the federal law Ön Gas Exportäpproved by the state Duma granted Gazprom exclusive rights to export natural gas: Law of Russian Federation of 18 July 2006, N. 117. In addition, Russia adopted two other Laws, with the apparent aim at getting state control over investments into natural resources: the Strategic Investment Law 123 and the Subsoil Law 124 (Law of Russian Federation of 29 April 2008 N 57—AP, and Law of Russian Federation of 03 March 1995 N 27—AP, amended 18 July 2008 N 120—AP).

[93] For more information: http://ec.europa.eu/energy/international/russia/dialogue/dialogue_en.htm.

[94] Due to fundamental changes in the global gas markets that put pressure on the indexation structures.

[95] Phone-Interview with the author, October 2012.

[96] The energy union strategy will be divided into five pillars (Ensuring security of supply; Building a single internal energy market; Raising energy efficiency; Decarbonizing national economies; Promoting research and innovation) and will give new impetus to existing legislation. Moreover, the G7 Energy Ministerial meeting in Hamburg has identified the support of most vulnerable countries, including Ukraine, as one of its top four areas of joint action. See: https://ec.europa.eu/energy/sites/ener/files/documents/BMWi%20Papier_G7_12_5_2015_e_final.pdf.

[97] European Commission's DG Energy top civil servant—Interview with the author, Brussels, May 2015, Brussels; Gazprom Export's executive—Interview with the author, Moscow, June 2015.

[98] The natural gas trade association Eurogas is a crucial lobbying player at the EU. Eurogas represents the gas sector interests at the EU institutions and, as such, participates in the Madrid Gas Regulatory Forum, the Gas Coordination Group, the Citizens Energy Forum and other stakeholder groups. *Eurogas*: www.eurogas.org.

[99] Although, admittedly, in December 2014, with the Ukraine crisis in full swing, Gazprom and BASF canceled their multibillion dollars energy asset swap: http://www.bloomberg.com/news/articles/2014-12-18/gazprom-deal-to-swap-assets-with-basf-ends-as-relations-sour.

[100] Euractiv, Šlovak PM calls Nord Stream expansion deal 'a betrayal,' September 11, 2015.

[101] Dempsey, J. Europe's Energy Companies Go Back to Business With Russia, Carnegie Europe, September 7, 2015.

most on vertical integration in the downstream segment backed by the national legislation on hydrocarbons. This goes directly against the vision adopted by the European Commission, which is based on a competitive system regulated by its *acquis communautaire* .

On its end, the EC has developed a trilateral approach to energy security that aims to respond to the so-called triangle of competitiveness, environmental protection, and security of supplies, all of which the Commission intends to tackle simultaneously. These ambitious goals are comprised of three pillars: diversification (to address security of supply),[102] liberalization (to enhance competitiveness), and sustainable development. It is worth noting that the latter is by far the most advanced aspect of the EU's triangle. It is the policy domain where the EU has full powers.[103] The same is true for competitiveness. Here the role of the DG Comp is crucial. DG Comp is one of the politically most powerful directorates of the EC, largely responsible for the energy directives packages such as the Third Energy Package. The latter requires a full divestment of the transmission networks from the vertically integrated gas and electricity companies.[104] Far-reaching unbundling of ownership (the separation of gas supply from transportation services) is the most controversial aspect of this legislation.

The transition to this new system has raised a great deal of problems for Gazprom. It puts barriers on Gazprom's movements in the EU's downstream markets by pushing for unbundling of the ownership of production and transportation capacities. It also includes a provision, the so-called 'Gazprom provision' in the 2008 Gas directive, forbidding foreign-producing companies from owning part of transit and transmission companies' stock. According to Gazprom's statements, some of the rules of the Third Energy Package could severely limit Russia's investments in Europe, directly calling into question Gazprom's business model. Putin himself has denounced this legislation because it requires Gazprom to give third-party access to its pipelines (especially South Stream), while simultaneously granting full political support and an exemption from this legislation to TAP, which aims to diversify gas supplies from sources other than Russia. Although the Third Energy Package also allows Gazprom to supply gas directly to EU customers (without the intermediation of major European utilities), the implications of this law are far more negative for its business model. The most important issue relates to the difficulty of securing markets, and thus potentially increasing the costs of its gas extraction and transportation. Many energy experts, such as Locatelli [50], Bressand [17] and De Jong (2012), have argued that the rules of the Third Energy Package, which are at the heart of the current controversy, should be reexamined with suppliers.

But most crucially, the European energy firms are united with Gazprom in resenting these measures. The Third Energy Package's complete internal liberalization, combined with stringent climate regulation and mature energy markets, forced European energy companies to adapt to the new reality, too.

In the late 2000s an increasing gap was created between the European energy security interests embodied in the Third Energy Package and the European energy companies' interests. Indeed, European companies' executives were warning against over-regulation. When formerly monopolized markets are privatized, the old monopolies generally retain a very high market share in their home market. This means that opportunities to grow through market expansion are limited and hence other growth strategies must be found [85]. Moreover, the European market has reached the maturity stage (i.e., growth rates have declined), which leaves the EU energy companies with two basic growth opportunities.

The first one is growing in new markets, in other words, becoming European, rather than national, companies. Cross-border expansion of these firms (together with broadening the scope of products) is often the answer to these dilemmas. This trend has led to a number of mergers and acquisitions in the European energy landscape. First, several major companies directed their growth strategy toward the east. Enel, RWE, and E.ON in particular have focused on growth in Central and Eastern Europe and Russia. Second, the "green agenda" offers new opportunities for growth.[105] Third, concerns about security of supply and market integration offer opportunities for companies to invest in gas storage, LNG terminals, interconnectors and long distance gas corridors.

Thus, Gazprom has not been the only actor challenged by the EU's Third Energy Directive. The unbundling of production, transit, and distribution operations has been resisted by major European utilities, too. However, in contrast to external energy policy (i.e., the Southern Gas Corridor), which is still primarily inter-governmental in character, competition legislation falls under the most supranational of the EU's policy-making.

This battle with the EU's energy legislation has been one of the biggest impediments to South Stream, and one of the main challenges to Gazprom. The Russian authorities are still hoping that the EU will support the project, above all by giving South Stream Trans-European Network (TEN-E) status, which would exempt it from the rules on third-party access and the separation of gas trading from gas network operations. Gazprom is seeking the help of German, French and Italian corporate partners to achieve this. With the help of these friends, Russia hopes to lobby the European institutions to change their course. However, the German government in particular refuses to discuss certain issues directly with Moscow or Gazprom. The Russia–EU format is preferred in this domain, where the EC's direct competency is undisputed. Thus far, the EC has proved reluctant to give priority status to the Gazprom-favored pipelines, although Nabucco West, a scaled down version of Nabucco (now out of the race) had these permits. The European Commission simply does not see South Stream as a means to improve the European Union's energy security, mainly because the gas would come from Russia, already Europe's main external supplier of gas.

Moreover, on several occasions, the European Commission indicated that it had not seen any blueprint for the South Steam project, and that it was "not possible" to build pipelines without having conducted a proper environmental impact assessment, as required under EU legislation.[106] And yet, at first, save these couple of environmental permits, the final investment decision seemed to have been made. Moscow's determination was such that Gazprom had invested several billion dollars on large volumes of steel pipe and teams of engineers who were poised to start construction. Suddenly, however, Putin made an announcement that the construction of South Stream would be stopped, on December 1, 2014. Until that moment, government officials and Gazprom executives were insisting that construction on the off-

[102] That said, it must be admitted that external energy policy still remains a national– rather than EU–prerogative.

[103] In line with the general objectives of the EU's efficiency policy, the EU aims to reduce Russia's energy intensity and thereby guarantee the availability of future gas supplies to the EU ([15], p.74). In this respect, the EU has real powers and Russia is very keen to work on the issue within the EU-Russia Roadmap to 2050. For more details see http://ec.europa.eu/energy/international/russia/press_en.htm.

[104] European Commission: http://ec.europa.eu/energy/gas_electricity/legislation/legislation_en.htm, Accessed in October 2012.

[105] Renewables, energy efficiency services, nuclear power, grids, and carbon capture and storage are the major fields where investments are needed. The remarkable growth of the German ğreen industryïs illustrative of this point.

[106] See, *EU puzzled by South Stream acceleration*, Euractiv, October 30, 2012 and *EU readies 'pragmatic' answer to Putin's energy agenda*, Euractiv, December 18, 2012.

shore section of the project was due to begin within months,[107] amid European Commission's "third-party access" concerns and an anti-trust investigation.

Especially in the current situation of raising tensions at the EU-Russia level, Gazprom officials have taken great pains to remind the EU that energy security is a 'two way street,' with Putin himself meeting with European energy executives and officials to discuss possible amendments to the rules that Russia considers 'discriminatory.'[108] But Putin's unexpected decision to scrap the South Stream pipeline clearly demonstrates that the Third Energy Package is here to stay.[109] Notwithstanding the reservations of a handful of European major utilities (with the support of respective member states) and of Gazprom itself, the European regulator has demonstrated that the liberalization of the European gas market is an unstoppable process, for all market participants.

In the debate over the Third Energy Package, it is hard to disambiguate fact and opinion and doing so requires careful study. At the macro level the challenge also lies in harmonizing rules, with the underlying risk of imposing ill-fitting rules on both sides. But at the *meso* and *hidden* levels, the problems are between the EU as a regulatory entrepreneur and energy companies (both the European ones and Gazprom) that try to resist the EU-imposed rules. For example, some European countries have still not yet fully transposed the EU gas directives to their national systems. In that respect, the EU is fully within its rights to continue dismantling the national gas 'bastions' [7] and start, as it has already done, infringement proceedings against EU states, while also prosecuting EU energy companies for breach of the competition rules.

The Third Energy Package will remain the epicenter of the controversies that hamper cooperation at the macro level for the foreseeable future. But in addition to this debate, it is necessary to examine the changing contractual structures in Europe, with price renegotiations and arbitration cases, which since 2012, created enormous problems for Gazprom.

7.4. Gas Contract renegotiations

When European demand crashed post-2008, many European import companies struggled to meet their contractual minimum take-or-pay (ToP) volumes.

In 2012 the spot prices for gas at European hubs collapsed, as did spot prices for liquefied gas on world markets. Indeed, the prices for gas at European hubs fell below the oil-indexed prices for piped gas from Russia, for the first time in memory. The result was disastrous for Gazprom's customers. They were obliged by take-or-pay clauses in their contracts with Gazprom to purchase gas that they did not need at prices that were significantly above those that prevailed on the spot markets.

The impact of this tectonic change was even worse for Gazprom, because of the significance of the European gas market for its revenues, and thus it was bad for the stability of the Russian state as well. A number of European companies started demanding both reductions in contractual take-or-pay volumes, and reductions in prices. Gazprom adapted, reluctantly, to the EU's counterparts' demands to breach or amend these contracts.

In this case, the EC, which has been calling to amend these long-term contracts for decades on the grounds that they hindered free competition, with vocal support from European gas utilities. In its haste to take advantage of these events, in 2012 the EC expressed an ambition to monitor, and in the longer run negotiate, energy deals on behalf of the EU member states and other countries. If implemented, this measure would make the EC an arbiter of member states' external energy policies, which this article considers impractical and undemocratic.[110] In the frustrated words of a Gazprom representative: "*We understand that now gas contracts can be challenged or even canceled by the European Commission, an actor that has no commercial responsibility. We currently don ' t know who is our counterpart, neither whether the transfer of responsibility from the national governments to the EC has already happened. We don ' t know . . . We assume that there is still a struggle between the member states and the EC.*"[111] Be that as it may, a number of contract renegotiations and in some cases international arbitration cases occurred because the European companies tied to Gazprom's contracts were now losing money. Because their residential and industrial customers paid prices for gas that were tied to the spot prices on the hubs, these firms were losing money buying piped gas from Gazprom without any ability to pass along the price difference.

At the macro level, the contract renegotiations were seen just as another example of the EU-Russia clash in values, in which the EU vision based on a competitive market is incompatible with Russia's norms and values. In the words of a EU official: "*Gas pricing is something that Gazprom has to adapt. Russia says the EU rules discourage Gazprom from investing in pipelines and gas storage facilities while they grant others access to EU's infrastructure. Some legitimate concerns regarding investment protection will be examined. However, when operating within the EU, Gazprom and the Russian government will have to respect the EU laws.*"[112]

Yet this quite overlooks the fact that the request for the breaching of existing contracts came from the EU side, and that for forty years Russia has not been alone in promoting vertically integrated business alliances and asset swaps. These accords were concluded in collaboration with the European 'champions' such as Gaz de France, ENI and E.ON. The wave of renegotiations and the mutual discontent regarding gas prices and volumes in the last few years has slightly shaken the forty-five-years long honeymoon between Gazprom and these gas giants. Nevertheless, it would be mistaken to infer from this evidence that the European gas utilities support increasing the EC's acquiring powers over external energy policy. Core European energy companies (supported by individual member states) do not want to damage their relations with Gazprom and would rather mediate a mutually acceptable solution, as was done in the arbitration case between E.on and Gazprom.[113] The EU companies warn against the dangers of an EU that is well regulated, but "left in the cold." Despite large challenges in the European market, Gazprom and its main customers have resilient commercial ties, demonstrated by the EU companies' readiness to jointly develop pipeline projects, invest in storage capabilities, and

107 See: http://www.ft.com/intl/cms/s/0/10f5bb96-795c-11e4-a57d-00144feabdc0.html#axzz3KmoIjlwX.

108 See, Putin slams Barroso: 'You know you are wrong, you're guilty', Euractiv, December 21, 2012, updated 03 January 2013.

109 The current rift between Russia and the West that erupted over Ukraine influences all these interactions at all three levels I have been analyzing. This is undoubtedly the most dramatic crisis in Russia's relationship with the West, since the breakup of the Soviet Union. This article was at an advanced stage of production by the time the decision to abandon the South Stream pipeline was made and the readers should note that the text has not been thoroughly amended to take account of the new development. However, the basic dynamics between the *macro, meso and hidden levels* are not critically altered by such events. The only thing we can be confident of is that as *the macro level* gains prominence, due to the increasingly hostile relations between Russia and the West, some interests typically articulated at the *meso and hidden levels* may be put on hold.

110 The role of the EC is limited by the very peculiar design of the European Union, which prevents the EU from acting legitimately as a broker of the c̈ommon interestïn foreign policy. Therefore, the EU is better advised to stay in the 'soft power' vein when it comes to external energy policy.

111 Interview with the author, October 2012.

112 European Commission's DG Energy top civil servant—Interview with the author, May 2012, Brussels.

113 See: http://www.eon.com/en/media/news/press-releases/2012/7/3/eon-reaches-settlement-and-raises-group-outlook-for-2010.html.

build and operate gas-fired power plants (i.e. Gazprom and RWE's joint venture).[114] The continuation of these projects has proven that price renegotiations and the EU Commission's antitrust raids have not profoundly shaken the well-consolidated partnerships between Gazprom and these big European gas companies.[115]

As this article has shown, the European corporate sector has, until recently, favored asset swapping and bilateral relations as much as its Russian counterpart.[116] In fact, here lies the *hidden* dynamic, which deserves to be highlighted: presenting it as a dichotomy between the large system of values and interests of the EU on one side, and the Russian normative 'package' on the other, does not do justice to the multi-level ties between Russia and the EU. Therefore we need a more subtle differentiation. Until recently, the battle has been chiefly between the interests of both Gazprom and the big gas giants within the EU, and the EU's liberalization agenda. More recently, these firms having started to suffer huge losses and have partially changed their view, but have not repudiated long-term contracts as such.[117] With Russia, the companies want to make sure that long-term contracts are still kept as the guarantors of the EU's energy security. In the words of Jean-François Cirelli, President of natural gas trade association Eurogas, "*The vast majority of the Eurogas membership still favors long-term contracts because security of supply is the first priority for a gas company and long-term contracts are well-suited for that. But clearly the market is going to have to change towards a gradual decoupling of oil and gas prices.*"[118] In spite of the recent difficulties with gas contract renegotiations, these relationships are developing substantially. The way Gazprom and its main partners in the EU relate to each other after more than forty years of successful cooperation is through an established political discourse based on trust, which partly explains the absence of clearly defined rules. In other words, the relationships among these companies assume features of limited reciprocity, which allows them to cooperate without being locked in regulatory agreements (i.e. PCA and ECT). Thus, in Western Europe, commercial contracts did and still do constitute the only bilateral commercial framework within which commercial terms and conditions of Russian supplies to the European markets can be agreed [90].[119] In turn, European gas executives,[120] dependent on cheap Russian gas, are quick to characterize Gazprom's gas disputes with Ukraine as commercial ones and defend Russia's record as a reliable supplier.

In fact, there is a strong path dependency in relations at the company level, which is hard (and costly) to leave [24]. One good example of this is the cooperation and asset swap that the German giant BASF finalized with Gazprom in November 2012, amid the EU's antitrust probes against Gazprom.[121] Indeed, highly relevant to Gazprom's price renegotiations and arbitrations – although not directly connected with them – is DG Comp's investigation into Gazprom's sales to eight Central and East European countries (for suspected anti-competitive behavior, including over-charging customers and blocking rival suppliers). At first, in September 2012, *at the macro level* Russia reacted particularly irritably to the European Commission's antitrust probes. A decree signed by president Putin blocked "strategic" firms from co-operating with foreign investigations without government permission.[122] But at the same time, *at the hidden level*, Gazprom has been trying to settle the case by putting forward concessions since then. It has, however, resisted regulatory pressure to change its pricing practices in Eastern Europe, which is the main concern of the EU regulators.

At this writing, a growing discord and tension characterizes the most interdependent dimension of EU–Russian relations. Energy relations are imbued with emotional and political considerations that defy economic logic. In the years to come, European and Russian interests are destined to clash even more at the *macro* level, resulting in a relaxing of the EU and Russia's interdependence and, by consequence, an even more fragmented institutional landscape between the two blocs. The increasingly hybrid pricing model, featuring both oil indexation and 'spot' pricing, has been accompanied by largely uncertain governance structures. Both policy-makers and businesses will find it challenging to skillfully navigate in this increasingly hybrid, fragmented Eurasian gas market environment, caught between state *dirigisme* and market liberalism [25]. Such a regional gas market environment will, nonetheless, be dominated by policy outcomes driven by corporate actors, as the recent Nord Stream expansion deal and the revival of a lucrative asset swap between Gazprom and Wintershall demonstrate.

8. Conclusions

The two related questions of this study are: Why, given the high degree of mutual dependency, has there been such fragmented governance architecture between Russia and the EU? More specifically, why do the EU and Russia lack legally binding instruments to govern their energy relationship? The absence of a core shared governance architecture devolved into a system where several rival poles push for their preferred practices (on issues such as investment, gas pricing, and gas transit). Each pole has its strategic partners, special relationships, and economic and political realms of influence. In such a fragmented system of relationships, energy companies are the most powerful actors. They exert decisive influence on the EU-Russia governance architecture. The recent Ukraine crisis and its destabilizing energy-related ramifications—the most severe since the EU–Russia energy dialogue was established—are an especially stark demonstration of the tensions and contradictions built into the system. The empirical analysis, however, was based

[114] Financial Times, R̈WE extends joint venture talks with Gazprom, October 6, 2011.
[115] For a more detailed discussion on this topic see: Riley, A. Commission v. Gazprom: The antitrust clash of the decade? CEPS Policy Brief, No. 285, 31 October 2012.
[116] See, for instance, the very recent controversial asset swap between Gazprom and the German chemical company BASF in November 2012, despite the rules of the EU's Third Energy Package. For more information: B̈ASF and Gazprom agree on asset swap K̈yiv Post, November 14, 2012.
[117] Traditionally, both the European companies and Gazprom have preferred the so-called Groningen model of gas trading to safeguard the needed long-term relations, which, as Gazprom is keen to point out these days, was not invented by Russia, but by the Netherlands at the beginning of the last century. Its major features are: (1) long-term contracts, with a pricing formula linking gas to oil; (2) regular price reviews (including both recalculation prices level under existing formulas, and reviews of the formula itself); (3) net-back to delivery point (which means deduction of the transportation costs); (4) minimum delivery and take obligations (take-or-pay provisions - TOP); (5) protection from price arbitrage to the detriment of the exporter (so-called d̈estination clauses)̈, [42].
[118] Ẅe need a decarbonization policy that favors gas, Interview: Jean-François Cirelli on change of the European gas industry, by Sonja van Renssen, European Energy Review, April 2012.
[119] When trading with relatively politically vulnerable states, such as the western CIS countries, Russia had tried to supplement the commercial contracts by intergovernmental long-term agreements, which would guarantee necessary gas supplies for consumers and a return of investments for the producers. On the contrary, the commercial contracts between the consumers in Western Europe and Gazprom were not underpinned by these political clauses.
[120] See for example former ENI's CEO Scaroni, speaking in Houston: Äny commercial dispute between Ukraine and Russia can and has resulted in supply interruptions, bringing Eastern European member states to their knees. This situation is obviously sub-optimal, and there are new pipelines in the works, which aim to bring gas into Europe through alternative routes. In the southern corridor, Eni, together with Gazprom, is fully committed to the development of South Stream [. . .], https://www.eni.com/en_IT/attachments/media/news/speech_Scaroni%20.pdf, p. 4.
[121] B̈ASF and Gazprom agree on asset swapK̈yiv Post, November 14, 2012.
[122] The D̈ecree on Strategic Companiess̈tipulates that any negotiations on gas prices and the contractual terms now have to be approved by the Russian government directly. See: http://www.gazprom.com/f/posts/89/747450/gazprom-questions-eng-2011-06.pdf.

on the data detailed at length in the four case studies, in addition to the application of the conceptual framework based on three levels of analysis, starting with the identification of the main actors, a subsequent the discussion of their interests, and finally, the consequences of their interest formation on the degree of formalization of the EU–Russia energy relationship. The application of this theoretical framework has yielded to a number of findings about the centrality of the business sector, the multi-level, multi-actor, and private-public dynamics in the gas sector, and the ways these affect energy governance between the EU and Russia. A narrow focus on nation-states, that is, the *meso* level, or only on the *macro* level, would have not revealed this interlinked web of relationships.

In sum, this article finds that companies face substantial complexity within the EU market design, in which they must shape their strategies both at a national level and decide on their overall approach. Meanwhile, member states, despite their arrangements at the intergovernmental level, still zealously guard against the EU's excessive interference with their foreign policy goals. Yet in energy, governments mainly act as supporters of their own national companies, who remain the pivotal actors in defining energy policy preferences with external partners, such as Russia. In fact, in key member states (i.e., Germany, France, Italy), energy security seems to be interpreted as maximizing their respective energy companies' market-shares and corporate strategy, with a lack of a comprehensive "national" strategic vision. Just as the energy companies that they support, these governments oppose some of the EC's regulatory actions, especially the ones that result from the EU's liberalization drive. Obviously energy companies' interests and the governments' interests do not always converge, but today the main rivalry seems to be unfolding between the member states and the EC, and not between the member states and corporate actors. Since the creation of the EU, member states have consistently expressed a preference for intergovernmental over supranational policy-making in the energy field. For example, until recently, in the gas trade with Russia, the member states, together with the gas companies, opposed the DG Comp's banning of long-term contracts that for decades have been essential to infrastructure development.

In the rapidly evolving interregional gas markets, with three main regional markets with different prices, both consumer and producer countries resist being locked in to agreements that would limit their ability to look for more attractive possibilities in the medium term.[123] Gazprom does not want to be locked in to any agreement that would limit its pipeline monopoly and the possibility of buying Central Asian gas, or to export both to the European markets and the attractive Asian markets. The EU companies do not want to be locked in long-term agreements that limit their capacity to buy gas on the "spot" market. If you are a Russian supplier sitting on an excessive supply of natural gas you need security of supply to develop expensive upstream projects. Thus, you have no incentive to allow "third party access" through your pipelines. The status quo, besides tying Europe's lucrative gas market closely to Russia, allows for a gradual expansion towards the dynamic Asian gas markets. If you are an EU consumer, it is not in your interest to have in place a system obliging you to buy expensive Russian gas, especially when cheaper gas is available on the spot markets. When it comes to investment protection, my study corroborates the findings that the companies themselves are the main actors in finding strategies to mitigate risk. Large investments in pipelines are no longer the result of state-to-state agreements, but increasingly rely on firm-to-firm contracts (sometimes backed by state to state agreements).

Typically, European firms choose to mitigate the risks with measures such as joint ventures, asset swaps, diversification of supply sources and routes, and by ensuring "resilience" (with gas storage, interconnectors, etc.). Gazprom manages the demand side with a planned diversification of export markets, mergers, and acquisitions [85]. The dominant actors, i.e., the business elites, have simply no interest in being tied to a common governance system, for reasons rooted in self-interest. Most of these situations reflect 'mixed-motive games,' characterized by a combination of conflicting and complementary interests. However, this article has endeavored to demonstrate that at least at the *meso and hidden levels*, where European energy companies and Gazprom dominate, the quest for cooperation has outweighed disagreements at the *macro* level.

Today, energy markets in Europe and Eurasia are in the midst of a revolutionary transformation in practices and contract structures. These are likely to have increasing influence on the decisions that companies make. The last years' liberalization of gas contracts has shown how dynamic changes can occur in established markets, leading to changes in global patterns of supply, prices and views of energy security. Yet *at the hidden level*, in a period of transition many European gas executives highlight the advantages of being strongly linked to the government and to key gas suppliers, such as Russia. In the process, they challenge the free market model underpinning the regulators' strategies.

Indeed, in recent years, Gazprom and the European energy companies have cooperated fruitfully outside the institutional domain on a quid-pro-quo basis, such as the one made known in 2006 between ENI and Gazprom that resulted in the decision to build South Stream. To back such efforts, individual EU countries have gradually distanced themselves from support for robust multilateral governance structures, to give stronger preference to bilateral energy arrangements.

An in-depth analysis through four case studies illustrates that the main objectives in EU–Russian energy cooperation are the maximization of national welfare and private profit. Among the two, maximization of private profit is the strongest force. While these two objectives often go hand in hand, they do not always converge.[124] Nevertheless, there is an important point of convergence; both member states and energy firms oppose the idea of ceding energy sovereignty to Brussels. Companies, which are the key actors, are wary of the European Commission managing external energy policy. In fact, this article argues that if the EC wants to take a more coherent stand, it will have to rethink its role and find a good balance between *laissez-faire* and improper intervention. From the perspective adopted in this article, the relationships between the energy firms (the dominant actors on both sides of the EU-Russia interdependent energy relationship) are aimed at expanding mutually beneficial economic ties, and only secondarily at developing shared governance structures. Both sides simply prefer to retain free hands. As intelligently noted by Douglass North,

[123] There is a lively debate on the question of where institutions come from. Some theories emphasize the supply side: institutions are the imposition by foreign powers (i.e., the EU) and the adoption of imported legal norms and rules. Unsurprisingly, Russia favors this explanation. In this article the theory of institutional lock-in is added as an interesting perspective. Different societies choose different laws or social practices that reflect their needs and concerns. In a globalized world, it is challenging to come up with deep transnational governance structures that respond to the needs and concerns of all the players included, because in general actors do not want to be locked in to binding structures unless they reflect their own priorities. Furthermore, like-minded Western countries are progressively losing their ability to set the essential rules and maintain them for the entire system, due to the current process of global power rebalancing and a 'rise of the rest.'

[124] See for instance, the internal conflict between Gazprom and the Russian government over the 'dual pricing' of natural gas, which means that gas is sold at a much lower price to domestic consumers (and some CIS countries) than on the export market. Gazprom is constantly lobbying to raise these domestic prices, but the government is cautious due to its use of natural gas as a "social shock absorber."

"institutions do not emerge spontaneously to create and nurture the market but reflect the interests of those players in a position to put them in place."[125]

This article has detailed both the limits of the narrow neo-realist lens (for being too dismissive of the profit motive, which indeed drives the multi-level dynamics between the EU and Russia) and evinced the reductive explanatory power of the broad family of neo-liberal explanations (that attribute the deadlock in EU–Russian governance to the EU's inability to 'speak with one voice' and/or the unsoundness of the Putin's regime). Through different case studies, it has demonstrated that commercial considerations made by corporate actors at a hidden level are the main obstacles to binding governance frameworks. Theoretically, it responded to an analytical gap in the IR literature and a weakness in the IPE literature by taking into consideration the variety of business-government relations that prevail in international politics.

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